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Plenary II - EU Integration: Social and economic implications for housing

Housing Systems ~ Change on the Way to EU – Similarities and Differences, Integration or Convergence

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Introduction

One of the most significant aspects of European integration has been the Union's expansion eastwards to take in the new democracies of central and eastern Europe. In this paper I would like to address the problem reflected in the following questions: what were the similarities and what were the differences in reforms of housing policies, housing systems and housing finance during the transformation of economy and society of former communist countries? What was shared and where individual approaches were adopted in the transition to the market economy among countries that joined the European Union in May 2004, i.e. among Hungary, Poland, Czech Republic, Slovakia, Slovenia, Estonia, Latvia and Lithuania? Other prospective member of the EU, such as Romania, Bulgaria and Croatia, will be added to this introductory comparative analysis, where information and data are available in English.

I cannot provide an overall systemic evaluation of the whole transformation process or establish a new typology of housing systems in the time available today. The aim of the paper is much less ambitious. It is to argue that we should look beyond the superficial facts when examining housing reforms and examine the fundamental changes to these housing systems. If we are going to find any real similarities in the area of housing next to those changes that logically followed from wider economic and political transformations, then we can find them only in a hidden and implicit form, behind the explicit divergence that is typical for transformation in former communist states. I would like to show that transformation in the field of housing was especially connected with relatively large, inefficient and untargeted redistribution of substantial economic subsidies – as a result of which an “insider-outsider” situation has been created whereby existing owners and tenants enjoy legislative privileges and low housing costs, but ‘outsiders’ have been excluded from those privileges, facing either access difficulties or very high housing costs.

After the short historical overview of the situation before the collapse of the communist regimes I am going to present a brief analysis of similarities and differences in housing reforms as transition states have become more closely integrated with the rest of Europe. In particular I will examine three areas: First, the change in housing systems (especially the impact of public housing privatization); second, developments in housing subsidies; and third, reforms of housing finance. The implicit similarities behind the explicitly diverged developments in selected three fields will be examined in the concluding part of the paper.

Brief historical overview

During the previous communist (or, more precisely, socialist) system there were many similarities in housing systems among the countries of former Soviet block, but there were also significant differences due to the different foreign or economic policies followed by communistic states. There were countries that had to copy the Soviet political, economic and housing systems simply because they were involuntarily part of it (like Estonia, Latvia, Lithuania) or they followed it slavishly because they were afraid of reactions of the Big Brother (like former Czechoslovakia). There were however also countries, including former Yugoslavia, Hungary, partially also Poland and Bulgaria, that began the process of economic reform way before 1989 and this had inevitable impacts on their housing systems – mainly on tenure structure and housing finance.

Though the starting point was not identical, the basic foundations of the systems were very much shared. The most of the economy was in state ownership, the economic and political

systems were dominated by the central state, and the economy was characterized by shortages while incomes were not high enough to support a desirable living standard. In the field of housing and housing finance this meant substantial state interventions, relatively high public (mostly again state) expenditure supporting new housing construction, and strong and inefficient state rent controls (sometimes even state household mobility controls). The system encouraged the existence of common and widespread illegal (or black market) practices, clientelism and corruption during the housing construction and allocation processes.

Changes towards new future

After the collapse of the socialist regimes, most housing reforms were consequences of wider economic liberalization and political changes. The *reforms of wider economy* led to the liberalization of housing construction material prices, privatization of construction firms and the rapid introduction of a legislative framework to support the establishment of new private construction companies where salaries were liberalized. Energy prices were also liberalized, although some weaker form of price regulation was established under anti-monopoly legislation. These reforms facilitated the fast growth of the private economic sector that was supposed to replace the former public companies and public subsidies.

The *wider political change* led to the decentralization of power over housing policy from the center to the local level and this was often accompanied by the transfer of public rental housing from state to municipal ownership. Fiscal decentralization generally went much more slowly (if at all) and therefore local authorities received new powers and often also housing stock with large backlogs on maintenance, but they vainly waited for additional financial means to effectively fulfill their new role.

