



Housing policy and housing finance in the Czech Republic during transition

An example of the schism between the still-living past and the need of reform

Martin Lux

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Martin Lux
Prague, July 2009

1 Introduction

1.1 Meaning of ‘transition’

The intention of writing this book is to retell the story of the transition in the field of housing in the Czech Republic using the concept of housing policy efficiency and effectiveness as the language tool for the narration.¹

Along with most other European post-socialist states, the Czech Republic underwent a profound reform of its political, social and economic systems after 1990; a process which we are accustomed to calling ‘transition’. Transition is generally understood to be the temporary process of system (regime) change from a planning economy and one-party (totalitarian) government to a market-based economy functioning in a democratic framework, although, as in the West, models of governance, as well as social and economic organisation might vary.

The notion of ‘transition’ has been criticised by some commentators as ‘an implicitly unilinealist concept implying a common and clearly defined starting point (communist legacy) and end point (Western market economies)’ (Kemeny & Lowe, 1998, p. 168). The word ‘transition’ resembles the effort to imitate the systems of Western democracies and market economies by the application of some ‘cookbook of capitalism’.

“From that perspective, the road to an advanced capitalist economy is the same road, regardless of the starting point, whether that can be from Sao Paulo, Singapore or Slovenia...[T]here exists some singular yardstick against which we could measure the particular cases as differing in degree, whether that can be the intensity, speed, or level of development of the assertion of democratic impulses.” (Bruszt & Stark, 1998, pp. 11, 15).

Bruszt & Stark (1998) thus favour the term ‘transformation’ which, on the contrary, resembles the effort to *innovate* old institutions in a new economic environment and stresses the importance of path dependence, strengths of historical social norms and specific institutional patterns leading to divergence in the development. They see this process more as a ‘reconfiguration’ than the ‘replacement’ of existing institutional elements (Bruszt & Stark, 1998, p. 83). Other names for this period, used in the social science discourse, such as ‘managerial capitalism’ (Szelényi et al., 1996), ‘banking socialism’ (Večerník & Matějů, 1998) or ‘state capitalism’ (Mlčoch, 1997), all are far away from the

¹ This book summarises descriptive and analytical information on the topic of housing in transition countries gathered from various conference papers, journal articles and books that I wrote either alone or as main author, and published between 1999 and 2005. The work on this book was supported by the Grant Agency of the Czech Republic, grant No. 403/09/1915 “Social Inequalities and the Market Risks Following from Housing Consumption. The Real and Desirable Response of State Fiscal and Monetary Policies”.

ideal of market economy,² support the idea of a very gradual and path-dependent transformation process drawn by too many specific national colours to cohere in one universal post-socialist picture. The nature of housing policy reforms applied in transition countries also supports this thesis, though, as I will show, only partially.

Stated with some caution and exceptions,³ the following institutional model was shared by many socialist countries prior to 1990. Most of the economy was in state ownership, the economic and political systems were dominated by the central state and political power was in the hands of one political party. In the field of housing (housing finance) this meant relatively extensive public (mostly state) interventions to decommodify housing production, housing management and housing consumption; interventions supporting new housing construction via extensive state subsidies, influencing tenure structure through property expropriation, and controlling housing consumption through rent and price regulation (Lux *et al.*, 2002; Lux (ed.), 2003; Lowe & Tsenkova, 2003; Donner, 2006).

This specific housing system is sometimes called the East-European Housing Model (Hegedüs & Tosics, 1998) where the state controls both demand and supply sides of the housing sector and does not allow the market mechanism to develop as an integrating mechanism. After several decades of operation, however, the system that tried to make housing a pure public good lacked financial resources. It was soon characterised by unskilled housing management, bureaucracy, free-riding, low-quality construction, inefficiencies, and encouraged the existence of illegal practices, black market, clientelism and corruption (Lux *et al.*, 2003).

When socialism collapsed, the national governments freed from the dictate of Soviet power could return to or partially reflect the pre-socialist na-

2 It is necessary to point out that even in more developed post-socialist states with some pre-war tradition of democracy and market economy, the established markets were, in fact, completely new and thus had, at least at the very beginning, only little in common with mature markets in developed countries. The economic systems early after the change of regimes were, in some patterns, close to the *laissez-faire* capitalism of 19th century (due to the lack of regulation, inappropriate legal framework, lack of new democratic societal norms and recovered virtue of economic individualism) and, in some other patterns, close to corporativism (due to the fact that the first post-socialist capitalists were representatives of former communist nomenklatura who tried to preserve strong links between economic and political structures).

3 Behind the curtain of institutional unity, substantial differences between countries in the communist bloc appeared even before 1989. On the one side there were countries that had to copy the Soviet political and economic system just because they were involuntarily part of it (Baltic states) or they copied it, at least during the final two decades of Soviet hegemony, because they were afraid of inadequate reaction to any deviation from the official course (former Czechoslovakia). However, other countries had started economic reforms well before 1989 and this had important consequences for their housing systems as well (former Yugoslavia, Hungary, partially also Poland and Bulgaria).

tional traditions and specific cultural patterns, as well as come up with their unique new visions of their own ways to democracy and market economy. In the competitive environment of the global market, economic differences between countries of the former Soviet bloc quickly became apparent (*World Development Indicators*). Before 1990, such discrepancies were hidden due to inaccurate economic measurement and unequal returns from non-market based international trade within the socialist bloc.

While the goal to establish (return to) market economy and democratic political structures has been officially articulated elsewhere, the meaning of ‘democracy’ and ‘market economy’ may very well have deviated from what we know as the Western model with the appearance of an entire assortment of motives, timing and, especially, particular reform acts; such divergence was clear even in the field of housing policy.⁴ Though some international organisations, such as the World Bank, tried to impose similar housing reform strategy throughout the region, their influence weakened in time and further development fully damaged the remaining pieces of the East-European Housing Model (except for some hidden and implicitly cultural patterns; see below).

The notion of transition as a universal linear process with clear evolutionary stages is thus hardly sustainable (less due to the initial position than to its real progress). However, as this book will concentrate on reforms begun or achieved specifically in the Czech Republic or those European post-socialist states that wanted to enter the European Union and became EU members in either 2004 or 2007, we can sustain the working definition of transition as the progression from a planning economy and one-party political system to the Western type of market economy functioning with a democratic political framework. Political, economic, social and institutional reactions to the challenges presented along this way may, however, vary largely among post-socialist countries.

1.2 The goal of the book

The book describes and analyses the process of housing system establish-

⁴ Some transition states began, after a while, to subsidise mainly the construction and acquisition of owner-occupied housing (Hungary, Estonia, Lithuania, Belarus, Croatia, Romania); some transition states introduced or recovered non-trivial supply-side subsidies for construction of rental housing and routed them to municipalities (Czech Republic, Slovakia, much later also Hungary and Romania); some states instead passed non-profit housing legislation and established grant systems to encourage the construction of non-profit rental housing by private social landlords (Poland, Slovenia); and many other transition states facing financial difficulties could not do more than support housing consumption by residual and *ad hoc* subsidies (often just solving acute problems with sharply rising electricity and gas prices). Moreover, housing policy measures were very volatile, changing quickly in time.

ment (reform) in the Czech Republic during the period of transition. As the establishment (reform) process is very complex, it was necessary to target the goal of the book to some particular facts. Transition, as defined above, is mainly the process of building new (or transforming old) social institutions. Such a process is far from spontaneous; on the contrary, it is highly regulated and shaped by political power, especially by the representatives of the state. The strong role of the state is one of the prerequisites of transition though its aim might paradoxically be (and in reality was) to ultimately reduce the power of the state. Transition, at least at the very beginning, enabled the representatives of the state to come up with a new social contract or, more realistically, with a new interpretation of social and economic reality. The ideological myths of the past were abandoned and empty 'interpretation' space had to be refilled. In highly centralised post-socialist societies the representatives of the state played the decisive role in such 'meta-narratives' (Lyotard's term, 1979). The behaviour (actions, interventions) of the state in the field of housing thus forms the main research focus of my book; sometimes this type of analysis is labelled as state-centred analysis or policy analysis.

Again, the state's activities in the field of housing vary largely as the state may intervene in many fields – housing production, housing consumption, land zoning, housing finance, distribution and redistribution, allocation, location (Doling, 1997, p. 8). The transition in housing policies was connected to changes in all these fields and, moreover, with substantial decentralisation of power over housing policy from the central to local levels of public administration. Both governments and citizens of transition societies paid, however, special attention to the 'housing needs problem' or 'housing affordability problem'. Housing affordability, as one would expect, worsened during the reforms, though, as I am going to show, unequally for different groups of society. Due to the fact that such a trend could endanger public support for the whole transition project, housing affordability became the most reiterated housing issue and policy target. This has been documented, for example, by a survey conducted in six transition societies in 2002 (Lux (ed.), 2003). As Doling stated (1997), "Governments may intervene in ways that improve the lot of those who would not otherwise be able to consume housing of a reasonable size and quality, but such an outcome is a consequence of an underlying motivation to preserve the social order" (p. 10). Housing affordability is especially connected to the level and quality of housing consumption and therefore those state interventions directed at influencing housing consumption (explicit or implicit subsidies to maintain or increase housing affordability) are chosen as the main focus of my book. These interventions should not only be described but also assessed, because description alone does not allow full understanding of their impact on housing consumption or housing affordability. Simply mentioning that some type of subsidy was introduced does not show its real influence on the level and quality of housing consumption.

Separating policy in the field of housing consumption from the wider socio-economic and political context, or from parts of other policies attaching, for example, housing production, is not a valid research approach since housing is logically embedded in a wider economic and political system and housing policy activities in different fields influence one another. The fact that I focus on the problems of housing affordability and consumption, does not mean that they will be analysed outside their social and economic context or outside those state interventions that are connected, for example, more with housing production than housing consumption. On the contrary, knowledge of wider context is an important precondition for developing any serious conclusions about housing policy in the field of housing consumption or its change. Narrowing the focus (i.e., 'dependent variable') on state policies in the field of housing consumption is necessary only as a methodological device that ensures the coherence of this book and helps me to avoid the temptation to describe and evaluate 'everything' but only formally and inconsistently, as would necessarily happen. Such limitation has no effect on the variability of contextual factors (i.e., 'independent variables') used to explain the specific policies in the field of housing consumption. The description of social, economic and political contexts will thus form an important part of my book.

The analysis of the unique housing policy in the Czech Republic without relative comparison with the situations in other transition countries could result in a somewhat biased picture. Though the main goal of this book is not comparative, a partial comparative analysis of policies in the field of housing consumption in selected transitional countries will be also provided to better understand and evaluate the state policy unique to the Czech Republic.

The main goal of this book is therefore to describe, analyse and evaluate the state housing policy (state interventions, subsidies) in the field of housing consumption between 1990 and 2005 (the period of economic transition) in the Czech Republic. This will be derived from:

- description and assessment of transitional housing policy in the field of housing consumption in the Czech Republic between 1990-2005; the assessment is based on policy outcomes (performance) and in comparative context; and
- analysis of possible reasons for particular Czech transitional housing policy; by searching the possible causes both through international comparison of relevant factors influencing policy formulation as well as through analysis of particular ideologies and institutions in the Czech Republic itself.

Only a few studies have tried to explain why transitional housing policy did not follow the same pace of reform as other state policies did (see Lowe & Tsenkova, 2003; Hegedüs & Tosics, 1998); even fewer studies could make any such conclusion (evaluations) at all. The goal of my book is therefore to fill

this gap by, firstly, to evaluate housing policy during the transition and, secondly, to understand the reasons for such policy performance.

