

Mortgage Finance in Japan: The Government Housing Loan Corporation

by Yasuko Shimizu

The housing finance system in Japan has changed in both the private and public sectors. In July 1994, the Ministry of Finance abolished interest rate regulations on housing loans. In the public sector, the government involvement has been continued with the lowest interest rate secured.

This article begins with a brief overview of the housing finance system in Japan and recent trends in the market, and then concentrates on the details regarding innovations which have recently been introduced into the Government Housing Loan Corporation (GHLC), particularly those concerning the new finance system, business practices, systems development and organizational reform.

OVERVIEW OF THE HOUSING FINANCE SYSTEM

The Japanese housing finance system is divided into two sectors: the private sector and the public one. Today, the circumstances of the housing finance system have considerably changed in both sectors. First, in the private sector, in July 1994 the Ministry of Finance abolished interest rate regulations on housing loans. This deregulation enables private financial institutions to offer their own loan conditions: fixed rates and variable rates

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based on the long- and short-term prime rates, repayment terms and maximum loan amounts. This also has resulted in strong competition among private financial institutions, which, in turn, provides consumers with a larger choice of housing loans and terms.

Meanwhile, in the public sector, the GHLC has begun to place greater importance on the quality of housing in line with the national housing policy. Barrier-free housing, high-durability housing, and energy efficient housing are eligible for the lowest interest rate—3% as of September. On the other hand, being in the public sector, GHLC loans are expected to conform with those of private institutions that have a minor share of the housing finance market.

In Japan, the total amount of new loans is approximately ¥34 trillion (US\$295 billion). As much as 55% of this is taken by the private sector and the rest of it, 45%, by the public one. In the public sector, the biggest lender is the GHLC, which shares 85% of all public sector loans (see Figure 1 and Figure 2).

The mortgages outstanding in fiscal 1996, the total outstanding housing loans, is about ¥173 trillion (US\$1.5 trillion). The ratio of the private sector to the public sector is 54% to 46%, which is almost the same as that of the new loans. At the same time, with both the new loans and the outstanding loans sharing about 40% in the market, the GHLC is considered to be the leading lender. That is to say,

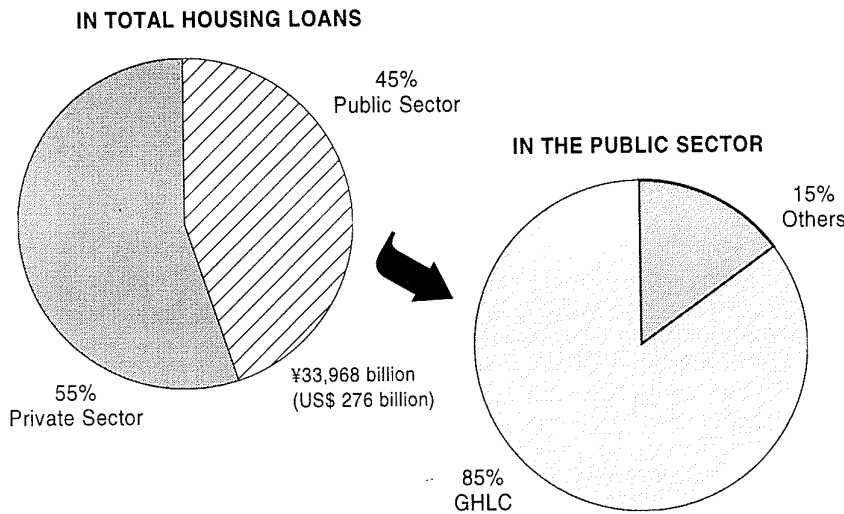
looking into the GHLC's loan system, we could see what happens to the Japanese housing finance system.

THE NEW FINANCE SYSTEM

Differing from private sector lenders, the GHLC plays a role in formulating policy targets with low interest rates, fixed rates and long terms. In June 1995 the Housing and Building Land Council, an advisory body to the Construction Minister, submitted a report illustrating the circumstances which influence housing policy. Significant among these circumstances is the fact that the so-called "aging society" is occurring at a rate even faster than predicted and that individuals are beginning to have a very diverse sense of what is desirable in a residence. More substantial development and improved investment in housing and cities is needed in order to satisfy these requirements. As a result of this report, the GHLC has reviewed its standards for housing and also its loan system.

