

## **How does “path dependency” explain changes in the Eastern-European Housing Model (EEHM)?<sup>1</sup>**

Talk given at ENHR Prague conference

“Path dependency” is a popular explanation for institutional changes. In my contribution, I will focus on how much explanatory strength path dependence theory has to explain the changing nature of housing systems in the region. I will shortly touch upon the main features of the Eastern-European Housing Model (EEHM) and move on to discuss some of the critical points I have met in my endeavor to conceptualize housing systems in the region.

The main characteristics of the Eastern-European Housing model were one-party political control over the housing sector, the subordinate role of market mechanisms, no market competition among housing agencies (bureaucratic coordination), and a broad control of the allocation of housing services (huge, non-transparent subsidies). However, under this model several “sub-models” (versions) emerged; these were the responses of individual countries to particular challenges in the development process of the socialist economy. While the main characteristics of the model could be interpreted as a structural explanation, divergences were understood theoretically as “policy options” taken by individual governments. This approach is thus a “soft structuralist” method, which combines a “rational choice” (policy choice or agency choice) type of explanation with structural elements. I used this approach in a paper to explain the role of “self-help” housing in Hungary in early 1990s.

The conflict which emerged in the course of socialist industrialization and urbanization (called “cracks” in our earlier papers) led to a critical junctures with respect to the institutional development of the model. “Illegal”, informal work in private construction is a good example: because of the second economy, the income created primarily in the agricultural domain was directed towards private housing investment, which in turn needed a workforce not available legally. The uncontrolled private transactions in the public sector provide another example: they forced the system to choose among the following options: either to allow these transactions in a controlled framework, or to use tough sanctions in order to minimize the scope of the private sector. These structural conflicts (“cracks”) were managed by different methods. Bulgaria, Russia, and East-Germany introduced a strict control mechanism, while Yugoslavia and Hungary allowed quasi-market processes. Differences were explained partly by exogenous factors, like the organizational development of the party and the state, economic and social policy, and partly by the endogenous development of the housing institutions. EEHM had a core common model (centrally planned economy – politically determined power structure), which was implemented in a national context (legislation, tenure forms, regulations, etc.). For example, the rental law developed in the Second World War was used with minor changes in the 1950s in Hungary. By contrast, in Germany there was no need to nationalize the urban housing stock, because the legal framework made public use of privately owned stock possible. “Path dependency”: the legacy of the system and “accidental factors” had an effect on decisions at critical juncture points, but our explanation was based on rational choice theory, when agents choose among a limited number of alternatives given the structural constraints (political power). For example, the

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<sup>1</sup> In this contribution I use some of the results of a research conducted in the EU 7th Framework Program DEMHOW Demographic Change and Housing Wealth (Grant Agreement Number 216865).

regulation of illegal work was influenced by earlier decisions on the future role of the agriculture, when the national agriculture policy was primarily based on the production of small household farms.

20 years after the regime change in the region, we, housing researchers in these countries, should tell how the housing system changed in the region. Before we get lost in the details, it is important to clarify some basic elements of the analysis. Firstly, the term “housing model” as for us educated in the pre-transition period means basically to understand the role of state intervention in the allocation, finance and operation of the housing sector. In modern societies, housing intervention is dominated by social housing policies. Consequently, the way in which different countries organize the social housing sector plays a decisive role in shaping the housing model. *Secondly*, if social housing is a crucial element in our approach, we cannot neglect the welfare regime, as social housing programs and welfare programs are closely interrelated. (Household income benefit programs, even if they are not earmarked for housing, have a strong housing element. Then again, housing allowance programs have strong welfare effects because the allowance frees up other income.)

The famous Esping-Andersen welfare regime theory did not deal with the housing system, and attempts to integrate it into the model did not bring about any breakthrough result. The theory and its modifications were used to classify systems and enable cross-national comparison and typology, not to understand development or a process of transition. The failure of research aiming to classify the welfare regimes of transition countries gives a strong signal of the poor “practical” use of the theory. Under “practical” I mean that the theory should shed light on causal relations between features of the welfare systems and other social, economic or political factors. The term “post-communist conservative welfare system” (Deacon) does not lead far. The bad news is that we housing researchers cannot turn to existing models and simply use them for housing regimes. I tend to agree with the criticisms of the welfare system that Kasza gave, arguing that different sectors of the welfare system do not necessarily develop according to the same logic, action and development are not necessarily coordinated, etc. This does not mean that we can neglect the welfare system – quite the opposite: we have to study the different elements of the welfare system which are relevant to the housing system with particular care. Not only are housing allowances important, but also the social aspect of the taxation policy, health care regimes, etc.

Path dependence theory was popular in political science largely not because it offered a plausible explanation of the transition, but because it was useful in the criticism of its social effect. One example is the path-dependency approach of D. Stark and L. Bruszt, who argued in a 1998 study that “continuity with the past” (meaning the effect of the network developed in the socialist period) makes the transition imperfect. The other example is the use of path dependency in relation to housing privatization, where privileged social groups transformed their good position in the public sector into high capital value in the owner-occupied sector (shown in a paper by Judit Bodnár and József Böröcz). The main point of this approach was to elucidate the fact that the communist ruling class kept its position in the market system, though its explanation of the institutions’ behaviour is limited. (Actually, analyses which point to the regressive effect of privatisation did not say less than the path-dependence theory, and do not fall so easily into the trap of the conspiracy theory.) Maybe these explanations had a value in light of the events immediately following the transition, but as time passed they lost their strength.

Actually, the general trend of housing privatization in the region cannot be explained in the framework of the path-dependence theory, as it was a consequence of the endeavours of institutions and social groups dominated by short-term interest. (However, lack of restitution

in Hungary was clearly connected to the fact that the privatisation process had started before the regime change.)