1.3 Preliminary questions

The goal of the book as stated above opens many methodological and theoretical questions. These should be addressed before the goal is finally operationalised into a set of research questions. Such preliminary questions are, as follows:

1. *How should the establishment (reform) of the particular housing system in the Czech Republic be described? What theoretical background would be useful for the description and analysis of housing systems? How have others in general narrated the establishment (reform) of housing systems?*
2. *What is the theoretical (rational) reason behind any state intervention in housing markets? What is the theoretical role of the state in the field of housing? Are state interventions justifiable in theory – why and in what fields? Are state interventions in the field of housing consumption theoretically justified? Why and in what forms?*
3. *How should state interventions in the field of housing consumption be assessed to understand their impact on housing consumption and housing affordability? What kind of assessment is appropriate to use to understand the influence of state interventions on housing consumption and affordability? What methodological device is suitable for this purpose?*
4. *What relevant international comparison of interventions in the field of housing consumption can be used to better understand the process unique to the Czech Republic? What methodological features should such international comparison necessarily hold?*

The following sections on the theoretical framework and subsections on methodological framework should help to refine the definition of the research questions provided at the end of this chapter. They serve as a necessary introduction to the problem of describing and evaluating housing systems.

1.4 Theoretical and methodological framework

The application of an appropriate theoretical framework is a prerequisite to meet the goal of this book and to answer the preliminary questions stated above. Clearly such a framework should be based on:

- theories and methodological tools related to the description of housing systems (often used in comparative housing studies);
- theories and methodological tools related to the understanding and evalu-

ation of the role of the state in housing; especially the role of the state in the field of housing consumption (often used in policy studies).

1.4.1 Theories on housing systems' development

In the following section I would like to answer the first preliminary question, namely:

1. *How should the establishment (reform) of particular housing system in the Czech Republic be described? What theoretical background would be useful for the description and analysis of housing systems? How have others in general narrated the establishment (reform) of housing systems?*

The theoretical framework used to describe, classify and understand housing systems, understand their evolution and interactions, can be found in comparative housing studies. The goal of comparative housing studies is to describe similarities and differences in the development of housing systems between regionally or culturally separate units (mostly national states) and, less often, to find the causes for the existence of such similarities or differences, and causes for the potential divergence or convergence of systems. Housing systems are therefore described and analysed in a way that allows for identification of the main factors influencing the specific and common features in their development; factors leading to processes that are shared among countries as well as unique in particular countries. Comparative studies try to understand specific national patterns in one housing system by comparing them with the patterns of other systems. It is this feature that explains why comparative housing studies might substantially help answer this first preliminary question.

1.4.1.1 Inspiration in comparative housing studies

According to Boelhouwer *et al.* (2000), since the end of the 1970s there has been a revival in international comparative housing research. Comparative information can be found in the majority of housing research papers; among the papers most often cited as methodological benchmarks are those belonging to Donisson, Ungersson (1982), Ambrose & Barlow (1986), Ball *et al.* (1988), Barlow & Duncan (1994), Boelhouwer & Van der Heijden (1992, 1993a), Kemeny (1992, 1995), Harloe (1995), McCrone & Stephens (1995), Balchin (1996), Kleinman (1996), Oxley & Smith (1996), Donner (2000, 2006) and others. They include the following types of comparative studies:

1. Useful numerical and statistical overviews (sometimes with short commentary) of large and diverse groups of nations, regions, cities, and so forth, using a standardised set of indicators with no or only a weak ambi-

tion to deal with context and underlying causes of differences, and definitely no ambition to verify a pre-formulated housing system theory (typology, development). For example, the statistics collected and provided by organisations such as UN/ECE, Eurostat, OECD, IMF, World Bank, European Central Bank, Bank for International Settlement, European Mortgage Federation, CECODHAS, IUT, publications such as *Housing Statistics in EU* (2005), Scanlon and Whitehead (2004) and many others.

2. More or less detailed descriptions and comparison of particular aspects of housing systems (or whole housing systems) within a bloc of countries (or between just two countries) with stronger emphasis on the underlying social and economic context, and with at least a weak ambition to detect factors (causes) influencing differences and similarities among selected countries – sometimes called ‘middle-level comparative studies’ (Oxley, 1999). For example, hundreds of housing comparative papers written annually in diverse languages throughout the world and including housing policy comparisons and evaluations. Often these studies are commissioned by governments for relevant intelligence on ‘how things work elsewhere’ or by international organisations to regulate or influence the development of housing systems elsewhere.
3. Scientifically sophisticated studies starting with the formulation of an appropriate theory and leading hypotheses, and providing empirical verification of theoretical arguments concerned with the detailed analysis of housing systems in a set of countries – sometimes called ‘high-level comparative studies’ (Oxley, 1999) – to which only a few research studies belong; most of these are cited above as ‘benchmark’ studies.

The studies in the third group are rare and mostly provided by researchers fully committed to comparative studies, although often not exclusively orientated to housing. They are aimed at putting forward theories on whether, how and why housing (welfare) systems differ among countries, whether they converge or diverge and what might be the causes for similarities and differences among them. With their elaborated theoretical concepts, the studies of the third group are also among those I need to use in order to find an appropriate theoretical framework for my description and analysis of housing system in the Czech Republic. Such studies are traditionally divided into following categories: convergent studies and divergent studies.

Convergent studies

Convergent studies present the view that homogenising policies is the overriding trend in the evolution of housing (welfare) systems (Milligan, 2003). Convergence theory played a key role in housing market studies until the mid-1980s (Boelhouwer & Van der Heijden, 1993a, p. 373); and they were especially connected to studies of functioning (growth) of the welfare state

(Wilensky *et al.*, 1987). Doling (1997) lists the convergent theories as those based on the conviction in 'objective historical progress' or 'natural development' in ethics (growing social conscience), in perception of human rights during the process of modernisation (from civil to social rights), in industrial development (the further industrialisation develops, the closer and more similar a welfare state becomes), or in social class formation and struggle (once all societies are free of human economic exploitation). In most of these studies the elements of determinism, historicism, and existence of 'objective' laws embedded in historical progress were present; they often drew on Marxist economic theory or were closely connected with welfare state theories (from later studies, e.g., Harloe, 1985).

An often cited convergent study is by Donnison (1967) who saw the rationale for convergence of housing policies in common economic and demographic developments in countries despite their different political and institutional differences (though economic determinism following from 'logic of industrialism' is rejected here). Donnison classified the housing systems of selected developed countries in three categories: embryonic, social and comprehensive. The classification of systems itself has connotations of evolution. As this is not particularly the goal of this book, there is no need for me to provide any further criticism of the assumptions, methodology and conclusions of these studies (see Boelhouwer & Van der Heijden, 1993a; Doling, 1997; Giddens, 1976; Kemeny, 1981, 1992; and others); such criticism became stronger when states retreated somewhat from housing policy and welfare state regimes began changing radically since mid-1980s.

Divergent studies

Studies defined as divergent contend that housing policy is shaped by very specific social, cultural, economic and political contexts and therefore there is little possibility for any future convergence in a common end. Divergent studies are more recent and may be reactions to historicism and the deterministic explanations contained in earlier convergent studies, to rupture in the 'linear' development of welfare states and ultimately the disintegration of the former Communist bloc and the intellectual shift away from Marxist theory as well as other types of deterministic theories. In the sociological theoretical (as well as methodological) debate at least, disillusionment produced by the instability of results from ambitious 'exact' social scientists (the vagueness of social 'principles' or 'historic objective laws', the sense of futility derived from the impossibility of grasping social reality in its entirety within a fully exhaustive theory) or produced by the abuse of 'objective' research results by the brutal ideologies of the 20th century meant that the social scientists' effort is increasingly aimed at 'understanding' rather than 'objective measurement' or 'prediction'.

Divergent housing studies concentrated on detailed and more comprehen-

sive understanding (description, categorisation or evaluation) of housing system formation. These studies lowered the level of abstraction and often highlighted important aspects of each housing system established (developing) in various cultural, social and economic environments. They arose from theories of corporativism and agency (Schmidt, 1989; Clapham et al., 1990; Lundqvist, 1988; Boddy, 1989), political structuralism and pluralism (Lundqvist, 1992), path dependence (Kleinman, 1996), structural functionalism and social regulation (Berry, 1999), social constructivism and ideology (Kemeny, 1992, 1995; Boelhouwer & Van der Heijden, 1992), economic individualism (Friedman, 1990), welfare state pluralism (Esping-Andersen, 1990) and others.

To quote Milligan (2003): “There is growing recognition that they are not mutually exclusive explanations and greater emphasis is being placed on accounting for both similarities and differences in housing systems.” (p. 40). Thus convergence as such is not fully rejected by a recent housing researcher (seeing, at least, some convergence in the shifts of housing policies from supply to demand-side subsidies) but the aspect of evolution has lost its ‘objective’ and ‘necessary’ status and far more attention is paid to the context.

1.4.1.2 What theoretical framework to choose?

As I am going to focus on Czech housing policy changes after 1990, that is, during a period of substantial social reforms, those theories based on a gradual evolution of systems (e.g., welfare state growth, ‘logic of industrialism’) would not give me the needed theoretical insight. Though transition in the field of housing policy (tenure, finance) basically shares a common starting point (Hegedüs & Tosics, 1998), it has not been a universal process by far (both by means and timing) and important differences among post-socialist policies have emerged (Lux et al., 2003; Donner, 2006). By admitting divergence in housing systems development and due to the fact that I am going to concentrate on policies in the field of housing consumption, I will take inspiration from the studies that are policy-orientated and, in context of housing system analysis, stress the importance (influence) of:

- ideology, social norms (Kemeny);
- traditional problem solution patterns; past receipts of today’s problems (Kleinman);
- recent social (Berry) as well as political (Lundqvist) structures.

Path dependence (present mainly in expectations, prejudices, norms and social values of ordinary people who often did not understand the meaning and goals of transition), revolution in macro-narratives, norms and ideology followed by the media and politicians (substituting the values of Marxism and collectivism with the values of liberalism and individualism) and the emergence of ‘new’ social and political institutions (new institutional links

between economic capital, bureaucracy and the political elite) will thus represent the main contextual features of transition used here to understand housing system formation (reformation) in the Czech Republic.

Here follow a few statements on the main theoretical (methodological) concepts selected for the analysis of the housing system in the Czech Republic.

Path dependence, a concept used originally in economics, refers to the tendency for solutions to problems to become locked in (through institutional setting and ideology) and difficult to change (Kleinman, 1996, p. 15). In other words, past experience, past form and content of public discourse, past policies and ideologies, past forms and behaviour of institutions and even past patterns of thinking about problems and their solutions strongly influence the present situation. Any revolutionary change is, therefore, hardly possible (and if there is some rapid social system change then it may only be formal or, if factual, it can elicit social disorder, 'contra-revolution'). As Kleinman discovered in his comparative research, despite common convergence patterns following on from European integration, economic globalisation or political shifts to neo-liberalism, there are powerful countervailing political and institutional forces in individual countries. He especially denied the notion of 'best' housing policy (and thus the ideal of convergent theories): "Trying to determine which country has the 'best' housing policy is an utterly fruitless exercise" (Kleinman, 1996, p. 16). The concept of path dependence was applied especially by Boelhouwer and Van der Heijden in their comparative studies (1993b).

The *regulation approach* is a concept closely connected to structural functionalism (studies by T. Parsons, B. Malinowski) as well as to the concept of path dependence. Its goal is to find and describe longstanding specific national patterns of housing policies reflected in specific types of social regulation. It was used by Berry (1999) who defines the type of regulation as "the set of institutional forms and processes which determines how and to what extent social reproduction is actually achieved" (p. 111). Locally specific economic factors and needs, and a limited number of publicly and ideologically accepted alternatives to meet them, may stay behind the specific type of social regulation, that is also behind a specific type of state housing interventions.

