Housing finance in crisis: the Chilean experience

By Ramon Undarraga Montes

THERE have been major changes in Latin American housing finance systems in the 1970s and the 1980s. Such systems have suffered from high inflation and unemployment rates, and have had to operate with fixed, and artificially low, mortgage rates while paying short-term higher interest rates on deposits.

The channelling of long-term resources into housing finance has been more difficult and loans to finance house purchase have been scarcer. Investors in most countries have not been protected against inflation and funds invested in mortgage lending have not had a positive yield.

Because of high budget deficits and the heavy commitment arising from the need to service foreign debt, the public sector has been able to direct fewer resources into the long-term financing of housing.

Housing finance institutions in many countries have contributed to the problem by increasingly relying on short-term financing, diversifying and transforming their organisation structure in a way to cause a move away from the initial objective of long-term housing finance.

The situation described so far has brought about a decline in the availability of housing for lower income groups. Savings for housing have been redirected to other sectors.

Chile and Colombia are among the Latin American countries that have been able to deal most successfully with the crisis.

Chile's housing finance system

There have been seven major features of the system adopted in Chile to deal with the increasingly adverse macro economic situation—

(a) Subsidies have improved access to housing for the lower income groups where the housing problem is most concentrated.

(b) Permanent and consistent resources have been aimed at the construction and acquisition of houses and the integration of housing finance into the capital markets, with the objective of ensuring the continuity of presence of these resources in housing.

(c) Savers and investors have been stimulated and protected so as to enable them to achieve a real return by means of monetary correction.

(d) Long-term loans and funding have been matched through mortgage instruments that have an attractive real return on a well-developed secondary market.

(e) Development of the subsidiary role of the state through the granting of subsidies to correct distortions in housing accessibility. The subsidy is directed to demand principally through a grant and permits the acquirer to spend it as he wishes.

(f) Full development of the private sector, stimulating it to assume the responsibility for the whole house finance process with the state concentrating on cases of extreme poverty.

(g) Establishment of clear and permanent rules to stimulate the private sector to project itself in its housing action towards the massive production of low-cost housing, obtaining a substantial reduction in construction costs and incorporating advanced techniques, so as to make better use of resources.

These major features have permitted the development of the secondary market of mortgage instruments with the principal investors being social security funds and insurance companies. The private sector has undertaken over 70% of Chilean housing activities. The state has been able to reduce to a third the budget resources required to produce the same number of houses that it constructed when it was a producer.

The private sector

Among the major features of the role of the private sector in housing finance in Chile are—

(a) The contribution of the purchaser has been stimulated through him being granted a housing subsidy as well as through savings.

(b) The housing subsidy system has permitted access through formal financing channels of low income families with a monthly income of between $75 and $280, these families being given a free choice as to how to use the subsidy.

(c) Institutions that cater for the demand of low income sectors have been developed and strengthened substantially.

(d) The private banking sector has participated in the financing of mortgage lending through issuing readjustable mortgage bonds that are acquired by social security and insurance companies.

(e) The state facilitates the process, adapting the regulatory aspects to the needs of each special situation, to be able to achieve most efficiency and permitting the housing subsidy to be an effective instrument. ■

RAMON UNDARRAGA MONTES is president of COVIP SA in Santiago.