The field 1: Housing system change and public housing privatization

When housing policy appeared on the scene, the differences immediately became much clearer. There are substantial conceptual differences among selected transitional countries. The first housing policy changes apparent in most transition countries consisted of sharp decrease of public subsidies for housing construction as well as reductions or even complete withdrawal of all other public subsidies directed to housing maintenance. Most of the countries stopped immediately their large-scale public housing construction programs. However, in some countries like Bulgaria or Romania, even the completion of on-going construction projects became very difficult (due to high public expenditures to meet this goal) and in some others, notably Poland, the State continued, to support at least cooperative housing construction with generous subsidies until the mid 1990s.

Let me look in more detail at the tenure structure changes in selected countries between 1991 and 2001, just because the tenure structure is often taken as the main feature of housing system. From a glance at Table 1 we can see that there were many countries that completely changed their tenure structure towards homeownership. If we compare it to the GDP per capita levels, it is also clear that those countries are not definitely richer or poorer than those that did not follow this course. In other words, both relatively well developed countries like Hungary, Slovenia and Estonia, as well those countries with lower levels of wealth such as Romania, Lithuania are among those that decided to radically change the housing model in favor of homeownership. However, there were other countries, like the Czech Republic, Poland and Latvia, where public rental housing remained the important tenure even in 2001,

and Bulgaria, where the homeownership tenure was common also during communism and therefore no substantial tenure change took place.

Table 1: Tenure structure differences during the transition

Country	GDP per capita PPP (in % EU-25)	Rental housing (in % total housing stock)		Homeownership (in % total housing stock)		Other tenure (in % total housing stock)	
		around 1990	around 2000	around 1990	around 2000	around 1990	around 2000
	2004						
Slovenia	77,8	39	9	61	84	-	7
CR	70,0	40	29	38	47	21	24
Hungary	60,5	26	7	74	92	-	1
Slovakia	52,0	28	9	49	74	23	17
Estonia	49,8	60	14	34	86	5	4
Latvia	47,8	79	30	21	70	-	-
Poland	46,7	32	17	43	55	25	28
Lithuania	43,2	n.a.	7	n.a.	91	n.a.	2
Romania	31,6	22	7	76	93	1	-
Bulgaria	29,8	7	8	91	92	-	-

Source: *Housing Statistics in EU 2004, Lux (ed.) 2003*

In countries with substantial tenure changes, right-to-buy legislation has been passed (something known well from UK) and therefore tenants of public housing received generally very favorable right to buy the flat under the conditions set by central government. (Indeed in some countries, such as Estonia and Lithuania, the transfer was almost free-of-charge as a part of voucher privatization process). No matter that at that time the housing stock was often transferred to municipal ownership – it was the state that gave the public tenants the chance to gain easy access to homeownership. Even in Bulgaria the conditions of transfer were set at the central level and in Latvia the whole process was only a slightly delayed. In Poland and the Czech Republic the right-to-buy legislation was not passed and, in this sense, municipalities were respected as the full owners of housing stock. In those countries it was left to the discretion of the municipalities as to whether and under what conditions they would privatize their housing – the speed of the privatization process as well as the scale of it was therefore lower than in countries labeled as “fast privatizers.”

It became standard (though often criticized) in developed countries to divide the housing stock into three or four main segments – homeownership, private rental housing, social housing and other tenures. Using this classification can give us, however, false picture for some transitional societies. In some countries (such as Poland, Czech Republic, Slovakia) the housing cooperative sector still commands a significant share of the total housing stock. This sector is often labeled as part of social housing, but, in the Czech Republic and Slovakia, it would be more appropriate to see it as a part of homeownership sector as housing cooperative members received during the transformation significant additional rights of disposal. The private rental housing that appeared relatively quickly mainly in those countries that introduced restitution laws (so where the property expropriated by former communist regime was returned back to previous owners – like, for example, in the Czech Republic and Slovakia) often remained bound by old tenant protection rights and strong rent controls, and therefore private landlords have very limited disposal rights. The same problem arises from using the standard categorization when we look at the remaining public housing because during the former regimes the public housing was occupied by very different segments of the population. Though the housing privatization in countries named above as “fast privatizers”

changed the household structure in public housing, very few changes appeared in those countries that did not apply the right-to-buy policy (especially in Poland and the Czech Republic). Is it meaningful to call housing “social housing” if the same share of households from the lowest decile of household income distribution and the same share of households from the highest decile of income distribution occupy the municipal housing in the Czech Republic?