In fact, since fiscal year 1996, the GHLC has employed a new finance system encouraging higher quality housing. A housing unit financed with the lowest interest rates must satisfy one of the following physical conditions: It must (1) be barrier-free to provide for the rising population of the elderly; (2) offer high durability so as to promote a large number of quality residences; or (3) be energy efficient and contribute to the conservation of energy and the elimination of environmental problems. Each

Figure 1. Mortgage Origination in Japan, 1996



housing type, of course, has its technical requirements (see Table 1).

In addition, for the lowest interest rate, the size of a housing unit must meet a formula. The rate being different according to a floor area, the lowest rate (3%) is applied only to a housing unit with from 80 square meters up to 175 square meters (see Figure 3).

Thus, under the new finance system, the mortgage rate would not only be appropriate to the size of the housing unit but would also raise quality standards to meet the demands of the times. So far over 60% of new owner-occupied housing financed by the GHLC has been built at the lowest rate. It could be said, consequently, that in line with the national policy, the new loan system is able to function efficiently in supplying a sufficient number of high quality housing units.

BUSINESS PRACTICES

Since entering the loan business in 1950, the GHLC has used a commission system. As business expanded over almost the entire nation, it was very difficult for the GHLC itself to carry out business with one headquarters and seven branches, and 150 employees. For this reason, private financial institutions have been commissioned to carry out the business of lending and collection. At the same time, local governments have been assigned to carry out design and on-site inspections (see Figure 4).

It can be said that the commission system is indispensable for handling the new loans for 830,000 units and for collecting payments on 6 million units, about ¥70 trillion (US\$ 600 billion) in fiscal 1996 (see Figure 5).

As of March 1997, as many as 862 private financial institutions with 19,553 service outlets and 197 local governments are cooperating with the GHLC. The GHLC now has one headquarters, 13 branches and 1,145 employees.

Figure 2. Mortgages Outstanding in Japan, 1996

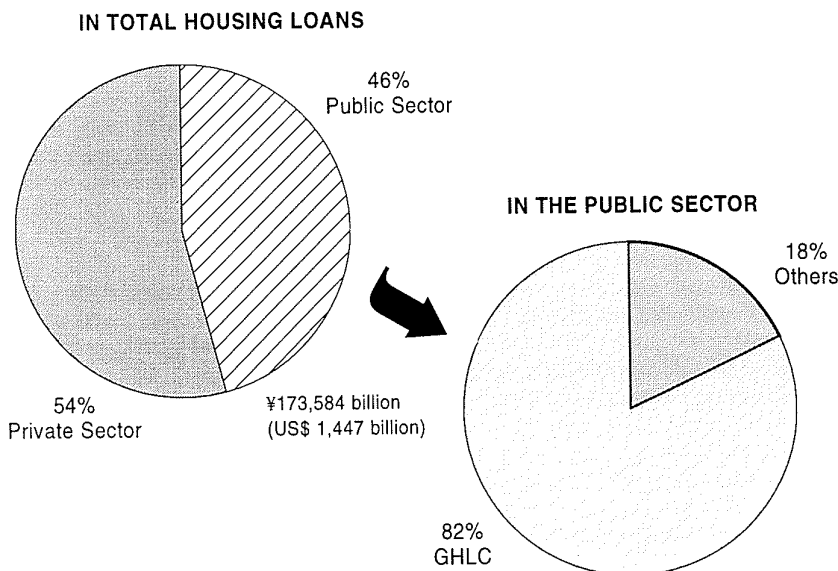


Table 1. Outline of Technical Standards

Housing Unit Type	Technical Standards
Barrier Free	<ul style="list-style-type: none"> • Elimination of difference in level • Handrails • Hallway: 780mm or over
High Durability	<ul style="list-style-type: none"> • Stronger construction materials • Measures against rot and termites • Ventilation in the roof and under the floor
Energy Saving	<ul style="list-style-type: none"> • Insulating materials for exterior walls, roof, and floor • Dual construction openings in cold districts