Political structuralism stresses the role that ideology and the interests of specific political parties or, more importantly, the process of political decision making itself, influenced or directed by powerful interest groups behind political structures, may have in shaping and developing state policies (studies by R. Dahl, G.W. Domhoff, N. Poulantzas and other political sociologists). Lundqvist (1992) applied this theory to housing policies and put his main emphasis on actual distribution of political power, that is on who is recently in power – whether political parties with related bureaucracy and interest groups having a market-weak position or political parties with related bureaucracy

and interest groups having a market-strong position. Market-weak parties promote non-market solutions, public interventions in the housing market while market-strong parties promote market solutions.⁵ Power relations of various agents internal or external to housing provision are uneven and locally specific.

Political structuralism is also close to the sociological concept of *social constructivism* (Berger & Luckmann, 1966) which postulates that social reality is socially constructed; such social reality includes not only such soft interpretations as ideology, norms, ethics, national 'myths' but also the such institutions as markets, money, government, police, housing. The repeated reciprocal interactions between individuals are institutionalised and in the process of such institutionalisation, meaning is embedded in a society. The meaning of social fact is thus subject to discussion, manipulation and political struggle. There is no true, 'objective' essence, neither only one right way, nor one true meaning, but the only reality is the battle of competing meanings given to social facts by the conflicting interests of particular social groups (see also studies by the postmodern sociologists Z. Baumann, J.F. Lyotard). The group in power may construct (manipulate) reality in such a way that would allow it to pursue its economic interests and, if it is in power a long time, to even capture the whole market (Mills, 1956; Bourdieu, 2005; and others).

The role of *social norms* (ideology) in housing system development (especially in tenure structure) is stressed in several studies by Kemeny. Kemeny (1981, 1991, 1995) paid attention to the wider social arrangements and ideological dispositions in various countries; and not to the economic logic or particular configuration of political power. He is thus close to social constructivism as his main emphasis is on the meanings (ideas, norms) assigned to reality rather than on reality *an sich*; according to Kemeny, however, such social norms cannot be changed by one temporal political representation and have a stable long-term character. Kemeny (1981) distinguished two general types of housing systems – home-owning and cost-rental. Using data on several industrialised countries including three case studies he concluded that there has been an important divergence between countries with prevailing social ideologies (reflected in their social policies) – whether it be collectivism or privatism. Such an ideological framework had an effect on 'political tenure strategy'. Thus governments create environments that favour one or another type of tenure and strongly influence tenure decisions of its citizens. In other words, governments set up tenure-specific subsidies directed either to homeowners or renters; the form of such subsidies is also an important aspect of policies as the subsidies might be connected to the stigmatisation of some

⁵ However, Boelhouwer and Van der Heijden (1993) challenge his theory by showing a weak correlation between the type of political party in power and housing policies in six developed European countries.

types of tenure. Kemeny (1995) then distinguished state policy models as dualist (stigmatising one type of tenure) and unitary (tenure neutral) and made a somewhat normative judgement about the causes of divergence – while a dualist model is applied to protect private and the for-profit sector, a unitary model is applied to ensure that the housing system as a whole meets general welfare goals.

1.4.2 Theories on the role of the state in the field of housing consumption

In this section I would like to address the second preliminary question, namely:

2. *What is the theoretical (rational) reason behind any state intervention in housing markets? What is the theoretical role of the state in the field of housing? Are state interventions justifiable in theory – why and in what fields? Are state interventions in the field of housing consumption theoretically justified? Why and in what forms?*

It is not possible to understand the role the state plays in the field of housing without understanding the specific phenomenon of housing itself. After this introductory section on housing specificity I will go on to discuss in the next section the theories describing the role of the ‘ideal’ state (independent, interest-free) in the field of housing.

Housing is not a simple category that can be viewed from a single perspective. On the one hand, it is one of the basic human needs and the right to adequate housing has been classified as a basic social human right in most developed countries around the world. On the other hand, housing constitutes a special type of private property, traded on the market. Although trade-offs between the social and economic aspects of housing may come into play, the purpose of both central and local housing policies lies in searching for a consensus that assures both the effective functioning of the housing market and the financial affordability of housing for all social groups in society.

1.4.2.1 Economic perspective

From a purely economic perspective, housing mainly constitutes private property because it is not available in a non-competitive manner and does not have the character of public goods.⁶ However, housing economics ob-

⁶ “A public good is a good or service that provides benefits which cannot be limited to those who directly pay for it” (Truett & Truett, 1987, p. 41).

serves the following essential differences between housing and standard market commodities (Maclennan, 1982; Fallis, 1985; Lux (ed.), 2002):

1. Housing is a heterogeneous, complex and multidimensional good. Individual houses and apartments differ in floor space, design, age, quality, standard, furnishings, tenure, size and number of additional spaces or buildings (garage, garden), location, quality of the environment, accessibility and so on. It is very difficult to measure the unit of output and the demand for housing in general because the rent paid for a small flat can be the same as for a larger family house, even under conditions of optimal distribution and market equilibrium. Therefore, housing economics introduced a theoretical construct called 'housing service'. It is assumed that in a state of equilibrium the price per housing service unit will be the same in all types of dwelling units. Households or individuals thus demand housing services rather than housing on the market.
2. Housing is a durable good and as such it becomes subject to both consumption and investment. "There are two housing markets. In one, the consumer good, housing service, is exchanged, and the price per unit of housing service is determined. In the other, the investment good, housing stock, is exchanged and the price per unit of housing stock is determined" (Fallis, 1985, p. 6). In a perfect market, the price of a housing stock unit will equal the discounted present value of housing service flows (discounted by the interest rate and depreciation). However, housing consumption and investment motives may conflict: the consumer wishes to maximise utility but the investor chooses from all the options a housing unit with a maximum net present value of expected future returns. Moreover, a household willing to acquire housing must make an important decision: to rent or to buy. By choosing to rent a dwelling, the household is participating only in the market of housing services; by choosing to buy a dwelling, the household also becomes an investor).
3. Housing is a spatially fixed good and cannot be moved from one location to another. To buy a dwelling means not only to buy a particular dwelling but also to buy the socio-economic status of a neighbourhood and the level of accessibility to the place of employment. The price per unit of homogeneous housing services varies with distance: near the centre of employment the price will be higher than farther away. The access-space trade-off model developed by Alonso (1964) explains why prices for the land production factor must decrease with the distance from the centre of employment.

Other specific features of housing include, in particular:

- High transaction costs of potential moving, that is, as finding and furnishing a new dwelling and moving involves considerable expense (not only monetary expenditure but also time and emotions invested) that do not

relate directly to the acquisition of a new dwelling. These constitute the 'transaction costs'. The market adapts to changes in household income (the income effect) very slowly, compared to potential adaptations, if the transaction costs equal zero. "Such costs may range between 5 and 10% of the total price of a house, particularly where movement entails both selling and purchase costs" (Maclennan, 1982, p. 61). Transaction costs are often so great (especially if intermediaries such as real estate agencies are included) that they, to a large extent, influence the selection of future housing itself.

- Housing is a relatively illiquid good, at least in comparison to financial assets, and at the same time a very expensive good. Therefore, people are extremely careful before they make the final decision to buy and it takes them far more time to make this decision than is the case with other consumer goods.
- It is impossible to attain perfect knowledge about the situation on the market. Neither the buyer nor the seller can acquire perfect knowledge about all the offers for various housing services in such a dispersed market. As mentioned above, housing is a heterogeneous good and to behave rationally (to make a decision) it is necessary not only to know the price of a dwelling but also the price of particular housing attributes in various regions and locations.

Due to its durability, lack of transparency (in prices), low liquidity, high transaction costs as well as high price itself, supply of housing adjusts only slowly to changes in demand; that is, in the short term the housing market is often in stage of disequilibrium. High income elasticity of housing demand, scarcity of land for new housing development and the above-mentioned low price elasticity of housing supply are all factors making housing (residential real-estate) suitable for pure, relatively safe investments; the nominal as well as real house prices follow the long-term growth trend (OECD, BIS, ECB), hedging well against inflation (Montezuma, 2004). The high level of speculation (short-term investments) can, however, increase market distortions, volatility of house prices and contribute to undesirable price bubbles on the housing market (Malpezzi & Wachter, 2002). Finally, due to the special fixity of housing, many externalities (both positive and negative) appear on the housing market.

If a market is perfectly competitive, all the participants (buyers and sellers) consider the price to be a given and assume that their individual behaviour cannot change it. In such a market, there must be a large number of sellers and buyers and none of them may control the market or a significant segment thereof. In such a case, the price equals the marginal utility of consumers and the marginal costs of producers and the market finds itself in a Pareto optimum. As Fallis postulates (1985, p. 148), even a market with a smaller

number of actors on the supply side may obtain an equilibrium price and the optimum amount of exchange, but such a market must be 'open to competition'. It must be a market where potential newcomers on the supply side may acquire complete information about its functioning, operate at the same cost and under the same production conditions as the existing producers and the entry to or the exit from the market must not be contingent upon any special costs. If the market is open to competition, even a market with only a few entities on the supply side may produce optimum output.

Although a perfect situation can never be attained, if we compare the number of players on the housing market with respect to the numbers of sellers and buyers in other markets, we will most likely come to the conclusion that on both sides of the market there is a relatively large number of players (by players I mean sellers and buyers of dwellings, not number of housing developers or construction firms; for new housing development itself the market might be characterised by oligopoly on its supply side). Even if we examine the market with owner-occupied housing separately from the market with rental housing, we will still find a great number of participants on the supply and demand sides. As Fallis states: "It is sometimes popularly asserted that a few companies own a large fraction of the rental stock. This is simply untrue – the rental stock is widely held in Canadian cities" (Fallis, 1985, p. 149). Maclellan adds: "In general, economists assume that the housing market is atomistically competitive. In the British context, assumptions of monopoly ownership have been made by political commentators or Labour Party legislators only in relation to private rental housing. Even in quite small areas of cities, the ownership of rented property is considerably dispersed and the development of new housing is also deconcentrated. Ironically, it is really only the local public authorities who are monopolists in a market sense and their monopoly may be reflected, not only in exploitative prices but also in poor practice which, in some cases, may result in some tenants paying council rents in excess of probable market rentals" (Maclellan, 1982, p. 155-6).

However, the adjustment of a housing supply on changes in housing demand, as mentioned, is slow; besides the stated factors this is also due to inelastic new housing supply (Meen, 2001, 2002). The price inelasticity of new housing supply is caused partially by state regulations (land zoning, urban planning, and building rules) but also by the specific features of housing as a good. Due to the lengthy time taken by housing construction and due to the fact that housing is so expensive, there are a number of specific business risks. This kind of activity presupposes capitally-strong developers having a good channel to banking project finance; for smaller developers the danger of a skewed investment portfolio may be too high. This leads to concentration, which may decrease housing market efficiency, become a market failure and which also be one of the reasons for supply inelasticity (Bourdieu, 2005).

Another example of market failure involves externalities. The indirect con-

sumer externalities, those following from housing stock reconstruction/regeneration and from land use, are usually considered to be the most significant ones in the housing market. Indirect consumer externality arises when the consumption of one household influences the total utility of another household's consumption indirectly, through another factor. For example, the housing consumption of one household (excessive number of people living in a flat as a result of the specific social situation of that household) may influence the crime rate in a given area (aggressive antisocial behaviour). This, in turn, may influence the total utility of housing consumption of other households. Health problems (infections), vandalism, intentional destruction and sabotage of the environment may serve as other examples.

In addition to negative externalities, there are also positive externalities on the housing market following from housing stock renovation. When purchasing or renting a dwelling, people consider not only the quality of such a dwelling but also the quality of the surroundings. If an owner invests in repairs and the renovation of his/her house, then not only the owner but also everyone else living in the neighbourhood gain from the renovation (also known as the 'neighbourhood effect'). There is a problem, though: if all owners renovated their houses, the profit would be much greater than if only one of them does. Thus owners must often consider whether or not to go ahead with renovation because they do not know whether other owners will renovate their houses too (the well-known 'prisoner's dilemma').