There are also important differences in rent control systems: while, for example, Slovakia, Estonia and Bulgaria abolished the central (state) rent control regime, in Poland and the Czech Republic the state decided to retain strong tenant protection and rent control for all current tenancies. The Czech Republic in particular became characterized by a very conservative, ineffective, untargeted, “old-styled” rent control regime. As in both countries rent control did not affect only public housing but also private rental housing created from the restitution of property, the long, painful and strong battle between the State and both private and public housing owners started. This battle exists both in Poland and the Czech Republic and has already crossed the national borders and landlords are taking the States to the Strasbourg Court for Human Rights – and the Court also decided in one Polish case in favor of the landlord.

The field 2: Housing subsidies and housing policies

If we leave public housing privatization and tenure structure aside and look more closely at new housing policy strategies, we will see that the differences between countries are again much more obvious than similarities. While some countries due to the insufficient public budgets (for example Bulgaria, Romania) and some countries due to the prevailing neo-liberal economic dogma (like Estonia) were characterized by the almost total lack of any direct housing policy (at least in the form of supply side subsidies), many other transition countries started with new supply and demand-side subsidy programs and pro-active housing policies. The countries differed not only in the fact, whether there was any new and real housing policy applied or not, but also in the forms, targeting and goals of subsidies in the countries that retained an active housing policy.

The subsidy rules are frequently subject to major change and therefore it is almost impossible to rank the countries among typical subsidy type introduced there but we can, with some caution, say that while Hungary and Slovakia concentrated mainly on direct subsidies for acquisition of owner-occupied housing (Hungary also on huge interest subsidies for market-based housing finance), Poland, partially the Czech Republic and Slovenia directed significant subsidies at the construction of rental housing. New not-for-profit housing associations with the goal to offer “social” rental housing were legally established in Poland and Slovenia and they became especially active in Poland. In contrast, in the Czech Republic the subsidies for new rental housing were allocated exclusively among the municipalities.

The field 3: Market-based housing finance

Finally, I would like to look at housing finance systems. Though there was again the common goal to establish efficient market-based housing finance system, again the means adopted to meet this objective differed significantly among countries. Table 2 shows the outstanding residential mortgage balance as a share of GDP (in 2003 - now it is higher). We may see that the role of market-based housing finance (in this case mainly housing loans) was and still is varies greatly between countries.

Table 2: Outstanding residential mortgage balance in 2003

Country	GDP per capita PPP (in % EU-25)	Outstanding residential mortgage balance on GDP (in %)	Homeownership (in % total housing stock)
	2004	2003	
Slovenia	77,8	3,5	84 (2003)
CR	70,0	4,5	47 (2001)
Hungary	60,5	7,8	90 (1996)
Slovakia	52,0	4,8	74 (2001)
Estonia	49,8	16,0*	94 (1999)
Latvia	47,8	8,3	91 (2001)
Poland	46,7	4,7	58 (2003)
Croatia	46,0	9,6	83 (2001)
Lithuania	43,2	n.a.	79 (2003)
Romania	31,6	1,0	97 (2002)
Bulgaria	29,8	0,0– 1,0	92 (2001)

* There may be some methodological differences in computation of balance though the figure was verified via the Estonian Statistical Office