Figure 3. Relationship Between Rate and Floor Area

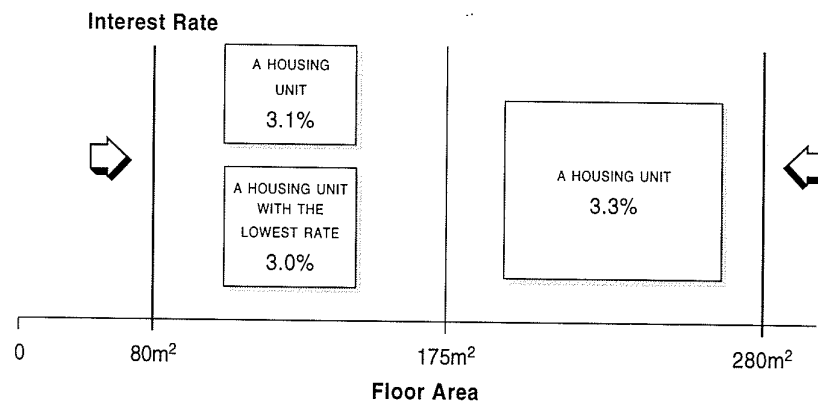


Table 2. Number of Commissioned Banks, as of March 1997

Type of Bank	Number of Banks	Number of Outlets
City Bank	10	2,649
Regional Bank	62	6,032
Shinkin Bank	400	5,417
Others	390	5,455
Total	862	19,553

Table 3. Number of Commissioned Local Governments, as of March 1997

Government	Number
Tokyo Metropolitan	1
Prefectures	45
Cities	151
Total	197

In other words, the GHLC itself is not involved directly with consumers, but the financial institutions and local governments throughout the country are (see Table 2 and Table 3).

Regarding business commissioned to financial institutions, the service outlets conduct acceptance and inspection of loan applications, the closing of contracts, delivery of loans and the collection of payments. Only the final loan decision is made by GHLC branches.

Since they are not in touch with consumers directly, the decision is made after analysis of reports from the branches of the financial institutions. Indeed, as almost all major financial institutions handle GHLC loans, consumers can conveniently use their neighborhood financial institutions in making monthly payments.

For the financial institutions and the GHLC there are, nevertheless, some problems regarding the commission system. The GHLC depends on the commission system too much to have a firm grasp on such information as the time of contract and delivery of loans. Therefore, it is impossible for the GHLC to respond immediately to consumer questions, should they contact the GHLC. Moreover, when the GHLC needs an accurate calculation for new loans, it can, without holding the ledger, only make a best estimate. In addition, the loan system is so complicated that the financial institutions can no longer bear the costs for the development of computer systems devoted only to GHLC business.

SYSTEM DEVELOPMENT

To cope with these problems the GHLC has established two types of computer systems. The Individual Loan System, after five years of development, went on-line in FY 1995 and now links the GHLC with the commissioned financial institutions. The Credit Management System uses a magnetic tape and is to go on-line by the year 2000.

Figure 4. Business Practices (Commission System)