The most important challenge of my research career was to give an explanation for changes in the housing systems in transitional countries. In the first part of 1990s (working closely with Iván Tosics) we were thinking in the framework of three integrating mechanisms (K. Polanyi) which could define four basic types: Western European, North American, Eastern-European, and the third world model. Well, it was an interesting conceptualization, but it did not lead too far. The weakness of the generalization of the “Eastern-European” housing finance system in “Eastern-European” cities was obvious as soon as you had to face the concrete cases (such as comparing Budapest to Bucharest). Later, working with younger colleagues at MRI (for example, Nóra Teller etc.) as Iván moved to other areas (but stayed in the same room, 1.5 m from me, provided he was in Budapest) we moved to another approach, which tried to understand the responses of the emerging societies in transitional countries to the common legacy of the socialist (housing) system. (This approach is legitimate if the challenges are the same and are connected to the socialist model. However, we knew that in the last 20 years the countries faced other challenges which cannot be connected to the socialist system, such as globalization, demographic changes and the recent economic crisis.) I am completely confident that the new housing regimes in transitional countries faced very similar challenges, namely the lack of a housing finance system, the legacy of the “housing estates”, lack of social housing and huge affordability problems. However, at a first glance, the answers are very different: in housing finance – mortgage banks, commercial banks, contract saving systems; in social housing: TBS, cooperatives, municipal housing; a wide variety of housing allowance programs and the uncertain future of housing estates. So the first theoretical question is, what, if any, are the common elements in the different countries’ responses. The second question is, after taking these developments into consideration, in what sense are these systems different from housing systems in other parts of Europe. To cut it short, my answer to the question is that the notion of a “weak state” can give a more general explanation to housing system development in Hungary, and maybe the theory can be expanded to other countries as well. But let me limit myself to the case of Hungary.

The “weak state” is a product of the premature democracies and a response to the totalitarian states of the socialist system. The emerging political parties do not share a minimum of common values and premises with respect to managing the economy and public policy. There is no common understanding of the role of the public sector in education, healthcare and housing, partly because of the socialist history, which offered “free services for everybody” on paper, but not in reality. There is no consensus among different agencies of the government (for example, responsibility for housing is divided among four ministries), but even the division of work is blurred among the different state organizations (such as the Constitutional Court or the Parliamentary Audit Office). Limited capacity to design, implement and enforce regulation is another factor of the weak state. It is not a coincidence that the wording of the interest rate subsidy enactment in 2000 was done with the help of private bank experts. The capture of the state by a private interest group is a clear sign of the weak state, which can be identified in the area of building regulations, PPP programs, and – in my view – in contract saving schemes. However, the most important consequence of the weak state is a low capacity to tax households. Tax evasion is a general phenomenon in Hungarian society, which means that 80% of total PIT revenue is paid by 20% of taxpayers.

Studying the welfare system, it is important to realize that welfare programs are crushed by the fact of “targeting failure”. Because of the difficulty to measure incomes, safety net programs (for unemployed, low income groups, family support, etc.) put the level of support

under the subsistence level, which means that households without other source of income cannot survive at a socially accepted level. However, the government would not be able to pay the adequate amount for the needy household based on official income because of the scarcity of resources. Households which have only the official low income supplemented with income benefits tend to live in deep poverty without recourse to the family network. Without help from relatives, they are unable to pay the cost of housing, and they will be forced to rely on illegal income sources (stealing, usury etc.). There has been a long, sharp debate among economists and sociologists devoted to across-the-board programs and to “targeted” programs. But this is a false debate, because without reliable measurement of income it is very difficult to move towards a more efficient, targeted system.

Development of the housing system in Hungary was conditioned by the weak state and “targeting failure”. The challenge of sociology is to explain the strategies of different institutions and social groups in the period of transition and evaluate the housing system which emerged. Path dependence, as the case of restitution in Hungary showed, is an important element in the explanation. However, “path deviation” seems to be the determining factor: new institutions emerged (for example private developers, private – foreign owned – construction companies), the function of the old institutions changed (for example banks, real estate management companies), the incentive structure and legal framework of household housing market behavior changed (for example limitation of ownership). There was no housing policy. Although governments produced white papers from time to time, actions did not follow the principles and proposed programs. Bengt Turner and Sasha Tsenkova described this situation as “scrambling through” in a paper on – if I recall correctly – Latvia. Government “housing policy” was under constant pressure from different interest groups, which led to an unstable policy. Interestingly enough, international agencies (both donor and private agencies) left their mark on the housing system. Examples are contract savings, TBS in Poland, short lived dual indexed mortgage, housing offices, non-profit housing cooperatives etc. However it would be a mistake to overestimate their effect, as the new solutions were embedded in the national-local power structure and function according to these constraints.

There is no simple conclusion to be drawn concerning the nature of the housing system in transitional countries. The concepts of “weak state”, “targeting paradigm” and the ongoing integration of these countries into Europe define the wide scope of the recently emerged housing regimes, making any generalized typology uncertain. In this sense, transitional countries are different, and not just because of the legacies I mentioned earlier, but because even global issues like ageing took place in this special context combined with a low GDP (40-60 % of the EU average). As ongoing research (DEMHOW) showed, elderly people will lean on their housing asset much more in transitional countries than in more developed EU states due to low income. In the past 20 years, the system has not moved in any single obvious direction. A substantial element of the system is hidden behind non-conclusive government papers, unreliable statistics and contradictory local processes. When will the state grow strong? When will we leave targeting paradigms behind? These remain open questions. The role of housing research is challenging: it must show how the various institutions operate, what effects they have, and it must confront politics with the consequences of housing policy (or the lack of it).

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