Source: EMF, World Bank, Eurostat, Housing Statistics in EU 2004, UN/ECE

There were substantial differences in the solutions adopted to tackle the “tilt” problem in the first period of transition due to the high rates of inflation. The Czech Republic solved it mainly by interest subsidies (only very occasionally loans denominated in foreign currency appeared); Hungary used deferred payment mortgages alongside interest subsidies; Poland introduced and extended indexed mortgage loans (dual-index mortgage) while in other countries loans denominated in foreign currencies instead became very popular. “Exclusive” mortgage banking laws to facilitate the establishment of specialist mortgage banks have been passed in Hungary and Poland. The legislation on mortgage banking has also been introduced also in Latvia, Estonia, Czech Republic, Slovakia, Bulgaria and Romania, but in these countries the establishment of a separate specialist institution was not required. It means that universal banks can obtain the license for mortgage bond issuance so long as mortgage banking operations and assets are kept in separate legal and accounting records.

Significant differences also appeared in the field of housing-saving schemes. The Czech and Slovak Republics introduced housing-saving schemes close to the German *Bausparkassen* model in 1992. Hungary followed in 1997, Croatia in 1998, Romania in 2003 and Bulgaria in 2004. Though the law on *Bausparkassen* was passed in 1997 in Poland too, it has not been yet been applied in practice. There are many variations of the system: they differ in the premium bonus paid to savers, the minimum saving period to obtain the bonus, minimum saving period to withdraw savings, etc. While in the Czech and Slovak Republics the *Bausparkassen* are very popular among public (and expensive for the state), the opposite is true for the same system in Hungary and in Poland the system exists only on the paper. In Slovenia the National Housing Scheme was also established in 1999 but it operates within the existing banking system, interest rates on savings and loans are variable and a very low interest margin is left to meet the operational costs of banks so it is effectively a not-for-profit scheme.

Conclusions

So what, at the end, were the similarities in housing reforms on the way to the EU membership if we leave aside those that were the logical outcome of wider economic and

political reforms? What if not in the field of housing privatization (or, more generally, tenure structure change), if not in the field of housing subsidies and if not in the field of market-based housing finance? I argued in the introduction of this presentation that similarities can be identified only implicitly behind the explicit differences.

I have shown that central governments were reluctant to surrender control over the main levers that influence decisively the form of housing system. In spite of the proclaimed decentralization of policy to municipalities, central governments did not want to be compromised by the reform programs of local governments and retained the exclusive power to lead housing reforms. In this way they preserved the housing privileges for existing occupants of public housing – whether by giving them flats for “give-away” prices or by giving them low rents and generous tenant protection. Whether the reason lay in the politicians’ fear of the possible consequences of rapid change, in their quest for electoral success or even their own selfish interest (as many of them definitely lived in public housing) is an open question. Social goals that are sometimes used as an argument seem to be odd when we see the income structure of those eligible for this economic transfer and how quickly the politicians decided to deregulate energy prices (leading the sharp growth in heating and energy household expenditures) and how soft was the price regulation of the often monopolistic energy (either gas or electricity) companies that was later applied.

If I take it another step forward we would find another quite universal outcome – the “insiders” enjoyed low housing costs and tenure protection (with no regard to their social needs or income levels) while the “outsiders” were often left to the uncompromising market forces. Additional subsidies directed to outsiders (if any) were, when compared to the hidden economic subsidies to insiders, marginal. This insider-outsider tension was, in fact, even more substantial due to the fact that market housing was inflated by the lack of incentive for the “insiders” to move or rationalize housing consumption. Though this problem did not overflow into significant social conflict thanks to the traditional inter-generation transfer of housing privileges, it is obvious that the costs and benefits of housing reform were unequally distributed. This distribution did not take into account any social criteria and could even be regressive.

It is always the case with any reform – there are winners and losers. (The distribution of profits is often unfair.) However, we also know well that things that happen now often influence what happens in the distant future – we call it “path dependency”. It is therefore a question whether future housing policies in those countries will or will not be freed from the heritage of the unfair and inefficient redistribution of housing wealth, dating from the beginning of their transition to democracy and market economy.