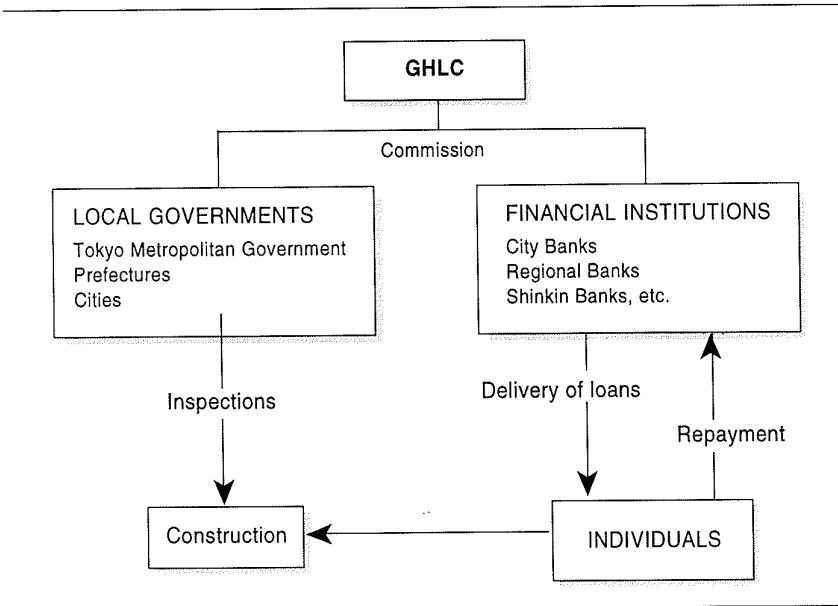
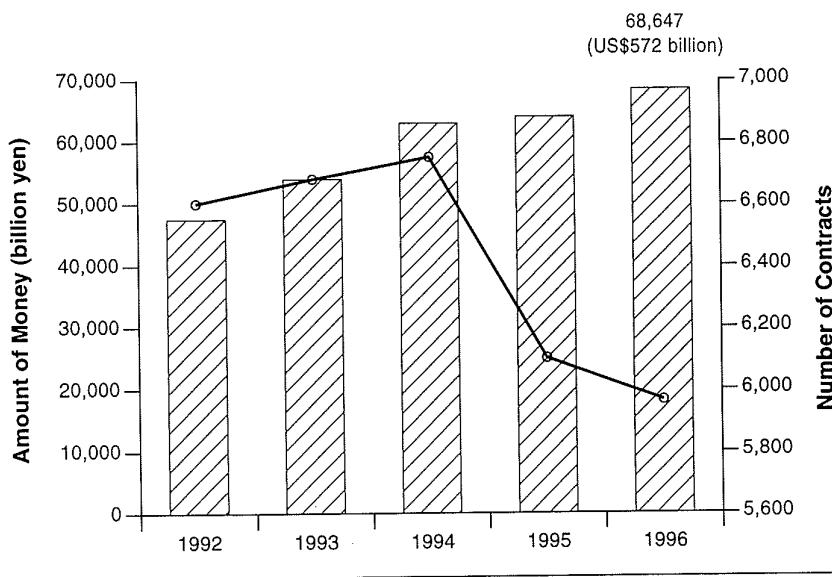


Figure 5. GHLC Mortgages Outstanding



The Individual Loan System

With data fed into the terminals of the financial institutions, the contents of application forms are screened. Whenever any of the following procedures occur or are due, the following data is to be input: (a) inspection of plans and on-site inspection, (b) registration of housing units, (c) closing of contracts, (d) mortgage registration and (e) delivery of loans. Dealing with such data in real time, documents for a loan can be automatically output at the terminals of the financial institutions. Then the completed data can be transferred to the Credit Management System (see Figure 6).