1.4.2.2 Social perspective

As mentioned above, housing is also perceived as a basic social need of human beings and its standard greatly influences the standard of welfare of the whole society. Housing insecurity can have far reaching consequences for the labour market, as well as for the political stability of a particular country. In view of the increased acceptance of the post-World War II concept of welfare state (a concept which is even more clearly redefined today) the right to adequate housing has become a fundamental social right in all economically developed countries and responsibility for housing provision has partially transferred from the consumer and family to public authorities and public finance.

The right to housing is a social right, and social rights constitute the third element of human rights (the other two being political and civil rights). The right to housing as a human right is formulated in a number of international documents, the oldest being the Universal Declaration on Human Rights, which the UN General Assembly adopted in December 1948. Article 25 of this document states that "Everyone has the right to a standard of living adequate for the health and well-being of himself and of his family, including food, clothing, housing and medical care and necessary social services...". Principle

4 of the Declaration on the Rights of the Child, adopted in November 1959, states that “the child shall have the right to adequate nutrition, housing, recreation and medical services...”. Part II, Article 10 of the Declaration on Social Progress and Development, adopted in December 1969, states that “the basic freedoms can be attained also by provision for all, particularly persons in low income groups and large families, of adequate housing and community services.” Article 11 of the International Covenant on Economic, Social and Cultural Rights adopted in 1966 states that “the State Parties to the present Covenant recognise the right of everyone to an adequate standard of living for himself and his family, including adequate food, clothing and housing, and to the continuous improvement of living conditions”. To support the realisation of the obligations under this international document, the UN Council for Human Rights has issued numerous recommendations, explanations and commentaries. In some countries, the right to housing was included directly in the Constitution.⁷

The right to housing is mostly understood as ensuring affordable housing (a housing price level that will ensure the fulfilment of basic needs in the field of housing, including the possibility of obtaining social support in cases when the family cannot ensure this fulfilment by its own means) and the availability of housing for disadvantaged and endangered social groups (seniors, children, physically handicapped individuals, victims of natural and other disasters, etc.). In November 1988 the UN General Assembly adopted a principal document concerning housing titled *Global Strategy for Shelter to the Year 2000* which stated: “The right to adequate housing is generally recognised by the international community. All nations without exception recognise some form of obligation in the housing sector, such as the establishment of ministries or other institutes for housing issues, allocation of funds to the housing sector and creation of housing policies, programs, and projects. All citizens of all states, including the poorest ones, have the right to expect that their governments will pay attention to their housing needs and will adopt fundamental measures leading to the protection and improvement of housing...”. Similarly, the *European Social Charter of the Council of Europe*, adopted in 1961, the revised version of which was adopted in 1996 by a number of Member States of the Council of Europe, states in Part I that “Member States adopt as the objective of their policies the attaining of conditions under which the following rights and principles will be effectively fulfilled”. Number 31 of the rights and principles states that “Every person has a right to shelter”. In Part II, Article 31 states the pledge to “adopt measures with the aim to support accessibility of housing of adequate quality in order to prevent homelessness and to imple-

⁷ Portugal has defined the right to housing in great detail, specifying that it includes accommodation of sufficient size, hygienic standard and a rent proportionate to income.

ment measures securing affordable cost of housing for those who do not have sufficient financial means”.

Housing is often termed a ‘merit good’ (term of R. A. Musgrave). Merit good is defined as a good about whose consumption society collectively believes that is inherently desirable and therefore, unlike the consumption of other goods, should be publicly supported (mainly due to such wider welfare goals as social cohesion, political stability, social integration, improving health and education). Merit good does not mean a public good. Education is another frequently mentioned example of merit good.

1.4.2.3 State as ‘rational economist’ and ‘understanding paternalist’

State housing policies challenge both the economic and social perspectives of housing and theoretically (if we assume the state is an independent interest-free actor) they are thus led by the effort to eliminate market failures and ensure that the housing market functions more efficiently, and by the effort to redistribute housing consumption or, to put it more precisely, to ensure affordable housing for all groups of households. Such housing policies form a part of general welfare state regimes directed at increasing efficiency, reduction of inequality, supporting living standards and improving social integration (Barr, 1998, p. 9-11).⁸ Although both main objectives – improving efficiency and reducing inequality in housing consumption – are far from complementary (being mostly contradictory), through their housing and other types of policies public authorities strive to eliminate monopolies and ‘internalise’ externalities following from the imperfect functioning of the market and, at the same time, they introduce various restrictions, regulations, licenses, plans and various fiscal subsidies for selected groups of households which do indeed lead to the erection of other market barriers and an even more imperfect functioning of the housing market. The double role of the state as *rational economist* and *understanding paternalist* (Lux et al., 2003) may be illustrated from the point of view of the welfare economics in Figure A.1 (Edgeworth box), shown in Appendix A (based on Barr, 1998).

The role of a public authority as *rational economist* derives in particular from the well-known definition of the economic optimum developed by Italian sociologist and economist Vilfredo Pareto. According to his theory, the market finds itself in an optimum if there is no possible allocation of goods other than the existing one (another manner of production, other legislative environment etc.) that could increase the utility of one of the participants without

⁸ In practice, there may be wider welfare goals for state intervention in the housing market, such as improving health or education, using housing as one of the tools to do so.

decreasing the utility of the other participants. If the situation on the market precludes any public inference that could increase the utility of one without decreasing the utility of another, we talk about a Pareto optimum (also the highest economic efficiency). If, on the other hand, the total utility could increase without decreasing the utility of any of the actors, then the process of 'improvement' is called optimisation, a 'Pareto improvement'. Such improvement involves, for example, the elimination of monopolies from the housing market or ensuring greater information dissemination among actors entering the market, that is, interventions leading to the elimination of market failures.

Public entities, however, also enter the housing market as *understanding paternalists* and come with a certain (diverged) concepts of a welfare state. It is clear that the scope and type of public interventions depend largely upon which type of welfare concept the particular administration favours. In the case of libertarians and liberals (right-wing parties) it is more likely that they will consider housing to be primarily a private issue and will leave responsibility for ensuring their housing to the individual citizen or his/her family. In the case of socialists and communists, on the other hand, it is more likely that they will consider housing to be a public matter and therefore the responsibility for ensuring housing will be placed on the shoulders of the state, municipalities, and public institutions. (The potential conduct of a public authority 'headed' by libertarians, utilitarians, egalitarians, and socialists is briefly outlined also in the Appendix A, based on Barr, 1998.)

A majority of the politicians will most likely consider housing to be both a public and private matter and therefore in all developed Western countries (even very liberal ones) we find housing policies aimed at ensuring greater equality in housing consumption (i.e., we find the state in the role of the *understanding paternalist*). The dual role of the state as *understanding paternalist* and *rational economist* may be rewritten into policies towards the (economic) efficiency of market functioning on the one hand, and towards the (social) effectiveness (equity) in market distribution of housing services on the other. Ensuring the efficiency of market functioning rests in the elimination of market barriers, in Pareto optimisation; ensuring effectiveness (equity) rests in the redistribution of housing consumption. A 'trade off' situation commonly arises between efficiency and equity (Barr, 1998, p. 11). Barr concludes that while "the efficiency aim is common to all theories of society ... redistributive goals depend crucially on which definition of social justice is chosen" (1998, p. 69).

1.4.2.4 Why do states intervene as 'understanding paternalists'?

In addition to the wide range of sociological system theories explaining the role of the state interventions in the field of housing,⁹ several social justice theories based on abstract assumptions of classic rationalism and rational choice (independent state) explain why public authorities behave not only as rational economists, eliminating market failures and externalities, but also as understanding paternalists. According to Downs (1957, in Barr, 1998), 'the poor', acting either on behalf of themselves or in a coalition, take advantage of their right to vote to increase their wealth through wealth redistribution. According to Tullock's (1970) presuppositions of rational choice, politicians behave selfishly and with the expectation of expanding their power, status, or income, they strive to maximise the number of potential electoral votes for themselves in the next elections. And because income distribution is mostly pyramidal (relatively few people with high incomes but many people with low incomes), politicians maximise the number of electoral votes by supporting the redistribution from the wealthy to the poor (theory of coerced redistribution). Total property equality will not occur only because:

- there is a certain fear among politicians of the consequences of complete property equality on the efficiency of market functioning (e.g., nationalisation of enterprises, high taxation);
- the minority of wealthy people usually concentrate relatively great influence on social and political events (elites) and manage to defend themselves against certain pressures;
- many poor people also 'want' a certain degree of property inequality to remain since they also wish to one day become lucky enough to be wealthier and more powerful than others – they never completely relinquish this possibility.

Another is the voluntary redistribution theory proposed by Hochman & Rodgers (1969, in Barr 1998), that suggests it is in the rational interest of every wealthy person to redistribute the wealth in the direction of the 'poorer' fellow citizens and therefore wealthy people do so not under pressure from the state, but voluntarily. The theory is based on the assumption that there are always several externalities on the market (the housing market is a typical one) and therefore the consumption utility of each individual is significantly in-

⁹ Examples of such theories include historic determinism (Marxism), agency and corporativism (Schmidt, 1989; Clapham *et al.*, 1990; Lundqvist, 1988; Boddy, 1989), path dependence (Kleinman, 1996), political structuralism (Lundqvist, 1992), social constructivism or theories of prevailing ideology (Kemeny, 1992, 1995; Boelhouwer & Van der Heijden, 1992).

fluenced by the consumption of others. Thus, the consumption utility of ‘the wealthy’ is influenced by the degree or form of the consumption of ‘the poor’. Moreover, redistribution is justifiable with respect to quasi-efficiency. Let me assume that there are only two citizens, wealthy W and poor P ; in the simplest version their own utility functions (U) are influenced only by their own incomes (Y):

$$U_w = f(Y_w)$$

$$U_p = f(Y_p)$$

Now let me assume that the amount of the utility of the wealthy citizen will depend not only on his own income but also on the income of the poor citizen:

$$U_w = f(Y_w, Y_p)$$

Then redistribution will follow from rational conduct of the wealthy citizen and will last until:

$$\frac{\delta U_w}{\delta Y_p} - \frac{\delta U_w}{\delta Y_w} > 0$$

that is, until the moment when an increase in the utility of the wealthy person’s consumption following from the increase in the poor person’s income by a unit equals the fall in the wealthy person’s utility due to a decrease in his income by the same unit as a consequence of redistribution towards the poor person (δ is the mark for partial derivation). The model is sometimes criticised, especially for neglecting the phenomenon of ‘free riders’ who always appear if there are not only two but n other people.

Rawls’s theory of justice (Rawls, 1971) became especially influential in this field. The actors in his theory follow their rational selfish interest but they are supposed to be behind a veil of ignorance, meaning they know nothing about themselves, their histories, social status, income, or expected life careers. The negotiators follow their own interests but are unable to separate themselves from others. When considering the principle of social justice the only rational consensus reached by negotiators would be to maximise the welfare of the least well-off individual (as nobody knows who it is and there is always some probability that each of them might be the least well-off). Such a conclusion leads to the imperative to redistribute the wealth till the point when complete equality is established. However, the assumption of this theory, the existence of a veil of ignorance, makes it more an abstract theory on social justice than an explanation of why redistribution of wealth actually occurs in practice.

In addition to the theory presupposing the purely rational and ‘selfish’ behaviour of social actors, sociological theories of ethics and social solidarity

also study the reasons for the redistributive aspects of public authorities' behaviour. These theories emphasise the aspects of values, emotions and norms in individual and social lives that economists tend to neglect. Regardless of in which social-economic theory the grain of truth can be found, the fact is that the redistribution of housing consumption has become the axis of housing policies in most modern states and an important part of their welfare regimes. Differences, however, appear when analysing particular housing policy instruments and power.

