

Long Money or Rooted Systemic Problems?

The Prospects for Mortgage Market Development in Armenia



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It is well-known that the major target group of mortgage financing is the people who are not top earners of income. This requires that there exist a strata of population who cannot afford real estate, although the present value of such real estate is within their means. Successful functioning of the mortgage market requires a confluence of three factors: the level of income of such social strata, the market value of real estate that is affordable to this category of people, and availability of financial resources within the economy at affordable rates and terms of maturity. With this in mind, the reality of the situation in Armenian is not encouraging. The low level of transparent income among the population, the progressive growth in real estate prices, and the present volume and terms of financing offered by the Armenian financial institutions all combine to make successful functioning of the mortgage market unlikely. In layman's terms, the income of an average Armenian does not allow him or her to make mortgage payments necessary to obtain an average apartment. Mortgages are affordable to a very tiny sliver of Armenia's population.

The Constraint of Long Money

The potential constraints on the demand for mortgages are less acute of a problem than the limitations on supply of mortgage financing. Financial resources necessary for long-term mortgages are either not generated in Armenia, or are available at disproportionately low levels.

Several countries that had comparable starting points have managed dramatic achievements to alleviate the problem of supply of mortgage by engaging funds from various international financial institutions and major financial groups. Thus, the government has an important and necessary role to play, by directing its assistance and efforts to demonstrate that the mortgage, as an institution and financial instrument, has major prospects in Armenia.

The Beginning

Targeting a small category of people and dispersing a relatively small amount of funds, the mortgage market has gone through a certain development stage in recent years. The number of people who "live in a house purchased with a mortgage" is slowly growing. This is, first of all, breaking a psychological barrier. Slowly but surely a new culture that is already part and parcel of ordinary peoples' lives in the Western countries is taking root in Armenia.

The Mirroring of Deeply-Rooted Problems

Mortgage financing requires stable and transparent income.

- Few people in Armenia can boast of long-term, stable employment prospects.
- The reality, that citizens try to conceal their income and the government pretends not to notice, reduces the number of potential mortgage borrowers. It is not only necessary to have a sufficient level of income; one must also be able to prove it.

The mortgage market can develop when property rights are truly protected, contractual relations are honored, and the justice system is fully functional. These are hard-core challenges that

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hinder the development of the mortgage market, as well as of the general economic development of the country.

The mortgage mechanisms display high rates of growth only within a stable and competitive environment:

- Given the existing symbiosis between the political and business elites, any realignment of the political leadership will inevitably result in a mechanical rearrangement in the field of financial agents, which realize that and display a conservative aversion to longer-term investments.
- Even as the mortgage market is making its first steps, the competition in this area is paralleled, significantly, by rivalry between various governmental agencies which contest the right to control this new field.

What Can The Government Do?

- It can bring order to the environment to promote its development, and leave this sector to develop on its own. The first stage of the development of the mortgage market seems to demonstrate that it is able to make progress without regulatory orders.
- Direct government assistance towards securing inflow and engagement of long-term financing from foreign sources.
- Find mechanisms for creating policy incentives, in particular through adjusting the income tax policies.
- Support, by all means possible, the development of private credit rating registries and bureaus.
- Concentrate on addressing the primary challenges peculiar to the Armenian economy, such as the shadow economy, protection of property rights, stable employment opportunities, the reputation of the judicial system, low income and other issues.

Goals (or Lack Thereof)

Although the Armenian financial institutions extending mortgages formulate development programs and goals, they have to constantly adjust for the changing economic realities. It seems that mortgage, as an economic tool, is developing randomly in Armenia. It is perhaps the time to know where we are headed.

The paper is elaborated based on the opinions passed by the participants of the discussion on Prospects for Development of Mortgage Market in Armenia, which took place on February 5, 2005. The roundtable discussion was attended by independent analysts, government officials, entrepreneurs, and representatives of the international organizations.