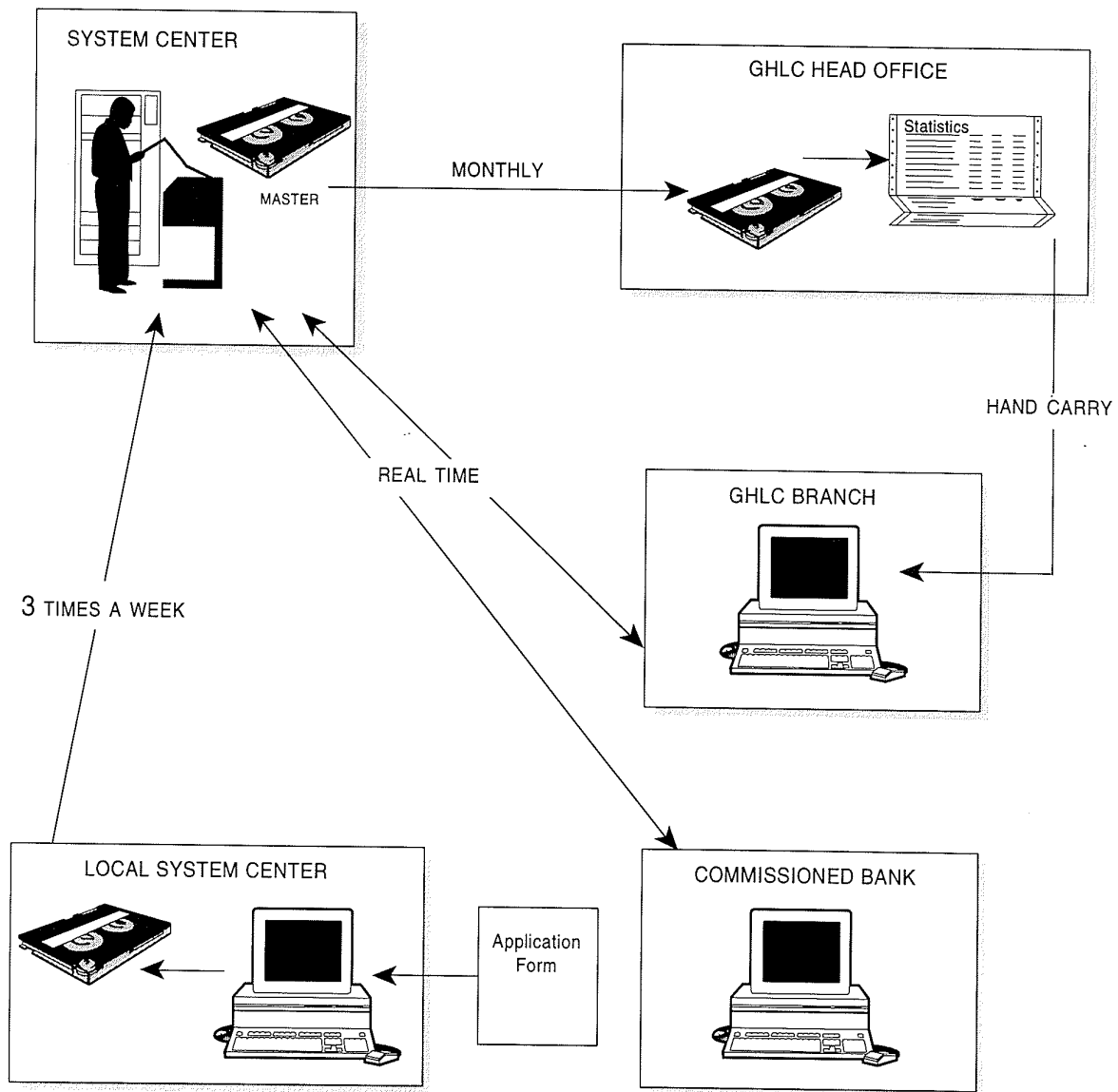
The introduction of this system has brought both advantages and disadvantages to both the financial institutions and the GHLC. Although the handling of consumers is considerably more efficient, the financial institutions are obligated to pay the costs for leasing terminals and for employees to input the data. Meanwhile, the GHLC has been able to greatly improve consumer service because of easy access to consumer information, thus making more efficient and accurate calculations for loans possible. Furthermore, based on the processed consumer information, up-to-date analyses—borrowing trends, for example—are available.

The Credit Management System

Instead of paper, magnetic tape is used for the reports on monthly repayment data from the headquarters of financial institutions to the branches of the GHLC. Now that all the data regarding 5.9 million borrowers can be controlled by the GHLC itself, GHLC branches and the headquarters of the financial institutions can easily receive information whenever needed (see Figure 7).

Two chores, outputting data from financial institution computers onto paper and inputting data into GHLC computers from paper, can be eliminated, ending the paper flood.

Figure 6. Individual Loan System



But double calculations of the total amount of loans must still be conducted by both sides. Data sent from the institutions once a month is, for the GHLC, one- to two-months old. Of course, because inquiries from various borrowers are quickly and accurately responded to, consumer service is enhanced to a certain extent. Now the development of a new Credit Management On-Line System has just begun and is scheduled for completion by the year 2000, just before Japan's expected "Big Bang" of 2001.

Regarding the plans of the new Credit Management System, the mainframe of the GHLC is expected to establish a network with related financial and insurance organizations. With the GHLC itself holding and controlling the master data, it could provide a variety of timely information and improve consumer service according to need, such as changes in repayment methods and terms. Also, daily data would be helpful in developing a new loan product swiftly. The primary function of the financial institutions might change to that of the loan recovery business (see Figure 8).

In fact, the on-line system would promote efficiency and improve consumer service of the GHLC, and the financial institutions could reduce costs in accessing data owned by the GHLC.

Above all, because the GHLC employs the commission system with private financial institutions for loans, and with local governments for the guarantee of quality housing, it is essential to introduce on-line systems into the business practices of related institutions. As with the Individual Loan System, the on-line system for the Credit Management System (instead of a magnetic tape report) is to be operative in three years.