1.4.3 Methodology of assessment of the role of the state in the field of housing consumption

The aim of this section is to answer the third preliminary question, namely:

3. *How should state interventions in the field of housing consumption be assessed to understand their impact on housing consumption and housing affordability? What kind of assessment is appropriate to use to measure the influence of state interventions on housing consumption and affordability? What methodological device is suitable for this purpose?*

Firstly, it is necessary to describe the scale of possible state interventions in the field of housing consumption (housing subsidies and/or regulations) and then, in the second part of this section, to analyse a potential methodological device for their evaluation, assessment, and mutual comparison.

1.4.3.1 Public interventions in the field of housing consumption – hypothetical cases

In principle, there are two ways in which the (independent, interest-free, 'ideal') state as understanding paternalist can ensure greater social equality and greater financial affordability of housing for low and middle-income groups of households: cash allowances increasing the income of needy households (housing or income allowance), or a subsidy lowering the cost of housing (operation and capital subsidies, rent regulation). With respect to the efficiency of both types of redistribution (defined here as optimal total consumption utility) it appears that the cash allowance is more efficient than an allowance aimed at decreasing the costs of housing. This comparison is shown in Figure A.2 of Appendix A which captures the impact of both types of state intervention on a housing consumption utility of needy households.

In reality, however, the situation may not be quite so simple. This case captures a situation where one household chooses between two types of goods – in practice there are many heterogeneous households that make decisions among a wide range of goods (including work and leisure time). More-

over, the goal of wealth redistribution is usually not merely to achieve the highest possible efficiency of state intervention but also to achieve greater effectiveness of the intervention, that is, the means allocated for increasing housing consumption must actually be used for housing by those in need. For the state as understanding paternalist effectiveness is often more important than efficiency and therefore we can imagine a situation where the state opts for a less efficient solution but the aid really does end up where it should.

Notice, for example, that in the case of intervention directed at decreasing the cost of housing, the household in Figure A.2 would consume more units of housing services than if a cash allowance were provided, although the cash allowance would move the household to a qualitatively higher level of total consumption, a higher level of total utility. If the objective of public intervention is to increase housing consumption (e.g., improve housing conditions, assuming housing is a merit good) and not so much to increase the consumption of all other goods (to increase the living standard as such) then of the above-mentioned possibilities the public authority would tend to opt for an intervention that decreases the cost of housing. Although it is theoretically possible to prove that a decrease in the cost of housing leads to a lower total consumption utility than a direct cash allowance does, it is not necessarily the case when modelling situations with actual macro-economic conditions, including the estimated elasticity of the supply side of the housing market (i.e., risking ‘capitalisation’ of income subsidies into higher housing prices).

In reality public interventions aimed at decreasing housing costs may, for political reasons, be preferred over a cash benefit as a minimum level of housing consumption is often easier to ensure and monitor by the first type of intervention. Similarly in education it is easier to ensure that the poor receive free basic education than to pay an allowance to the poor so that they may pay for their education. In order to support this fact with a formal analysis, let me turn again to Barr (1998) to expand the argument concerning the interweaving of utility functions of the rich and the poor which I have used above. Let me assume now that the amount of the total utility (U) of wealthy citizen W is given by his income and the consumption (C) of his poor fellow citizen P . Let me also presuppose this time that the utility of the rich person is influenced by the consumption of the poor person rather than by the poor person’s income:

$$U_W = f(Y_W, C_P)$$

From the point of view of the wealthy citizen (i.e., based on his/her evaluation, his/her own values and norms), the consumption of poor citizen C_p may be broken down into ‘good’ consumption ($C_{p_{good}}$) consisting of, for example, the consumption of quality housing, and ‘bad’ consumption ($C_{p_{bad}}$) consisting of, for example, the consumption of alcohol, tobacco, etc. Thus, we would transcribe the utility function of the rich citizen in the following manner:

$$U_W = f(Y_W, C_{Pgood}, C_{Pbad})$$

If the rich citizen decides to redistribute resources toward a poorer fellow citizen, the rich citizen will naturally strive to direct the resources exclusively to good consumption, which simple cash benefit does not necessarily guarantee. In the case of a simple cash benefit, the poor citizen may support what the rich citizen may view as bad consumption, which in turn would decrease the total utility of the rich citizen. Therefore, redistribution through intervention aimed at decreasing housing costs (e.g., the support for the construction of social housing) offers the rich citizen a better guarantee that his/her money will be used for good consumption by the poor fellow citizen and thus contribute to an increase in his/her own total utility. Similarly, even the poor citizen may, under certain conditions, favour supply support over a cash allowance because he/she will perceive such a situation as less stigmatising than 'having to stand in line for social benefits'.

1.4.3.2 Public interventions in the field of housing consumption – practical cases

The following are fundamental public housing policy instruments aimed at securing greater financial affordability of housing, that is, the most common public interventions in the field of housing consumption:

1. rent policy/rent regulation (in social and/or private rental housing);
2. allocation policy for social rental housing;
3. supply-side subsidies (both capital and revenue) for social rental housing;
4. demand-side subsidies for rental housing (housing allowances);
5. subsidies to promote the affordability of owner-occupied housing (tax subsidies, interest subsidies, grants, qualified loans, housing allowances and other indirect supports for housing finance).

Social housing (representing the subsidies aimed at decreasing the cost of rental housing) and housing allowances (representing the subsidies aimed at increasing the income of needy households) form the pillars of public housing policies in the sector of rental housing in most developed countries. Similarly, the tax subsidy (called sometimes fiscal subsidy) is often the most important subsidy in the segment of owner-occupied housing. However, I must point out that there are great differences among countries (Donner, 2000): for example, housing allowance plays a marginal or even no role in countries with income-related rents applied in social housing (Belgium)¹⁰ and also in

¹⁰ Income-related rent means that the rent for a particular social dwelling is set according to the income of the eligible household that live in it.

countries like Italy or Spain; on the other hand, there are some countries with no or only few social rental flats (Greece, Spain, Portugal, Switzerland) and countries that have already substantially decreased the level of tax subsidies (UK, France, Scandinavian countries).

The next part of this section provides more details of the main practical examples of state intervention in the field of housing consumption: social rental housing, housing allowances and subsidies to promote the affordability of owner-occupied housing.

Social rental housing

The meaning of the term 'social housing' changes with cultural context. Although the term is widely used, different social policy ideological constructs, historical traditions and experiences, various routes of economic development and diverse applications of welfare state principles have altogether created too many 'national' colours to draw one universal picture. In developed Western countries, the term most often relates to rental housing (but we find exceptions in UK, Greece, Spain and probably other countries where it is also used for state-supported owner-occupied housing; or in Sweden, Germany, Netherlands or Denmark where it also relates to cooperative housing) which is rented out by public or private landlords on a non-profit basis (but in some countries, such as Germany, private landlords can obtain limited profit). The dwellings are generally built and/or operated with subsidies from public budgets to keep rents affordable for low-income households (but an increasing number of developed countries have substantially cut their supply-side subsidies, which has resulted in a substantial growth in social rent). The dwellings are allocated according to the principle of need (but in many countries social housing landlords receive large autonomy in this respect and in some countries the dwelling allocation is not limited by any ceiling or target).

The sector of social rental housing is found in almost every 'old' EU member state. It varies from 1% of housing stock in Spain up to 34% in the Netherlands. Social landlords must fulfil explicit provisions concerning the social housing operation when using a grant or preferential loan from public budgets. These provisions concern mainly the allocation system and the system of rent setting. The allocation of social flats often depends on the fulfilment of certain social criteria. In many countries, national law sets explicit income ceilings for access to the social rental sector (e.g., France) or it simply specifies target social groups (e.g., Great Britain). The Swedish concept of social housing, where neither income testing nor other examination of social needs is applied during dwelling allocation (about 20% of Swedish housing stock) is an example of a country where the social housing sector is open to all households. Rents in the rental social housing stock are regulated by special laws. They are mostly calculated on the assumption of non-profit construction and management. Although maintenance of the social housing stock was of-

ten subsidised early on (and this kind of subsidy continues in some cases up to the present), in general the rent covers all costs connected with housing ('cost rent'): operation, maintenance, administration, repairs and construction loan repayments (historic capital costs). Belgium, Portugal and Ireland use the model of income-related rent (social dwelling rent is computed according to the income of the resident household).

There are many types of social housing operators: state, municipalities, housing cooperatives, non-profit housing associations, and private investors (Boelhouwer & Van der Heijden, 1992; Donner, 2000). Wide-ranging housing reforms introduced in the 1980s and 1990s increased reliance on private capital to finance social rental housing construction and regeneration. The role of public budgets (not only in the sphere of financing) decreased and independent social landlords gained more freedom in the UK, Ireland and Netherlands (Maclennan & More, 1997).

Housing allowance

An income-tested rent/housing allowance is the second important instrument of housing and welfare policy in developed European states, again especially in the field of rental housing. With respect to housing policy, this is a demand-oriented instrument that directly influences the demand for housing. Indirectly, it may affect the supply. Increasing the disposable income of the population by providing an allowance stimulates demand based on purchasing power; the reaction to an increase in demand should be a corresponding increase in the supply. Income-tested housing allowances were implemented in the developed Western countries from the middle of the 1960s (Germany 1965) onwards, but especially during the 1970s (Great Britain 1972, France 1977) and 1980s. The basic principle of housing allowances is to provide entitled households from the rental or owner-occupied housing sectors a benefit amounting to the difference between the actual and normatively settled level of household burden by rental/housing costs, defined as the share of housing expenditures from total household income. When calculating housing allowance, three factors in particular are taken into account: household income, housing expenditures and size of household (an international comparison of different models is found, for example, in Kemp (ed.), 2007).

Social housing versus housing allowance

There is a long-standing discussion, both scientific and practical, about the comparative benefits of supply and demand-side subsidies for rental housing. The following are often-cited advantages that supply-side subsidies (social housing support) may have over demand-side subsidies (housing allowances) in the field of rental housing (Maclennan, 1982; Fallis, 1985; Barlow & Duncan, 1994; Thalmann, 2004; Ball & Harloe, 1998; Laferrère & Le Blanc, 2004; Oxley & Smith, 1996; Wilcox & Meen, 1995; Boelhouwer & Van der Heijden, 1992; Don-

ner, 2000; Haffner & Oxley, 1999; and many others):

- in some cases the state can react to expected trends or a sudden housing deficit more flexibly than the market, because market entities have to account for the relatively high risks of long-term housing construction;
- the state/municipality has the power to ensure low construction costs relatively quickly and flexibly (e.g., through subsidy policy, provision of land lots for the construction site free of charge);
- support for social housing construction directly increases the supply of dwellings in a given housing market and thus creates pressure on reduction of rents and prices;
- if housing supply elasticity is low then in the short term the market will react to the demand shock with a price increase; unlike private landlords, social landlords will not use excess demand to generate economic profit 'from insufficiency';
- in the case of social housing the crowding out effect of private investment is probably low, because the private sector is not very interested in providing standard-quality housing to relatively risky groups of consumers;
- private rental housing constituted by minor investors owning one or two dwellings for lease is not a true alternative to long-term lease agreements in social housing – there may also be institutional investors in the private market, but their interest in this field generally decreases (Thalmann, 2004; Ball & Harloe, 1998).

The following are the most-cited disadvantages of the social housing alternative:

- high likelihood of poor effectiveness in allocating social dwellings;
- high likelihood of poor efficiency in constructing social dwellings – construction costs are higher due to missing competition pressures than in a free-market situation;
- low mobility of households due to the fear of losing privileged access to the social housing sector in a new place of residence, which may have negative consequences for the labour market;
- danger of poor efficiency of the support in a long run – the eligibility to social housing, once allocated, often does not terminate once a household reaches a higher income;
- danger of creating an artificial housing shortage since in the social housing sector rent is kept lower than the market level, while housing demand, even among those who could afford market rent, is concentrated precisely in the social housing sector;
- danger of a black market in social dwellings – if the difference between market rent and controlled rent in the social housing sector is considerable, then there are only a few people who will leave social dwellings and many people will be interested in being allocated such a dwelling – if

a household no longer needs a social dwelling, it is profitable for such a household to rent such a dwelling illegally at higher than the regulated rent or to 'sell' the right to the low rent.

Demand-side subsidies may have the following advantages over the social housing alternative:

- since this is an income-tested benefit, it is in principle an efficient housing policy instrument which, at least in the short run, is cheaper for public budgets than constructing and operating social dwellings;
- unlike administrative allocation of social dwellings, a housing allowance does not restrict the entitled household's choice of where to live according to their own preferences, and thus results in greater utility of housing consumption;
- high effectiveness of support (income targeting) and great flexibility of the amount of this benefit if the social situation of a household changes;
- regardless of the danger of the poverty trap, the housing allowance supports flexibility on the labour market more than a rigid system of social housing with low rents – the allowance is a transferable benefit that can be claimed in various locations;
- within the entire area of housing policy, the housing allowance allows greater rent deregulation and re-arrangement of relations on the often distorted rental housing market (removes black market);
- a properly constructed housing allowance model stimulates households to seek adequate housing (and removes 'over-consumption' of housing).

These are the most-cited disadvantages:

- stimulating housing demand by allowance results in a rent price increase, inflation pressures, at least on a short-term horizon (Le Blanc & Laferrère, 2001);
- standard disadvantages of all means-tested social benefits such as stigmatisation, personal deprivation due to the necessity to apply at regular intervals for the benefit, often also the bureaucracy involved when completing the relevant forms;
- significant administrative costs (direct and indirect) related to the payment of the allowance (Oxley & Smith, 1996, p. 143);
- as with other benefits, the allowance with a high taper may create an anti-stimulation effect on the labour market, that is, it may lead to poverty trap;
- prioritising the allowance in combination with rent deregulation in social housing usually leads to an acceleration of the social exclusion process;
- private investments in rental housing are unstable and greatly influenced by the actual interest rate, house price appreciation and returns from alternative investments – a housing allowance can then become a very expensive instrument for maintaining the interest of private investors in the

rental housing;

- the shift away from social housing to a housing allowance and private capital does not address the issue of a growing number of homeless people, socially disadvantaged households, and income polarisation, that is, the need to give efficient help to those who sorely need it (Fitzpatrick, 1998).

Support for homeownership

Support for homeownership was especially popular in 1990s and is still very popular today. In some countries support for the acquisition of owner-occupied housing is becoming one of the main pillars of state housing policy if not of domestic policy in general. Gabriel and Rosenthal (2005) note that in the US both President Bill Clinton in 1994 and President George Bush in 2002 indicated support for owner-occupied housing to be the foundation of American housing policy:

"...Homeownership strengthens families and stabilises communities.... Today, I am requesting that you lead an effort to dramatically increase homeownership in our nation over the next six years.... Your programme should include strategies to ensure that families currently underrepresented among homeowners – particularly minority families, young families, and low-income families – can partake of the American Dream." (letter from President Clinton to the Secretary of Housing and Urban Development Henry Cisneros, on 3 November 1994, cited by Gabriel & Rosenthal (2005, p. 102)).

"The goal is that everybody who wants to own a home has got a shot at doing so. The problem is we have what we call a homeownership gap in America. Three-quarters of Anglos own their homes, and yet less than 50 percent of African Americans and Hispanics own homes. That ownership gap signals that something might be wrong in the land of plenty. And we need to do something about it." (President Bush's comments at a press conference on 18 June 2002, cited by Gabriel & Rosenthal (2005, p. 102)).

Owing one's own home is a part of the norm for American society, or at least part of its convictions and ideological assertions, usually articulated as 'the American dream'. A strong preference for homeownership is equally present in other Anglo-Saxon countries (Canada, New Zealand, Australia, United Kingdom), but it can also be seen in Belgium, and in places where the United States or the United Kingdom have had a relatively strong influence on domestic policy (Latin America, India and other Commonwealth countries); surprisingly in recent years it has also been true to a lesser extent for the Netherlands. The most recent form of grant support for acquiring owner-occupied housing in the United States is called the 'American Dream Down Payment Program'. It is said of Belgians that they are born with a 'brick in the stomach'

(Stephens, 2003, p. 1013), allegedly a result of the strong influence of the Catholic political parties. The social doctrine of the Catholic Church, expressed explicitly in several Papal encyclicals, regards homeownership not only as a guarantee of the quality of individual and family life, but also as a guarantee of social order in society (De Decker & Geurts, 2003, p. 23). In these countries owning one's own home is often the primary stimulus behind economic activity, and setbacks in this regard are accompanied by frustration.

Unlike people who rent their housing, homeowners enjoy several additional rights that are tied to ownership in general – the option to exclude all others from the consumption of housing in their flat or family home, the right to make full use of their property as they wish (including the option to lease their property or to re-mortgage it to acquire money for other consumption purposes), and the right to sell their property. The option of being able to rent and sell their property can also bring homeowners some capital gain, as is the case with other investments. In absolute values the housing expenditures of homeowners are usually higher than those of tenants, especially when they are paying off a mortgage loan, but unlike tenants outright homeowners can limit these expenditures to essential items if they find themselves in a tight financial situation. They usually have substantial wealth lodged in the house or flat they own, often the main share of their personal wealth, and for owners this provides a sense of security and stability.

People who own their housing have by definition (owing to the above-mentioned external factors and the investment nature of homeownership) an interest in maintaining good neighbourly relations and in the development of the vicinity they live in, and given that they tend to share this interest with others around them, they usually live in environments that are less anonymous and affected by criminality (DiPasquale & Glaeser, 1999; Glaeser & Sacerdote 1999). They benefit from the fact that other homeowners are willing to contribute more to the development of the local community than tenants generally are. There is a general consensus that homeowners look after their homes or flats better than tenants (Henderson & Ioannides, 1983), and that they are also more successful in the labour market (not just because they need to pay off their mortgage loan, but also because they belong to larger and more stable social networks than tenants). Homeowners are obviously far less mobile than tenants (they move less frequently) and the stability of the social structure in the neighbourhood they live is an advantage, as a large turnover of inhabitants in a certain area leads to the destruction of social networks and in extreme cases, when multiple negative factors coincide in effect, can also lead to certain pathological patterns of behaviour (vandalism, criminality, anti-social behaviour). In the United States much has been said and written about homeownership also being positively linked to the performance of children at school (Boehm & Schlottman, 1999; Aaronson 2000; Haurin et al., 2002), life satisfaction (Lam, 1985; Rossi & Weber, 1996), and better physical

and mental health of homeowners (Macintyre *et al.*, 1998).

On the other hand, considering how expensive owner-occupied housing can be, often the only means of acquiring such housing is by first obtaining a large amount of credit that is repayable over a long period of time. Thus for homeowners the risk of losing their housing if they experience a decrease in income can be much higher than it is for tenants. Credit repayment constitutes a considerably large expense and can significantly interfere with other planned consumption expenses of a household. Unlike rental housing, owner-occupied housing is a form of investment, and like any other investment it need not just to bring a profit; it can result in a loss, and this loss might be substantial and relatively long-term (Ioannides & Rosenthal, 1994; Arrondel & Lefebvre, 2001; Meyer & Wieand, 1996). House prices are highly volatile in all advanced countries and the cycles in the housing market usually last much longer than basic economic cycles tend to be (Girouard *et al.*, 2006). In addition to the standard price cycles related to the macro-economic cycles, the residential property market also experiences price bubbles. The risks connected with homeownership (price volatility and market instability) became obvious during the credit crunch and mortgage crisis of 2008.

As transaction costs associated with the purchase or sale of property are much higher, homeowners tend to be less mobile (Rohe & Stewart, 1996; Lundberg & Skedinger, 1999; Wheaton, 1990). While this brings a number of positive aspects, one negative consequence is that it makes it far more complicated for homeowners to move, which can be a problem when there is a rise in unemployment or an economic crisis. When house prices fall homeowners are often reluctant or even unable to sell their homes and move elsewhere (Oswald, 1997; Partridge & Rickman, 1997; Engelhardt, 1994). Owner-occupied housing connotes 'stability', and as such it may be at odds with other developments in contemporary society, the world economy (global markets), and the labour market, which are now more characterised by 'flexibility'. It may ultimately make economic crises even worse in the future (Smith, 2005; Stephens, 2005; Burchard & Hills, 1998; Ford & Quilgars, 2001). Public subsidies of owner-occupied housing may on the one hand lead to a more affluent society and social stability (as a result of the financial and other concomitant socio-cultural 'gains' derived from owner-occupied housing) but may on the other hand lead to increased social and individual risks in an already unstable 'risk society' (Beck, 2004).

It is more difficult to distinguish between supply-side and demand-side subsidies in the segment of owner-occupied or cooperative housing, than it is in the rental housing segment. Strictly speaking, most public subsidies of owner-occupied housing takes the form of demand-side support, which is not about directly financing the construction of 'reasonably priced' new flats but rather about increasing the public's disposable income and purchasing power – for example, by providing favourable loans, interest subsidies, premiums

(in housing-savings schemes), guarantees (for repayment of private loans), grants (down payment grants that cover the difference between the maximum credit obtainable from private sources and the end cost of the owner-occupied housing), or tax subsidies (e.g., the option to deduct the repayment of the principal or interest from the tax base or from the tax; exemption from the capital gains tax or exemptions/discounts from the tax on imputed rent).

However, these forms of subsidy may also be conditional on investment in new housing (i.e., they are only provided when the housing is new), in which case they should be regarded more as supply-side subsidies, even though the flat owner, flat user, and subsidy recipient are one and the same person, and that this form of subsidy also increases the income and the purchasing power of the recipient. Moreover, public subsidies on the construction of rental or cooperative housing, which, usually over a fixed period, are sold at a residual (low or even zero) price to flat occupants, that is the privatisation of 'social' housing, is most certainly a supply-side subsidy. In this case we can speak of an economic subsidy, that is a hidden subsidy derived from the seller's option to suspend the historical growth of housing prices (to forgo the capital revenue from the price appreciation of the residential real estate investment), without incurring any real loss that would have to be covered by public resources. It is more an opportunity cost than an explicit form of public subsidy.

The comparative advantages and disadvantages of subsidising supply and demand in the sphere of owner-occupied housing are similar to those cited in the sphere of rental housing. Supply-side subsidies increase and modernise housing stock and push the prices of existing housing down. Indirect demand-side subsidies can have the opposite effect on the price of existing housing, however, it does not restrict the recipient of the subsidy to choosing just new housing, and in terms of targeting there is less of a bias towards higher-income households, which is the group that tends most often to acquire new housing. The second option also manages to avoid generating the various social injustices that arise from the selective and arbitrary privatisation of flats at favourable prices to existing occupants.

Another important observation is that, owing to the low price elasticity of the supply in the residential real estate market, subsidising demand in the sphere of owner-occupied housing can have far greater unintended and, probably, negative effects on the housing market (e.g., from the capitalisation of subsidies into an increase in the prices of properties for sale) than in the case of demand-side subsidies affecting rental housing. Examples can be taken from the UK or the Netherlands, countries with low price elasticity of supply, where in the past fifteen years there has been an increase in the indicator of the price-to-income ratio (the ratio of the average price of a flat to the average annual net household income) from values around four to values around seven (Lux *et al.*, 2008); in these cases this may rather be due to the liberalisation of the mortgage credit market and low inflation rates.