REFORM OF THE GHLC

Among a series of reforms carried out by the GHLC, an organizational reform of the

Figure 7. Present Credit Management System

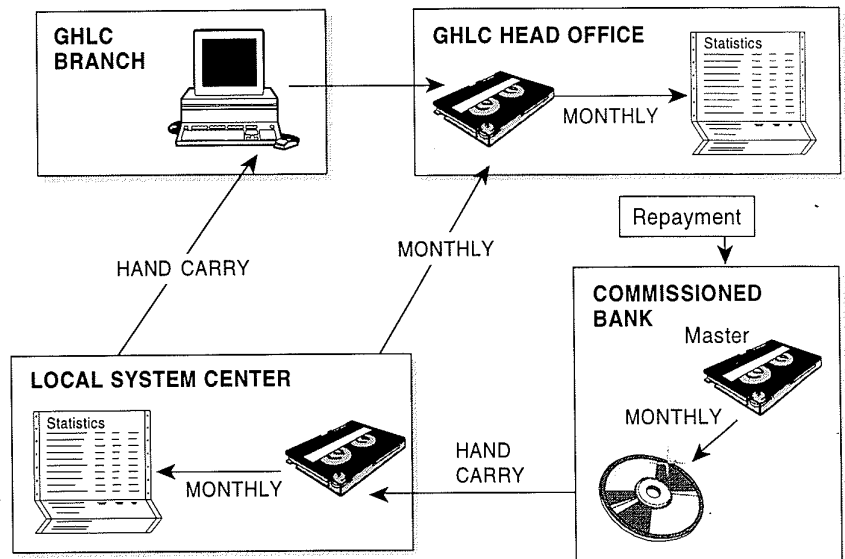
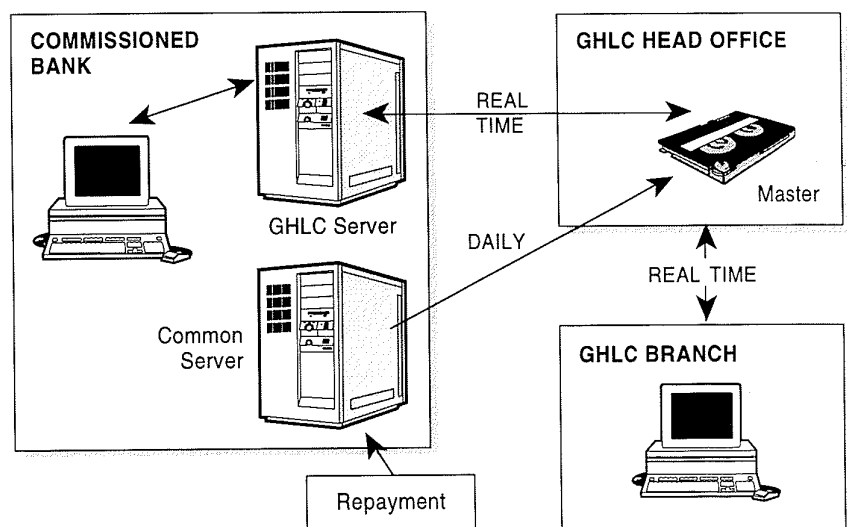


Figure 8. New Credit Management System



branches deserves special mention. In October 1996 reforms were made aiming at the improvement of services to consumers and the strengthening of cooperation with commissioned financial institutions and local governments. The reforms included two main features:

1. For loans to individuals, loan origination and loan recovery affairs are now managed by one section, not two, so that consumer queries can be dealt with more quickly. Similarly, a financial institution is now controlled by only one section. In other words, only one window of the GHLC is needed for a user to contact a branch.
2. As for loans to entrepreneurs, qualification inspections of both the project and the applicant are carried out by only one section as well. The consumer need not contact two windows anymore. In short, regarding loan origination and recovery, both affairs are now handled in one section of the branch making the way smoother for consumers.

CONCLUSION

Due to drastic changes in financial circumstances, especially Japan's so-called "Big Bang" financial reform—the complete financial liberalization—and the Administrative

Reform Council's plans for reorganizing government ministries and agencies, it is inevitable that the GHLC, as a governmental organization, comply with the demands.

Aiming at the creation of a better housing environment and the pursuit of comprehensive consumer services, the GHLC is striving for even greater innovation. In particular, high quality living led by the lowest interest rate, an on-line network system set for completion before the beginning of the next century, and changes in the organization itself could assuredly contribute to consumer satisfaction and increased efficiency of the loan business.