Given that owner-occupied housing is a very expensive good, one most often acquired by households with mid-to-high incomes, public subsidisation of owner-occupied housing is also often regressive – that is it tends to help higher-income households more than lower-income ones. It is precisely because owner-occupied housing is expensive to acquire that it is usually very difficult to target subsidisation, and unlike rent subsidies, for example, in the sphere of rental housing, it can never achieve the same kind of effect: a ‘small’ subsidy is in its scope insufficient to make a difference for the majority of lower-income households and therefore is of no interest to them (even targeting this support would do little to change things), while a ‘large’ subsidy generates much greater market distortion (especially when directed at the purchase of existing flats), false expectations (it dramatically alters market preferences), and is usually too costly for public budgets. Unfortunately, the subsidisation of owner-occupied housing tends to be more or less regressive.

There is a genuinely diverse range of specific forms of intervention. Generally it can be said that in ‘old’ EU member states there is a tendency to limit tax subsidies and reduce direct public expenditures (Lux, 2005a). While there are genuinely fewer and fewer low-interest loans being provided by the state, and it is generally possible to see a reduction in the significance of direct subsidisation of owner-occupied housing, in the second half of the 1990s and in the early years of the new millennium in some countries (USA, Australia, the Netherlands, and until recently also Germany) new forms of down payment grants were introduced. This return to grant subsidies can depend largely on the position that the main political authorities in a country take on how substantial the social and personal gains are to be derived from the high degree of owner-occupied housing in the country, or even an attempt to draw more low-income households into the owner-occupier housing sector (Lux, 2005a).

Recent housing policy shifts

Although no government has ever questioned the important role of the public sector in ensuring greater equality in housing consumption (the role of understanding paternalist), achieved especially through the use of instruments aimed at increasing the affordability of housing for low and middle-income households, most EU countries in the 1980s and 1990s saw dynamic reforms of housing policies, massive cuts in public housing expenditures and a move away from social housing construction and operation support towards support through income-tested housing allowances and support for the acquisition of owner-occupied housing (Donner, 2000; Boelhouwer & Van der Heijden, 1992, 1994; Priemus, 1997; Maclennan & More, 1997). The move away from supporting supply towards supporting demand in the field of rental housing is most visible in Great Britain, Netherlands and Sweden, that is – and this is very important – in those EU countries with the highest share of social housing in the total housing fund. The following reasons are most often cited as

being behind the housing policy reforms (Boelhouwer & Van der Heijden, 1992; Priemus, 1997; Maclennan & More, 1997):

- the need to decrease public budget spending (due to budget deficits, growing economic globalisation creating the pressure on tax systems or the need to comply with Maastricht criteria upon entering the EMU) assuming that demand-side subsidies are cheaper than supply-side subsidies;
- low performance efficiency of social housing providers (bureaucracy, inflexibility, inefficient management, high construction and management costs);
- low effectiveness of social housing provision using the argument that low rents are often paid also by households that do not need state aid;
- the political will to meet the growing preference for homeownership (often exaggerating the positive aspects of homeownership and hiding the risks);
- the attempt to return private investors back to the housing market from which they were pushed out by post-war massive public housing construction;
- the conviction that the problem of post-war housing shortage is no longer a problem.

While many of the above-mentioned arguments are generally correct, a profound context-based cost-benefit analysis was often missing when reforms were implemented. For example, according to Amann & Mundt (2006) the share of public housing expenditures in the GDP of 'conservative' Austria is currently lower than in many countries that underwent policy reform. Even if re-orientation of housing policy may actually lead to lowering public housing expenditure, other, insofar neglected public expenditure may rise and compensate for part of the achieved public benefit. A comparison of demand and supply-side subsidies is not a simple equation with one optimal result and both types of subsidies may have relative advantages and disadvantages, mainly when taking into account the wider context in particular country.

The fact is that in the period between the two United Nations Conferences on Human Settlements, HABITAT in 1976 and HABITAT II in 1996, in which policymakers from almost the entire world took part, there was a complete change in the understanding and perception of housing with respect to the responsibility of the government and the state. Generally, this shift is summarised by the slogan: 'from housing supply to enablement'. According to *Global Strategy Until 2000* (1988), states should focus on the creation of a legal and economic framework for citizens, non-governmental organisations, and the private sector so that they all can ensure housing and related services more efficiently than the state ever could. In the famous World Bank report entitled *Housing: Enabling Markets to Work* (World Bank, 1993), the issue of housing and urban development is defined as part of a more general economic strategy. The most important items of the strategy concerning housing are:

ensuring property rights; development of private long-term mortgage credits; support rationalisation; stimulation of infrastructure development support of the private sector in all spheres. Changes during the 1980s and 1990s in the understanding of the state housing policy and the role of individual actors on the housing market may also be formulated as moving 'from housing needs to housing rights'.

Over the past few decades, the absolute scope of public finance allocated for the construction of social housing has significantly decreased (see the special volume of *Housing Studies* 12/4; Boelhouwer & Van der Heijden, 1992; Priemus, 1997; Maclennan & More, 1997; Van der Heijden, 1999) and monitoring of efficiency/effectiveness of social landlords' performance (through measurement of different performance indicators) grew in importance (especially in the UK where it is led by the Housing Corporation and the Audit Commission). Furthermore, in some countries a dominant position in the sphere of new social rental housing construction has been given to private non-profit landlords (housing associations) that up to this point had played only a marginal role (UK, Ireland). In the Netherlands (the EU country with the highest share of social housing in the total housing stock) where non-profit housing associations historically became almost exclusively social landlords, they were completely cut off from state resources in the mid-1990s (Priemus, 1997). In the future, housing associations in the Netherlands are to cover the costs of their 'noble' activities solely from private loans and their own capital (Salet, 1999; Boelhouwer, 2007). Housing associations in UK are also increasingly being forced to use private capital. In the 1990s they became the exclusive developers of new social flats and the share of capital expenditures for social housing construction covered by grants from the Housing Corporation funds (the state budget, in fact) fell in the course of the 1990s from 90% to 50% of total construction costs (Maclennan & More, 1997; Malpass, 1999; More *et al.*, 2003; *Housing Corporation*, 1997, 2001).

In Sweden the conservative government launched a tax reform in the 1990s related to a sharp cut in public subsidies on social housing (Turner, 1997) that forced public operators of social dwellings (municipalities) to transfer the burden to the tenants, thus making housing less affordable (housing expenditures to income ratio in Sweden is the highest among EU countries and grew the fastest in the 1990s). Social housing reform in France led to an expansion of the semi-public/semi-private legal form of housing associations called OPAC (to the detriment of the completely public form), that have on the one hand obtained greater power because of their position as a private company but, on the other hand, now receive less public funding (Edou, 1998).

1.4.3.3 The methodology of assessment of housing subsidies: the concept of efficiency and effectiveness

After summarising several hypothetical and practical examples of state intervention in the field of housing consumption, in this section I will go on to discuss a possible methodology for their assessment. There may be a whole range of possible evaluation tools to assess policies (state interventions) in the field of housing consumption but welfare economics is gradually becoming the standard approach in policy studies. “Welfare economics is a branch of economics that uses micro-economic techniques to simultaneously determine allocative efficiency within an economy and the income distribution associated with it. It analyses social welfare, however measured, in terms of economic activities of the individuals that comprise the theoretical society considered” (Wikipedia).

As mentioned above, the dual role of an ‘ideal’ (independent, interest-free and corruption-free) state in the field of housing policy as rational economist and understanding paternalist can practically be rewritten in policies directed towards the (economic) efficiency of housing market functioning on the one hand, and towards the (social) effectiveness (equity) in distribution of housing services on the other – they thus simultaneously include allocative efficiency and income distribution, that is the main subjects of welfare economics. Common trade-off situations arise between efficiency and effectiveness. Redistributive interventions, though very effective may be at the same time inefficient and may thus distort the function of housing market. While efficiency is a common concept for all economic systems, the concept of effectiveness (equity) crucially depends on the selection of the type of welfare state (or concept of social justice) in a particular social and political environment.

The concept of *efficiency* originated in neoclassical economics and in the field of welfare economics was applied in the social welfare function – simply by summing comparable (similar!) individual utility functions (the work of F.Y. Edgeworth, H. Sidwick, A. Marshall described in Ng 1983; Just et al., 2004 and others). However, this approach would produce rather different conclusions about ‘efficient’ social welfare; including such distributions that would lead to deep income and wealth inequalities in a society. The *New Welfare Economics* (studies by V. Pareto, J. Hicks and others) has clearly distinguished the efficiency and equity (effectiveness) parts of theory – the first is analysed using the Pareto criteria of efficiency and the second can be analysed only in close conjunction with particular social norms and values, welfare state regime and/or social justice theory. In this way the concept of efficiency has been ‘freed’ from the influence of varied normative statements and/or social justice theorising. In contrast, the concept of distribution (of incomes, wealth or goods and services) has become fragmented into various theories of social justice

and, consequently, into many types of particular welfare state regimes.

It was mentioned that efficiency is defined through the Pareto lens: if any alternative allocation of goods increases utility from consumption for at least one actor on the market and at the same time does not decrease utility from consumption for other actors then we say such allocation is inefficient and there is room for improvement in market performance. This is called Pareto optimisation or Pareto improvement. Such improvement may often be ensured only by state intervention. For housing markets, particular examples of market failure may be the existence of oligopoly or monopoly in housing finance or production (leading to above-normal profits for service suppliers), asymmetric information among market agents (information access barriers), externalities during housing production or consumption. An example of this inefficiency may, however, be the existence of public subsidies (state interventions) that crowd out the private investments, impede lower taxation and distort efficient market functioning. A final example, which points to my main interest, is the situation when the state spends tax-payers' money for production and allocation of goods or services that could be allocated similarly (or even more efficiently) by private entities, or the situation when alternative subsidy settings can produce, under the condition of holding the same quality and quantity of consumption distribution, public savings.

Effectiveness (equity) is closely associated with the idea of social justice, welfare state; it relates to the 'fair' distribution part of social welfare studies. As such, it is closely connected with particular welfare state regimes and particular social norms. The redistribution of wealth (achieved generally by states) forms a crucial part of the whole concept as this is the only possibility for ultimately attaining 'fair' or 'desirable' wealth distribution. In fact, effectiveness and equity, terms I used as synonyms up to now, do not hold in theoretical welfare studies the same meanings. The concept of effectiveness is a broader one. The effectiveness may be understood as the degree to which the originally defined goals of state intervention are met, that is, whether public funds are actually spent where they were allocated and whether those for whom they were intended actually are helped. The goals of state interventions vary and do not have to necessarily relate to redistribution of housing consumption towards low income households (equity); the example in housing policy may be creating incentives for housing stock modernization. Some intervention targets, like for example higher take-up of social transfers, relate to the wealth redistribution and equity goals indirectly. Equity is a subset of effectiveness, clearly relating to the income and wealth redistribution goals.

The concept of equity is thus not left to a vague 'definition infinity' of the concept of effectiveness; the concept is not left solely to the will of lawmakers or governments who define the intentions of the state interventions. The equity as a subset of the concept of effectiveness is, at least partially, generalised into the common shared assumption that whatever state redistribu-

tion of wealth is finally applied, it should decrease income inequalities in society, that is, redistribution policies should help the worse-off with the costs of the better-off (it relates to income distribution). The scale of income and wealth redistribution may be small (residual welfare state regime) or high (social-democratic welfare state regime) but in either case, all modern concepts of social justice share the assumption of the direction of redistribution from high-income to low-income members of society. Going in the opposite direction, redistribution would breach theoretical foundations, on which modern democracy and the concept of human rights stand. It would not be sustainable if the state pronounced on the equality of human beings and, at the same time, asked for support to be directed to high income households, thus asking for higher income inequality. The concept of equity and equality are all derivatives of modern liberalism and political democracy, clear and living relicts of liberal thought.

Welfare economics also distinguishes between vertical and horizontal equity (Barr, 1998). Vertical equity measures the degree of redistribution of income and wealth from the rich to the poor. In the case of particular housing subsidy it measures the extent to which such subsidy is actually allocated to low income households. It measures whether it ultimately decreases income (wealth) inequality in society. Horizontal equity is connected with the idea of setting a minimum income (wealth) that would be ensured for all members of society, as well as with the assumption that all low income (poor) households have equal and unrestricted access to subsidies, that is none of the low income (poor) are excluded from such redistribution. In the case of particular housing subsidy it measures whether any low income (poor) household is not eligible to apply for the subsidy. Some low income households are excluded from subsidies because, for example, the programme has been set up badly or the potential claimants are badly informed (or may be afraid of potential social stigmatisation).

On the second side, theoretically more generalized concept of equity does not take into account, when compared to the concept of effectiveness, particular aspects of particular policies. It applies the idea of 'fair' redistribution from high-income towards low-income households by simply measuring the scale of income distribution brought about by state interventions. However, in housing policy particularly, the households in need of public help do not have to be often those with the lowest incomes; and this may be especially the case in transition countries. Let me give the example of a housing system with two main rental housing segments – segment A with low regulated rents and segment B with much higher market rents. The difference in rents between segments A and B for comparable dwellings is really high – rents in segment B are, let's say, six times higher than rents in segment A. The government introduced housing allowance which is well designed to help especially low-income households, by setting maximum income of eligible household

and maximum notional housing costs on very low levels. However, as it is often the case, the turnover in segment A is low and many households do not have other option than to find their housing in segment B. As the amount of housing allowance is computed from low notional housing costs (for example, reflecting rents in segment A), many low-income households, though eligible for an allowance, find out that an allowance is not high enough to allow them to pay six times higher market rents. Moreover, households with slightly higher incomes (middle income households) are due to their higher incomes no more eligible for an allowance – even though that they spend, for example, more than two thirds of their incomes on market rent they do not receive any effective help from the state. The main inequality arising from such situation is not income inequality but inequality in rent-to-income ratio (housing costs burden). Housing allowance under such situation would be evaluated as equitable (redistribution well towards low income households), but it could hardly be evaluated as effective. Under the situation of such market segmentation, effective way of redistribution (i.e., the application of the role of the state as understanding paternalist) should not be restricted only to the redistribution towards low income households – though equitable from the point of view of income redistribution it produces substantial social, though not strictly income, inequalities.

Another example may be a housing allowance which leads, due to its high (let's say 100%) taper, to the situation of poverty trap. It is well designed to help especially households with the lowest incomes but the fact that the allowance amount decreases in the same pace as potential income from employment leads rather to preservation of existing social inequalities than to their reduction (many people will stay unemployed). Social and income inequalities are not always the same, and this is particularly the case for housing policies and particularly the case for transition countries, as I am going to show in more detail below. Therefore in this book I am going to use the concept of effectiveness (and terms 'effectiveness' instead of 'equity'; 'vertical and horizontal effectiveness' instead of 'vertical and horizontal equity') though it will be narrowed to the role of the state as understanding paternalist in the field of housing consumption, i.e., to interventions (housing subsidies) aiming at decreasing income but also broader social inequalities. Although I am not going to use the term 'effectiveness' as synonym for 'equity' I will assess only those interventions that are connected with redistribution of housing consumption towards those in need. The evaluation itself will use almost the same theoretical and methodological device as studies of equity; the only but important change of perspective is that social inequalities in the particular practical field of housing consumption (housing accessibility, housing affordability) do not have to be always connected with income inequalities and households in need of public help do not have to be always low income households. The other reason for use of the term 'effectiveness' rather

than 'equity' lies also in restricted statistics in transition countries, including the Czech Republic – measurement of income redistribution effect (equity) of particular housing subsidies is often impossible due to non-existing data. The redistribution effect of subsidies can be often estimated only indirectly but, in such a case, only on more broadly defined social inequalities. Finally, my decision can also be justified by an earlier version of the "Welfare Economics" of Barr (1993) where only terms 'horizontal and vertical effectiveness' are used to assess the state policies from the point of view of their targeting and meeting the redistributive goals of the state.

The concept of efficiency is also, as described above, broader. Next to interventions in the field of housing consumption it also relates to state interventions concerned with the general functioning of the housing market, covering for example problems such as price speculations, oligopoly structures in housing supply, restrictive urban planning, asymmetric information, etc. Therefore, in my book I limit the concept of efficiency to the efficiency of those state interventions that have direct influence on housing consumption, or defined more precisely, those state interventions aimed at redistributing wealth, goods or income. In this way I relate the concept of efficiency directly to the concept of effectiveness (with respect to housing consumption) or, in other words, I subordinate the concept of efficiency to the concept of effectiveness.

In sum, I will firstly analyse and assess both horizontal and vertical effectiveness of particular state interventions (subsidies) in the field of housing consumption and, secondly, analyse and evaluate the efficiency of the same set of subsidies from the somewhat restricted perspective of the efficiency concept. Efficiency will be limited to the analysis of possible public savings under an alternative subsidy setting, or under an alternative set of subsidies, and only for those state interventions that will be evaluated from the point of view of effectiveness. Efficiency will be thus subordinated to effectiveness and narrowed to potential public savings; it will be limited mainly to a cost-benefit analysis of selected state subsidies.¹¹

There is often a trade-off between efficiency and effectiveness of housing subsidies. Clearly, the lower the public support per household (or per dwelling), the lower the public spending and the higher the efficiency of the subsidy (one euro of subsidy produces more euros of private investments). On the other side, small public subsidies often help only those who do not need them; they are seldom targeted well at those in highest need. Such trade-offs are solved in this book by subordinating efficiency to effectiveness. In other words, the main intention is to measure and evaluate the effectiveness of

¹¹ "Economic efficiency is about making the best use of limited resources given people's tastes." (Barr, 1998, p. 70)

subsidies, because the main goal of wealth redistribution (intervention of the state as understanding paternalist) is to decrease social and income inequalities; otherwise it loses all meaning. The subordination of the concept of efficiency in my state-centred analysis is therefore a natural methodological step.

I can now define a set of assumptions, used in my further empirical work, which derive from the definitions of efficiency and effectiveness stated above.

For effectiveness the assumptions are as follows:

Main assumption 1: Effective subsidies assist lower-income (needy) households more than higher-income (less needy) households. (Vertical effectiveness)

Main assumption 2: Effective subsidies do not exclude any lower-income (needy) household. (Horizontal effectiveness)

Sub assumption 1: The absolute amount of subsidy should be significantly higher in the group of lower-income (needy) households than in the group of higher-income households (less needy).

Sub assumption 2: The subsidy should contribute to a reduction in the level of inequality in the society.

The evaluation of the effectiveness of a certain measure should therefore be based on a comparison of the degree of inequality in society before and after that measure is introduced. If the effect of such a measure reduces the level of inequality in society, it can be assessed as positive in terms of its effectiveness. Given that the income of households with more members tends to be higher, attention will be paid not only to the distribution of subsidies according to the total household income but also according to the equivalent income, that is household income adjusted according to the OECD equivalence scale.¹²

For efficiency the main assumption is, as follows:

Main assumption: Subsidies are efficient when it is not possible to meet redistributive goals in the field of housing consumption in a less costly way, that is, under an alternative setting of the subsidy or an alternative setting of the whole set of subsidies.

Appendix B lists the questions formulated for the purpose of evaluating effectiveness and efficiency of different housing policy instruments in the Czech

¹² OECD equivalence scale is derived from the number and age of individual household members: for the household head the weight is equal to 1.0, for children aged 0 to 13 it is 0.5, and for each additional household member it is 0.7.

Republic as well as in selected transitional countries used in this book for a partial policy international comparison. All the questions are intended to estimate approximately whether the subsidies are well-targeted to those in need of help (effectiveness) and whether they are introduced in a way that would ensure an economical use of public sources (efficiency).

Besides the 'working' questions listed in Appendix B, the evaluation of effectiveness will be improved by the use of statistical methods and concrete measurable indicators. I applied standard statistical tests for the evaluation according to sub assumption 1. The literature points to no general rule for determining at which rate of redistribution a given instrument exhibits high effectiveness or at which rate of redistribution its effectiveness is poor. Setting limits is always a normative decision. For the purpose of the following analyses the assumption was that if 90% of the total sum of resources distributed by means of a given instrument went to 50% of the lowest-income households and at the same time 75% of the total sum of resources went to 30% of the lowest-income households, then the given instrument shows a relatively high degree of effectiveness.

For an evaluation according to the sub assumption 2, I used indicators of inequality presented, for example, in Barr (1998, pp. 149-152). These indicators were used to compute income inequality in a society before and after the application of a particular subsidy; the difference shows whether or not the subsidy reduced the income inequality. One of the simplest indicators of income inequality is the standard deviation computed as follows.

$$V = \sqrt{\frac{1}{n} \sum_{i=1}^n (y_i - \mu)^2}, \text{ where}$$

y_i - income of household i ;

μ - average income;

n - number of households.

The disadvantage of standard deviation is that it is sensitive to the absolute income level. This may be eliminated by the coefficient of variation, which standardises standard deviation in relation to mean income, as follows.

$$C = \frac{\sqrt{V}}{\mu}$$

The main disadvantage of the coefficient of variation is that it does not take into account the level at which income redistribution occurs. In other words, if CZK 1,000 is transferred from a household with an income of CZK 20,000 to a household with an income of CZK 6,000, it expresses itself in the value of the coefficient of variation equally to what it would if CZK 1,000 were trans-

ferred from a household with an income of CZK 500,000 to a household with an income of CZK 400,000. The variance of the log-income makes it possible to take into account the greater weight of redistribution in favour of low-income groups, as follows.

$$H = \frac{1}{n} \sum_{i=1}^n (\log y_i - \log \mu)^2 = \frac{1}{n} \sum_{i=1}^n \log\left(\frac{y_i}{\mu}\right)^2$$

Probably the most commonly used measure of income inequality is the Gini coefficient (represented by the Lorenz curve). Each point on the Lorenz curve denotes what portion of the total income is distributed among $x\%$ of the lowest-income population. The Gini coefficient is calculated as one-half of the arithmetic mean of the absolute value of the differences between all the pairs of incomes standardised in relation to mean income.

$$G = \frac{1}{2n^2\mu} \sum_{i=1}^n \sum_{j=1}^n |y^i - y^j|$$

Another recommended indicator (Wiles, 1974) of income inequality is the ratio between the mean income of 5% of the highest-income households and the mean income of 5% of the lowest-income households (hereinafter this indicator will be referred to as W). All the aforementioned indicators will be used in the following analyses (the Gini coefficient will be graphically illustrated by the Lorenz curve) if data on allocation of subsidies and income of eligible households are available. In all other cases I will have to find alternative data sources, such as sociological (attitude) surveys.

Measurement and evaluation of efficiency of subsidies is far more difficult than measurement and evaluation of their effectiveness. For example, housing policy reforms (alternative subsidy settings) could lower public expenditures and increase efficiency of public spending in the short term, but many side effects, caused by speed of reform and application of the 'black-and-white' perspective in practical policies, may create substantial drawbacks in the long term. Policy changes often create, some while after their implementation, the need for unexpected additional public expenditures. Such expenditures may offset substantial parts of the achieved public savings. It was, for example, demonstrated by Lux (2004) or Wilcox & Meen (1995) that public costs following the housing policy reform in favour of demand-side subsidies in UK (or Scotland) may be, in fact, far higher than generally quoted, if we also include administrative costs with allocation of housing allowances, costs following from up-rating pensions and benefits (when social rent increases are reflected in CPI), costs following from growing social segregation (from vacant flats in residualised ghettos, or social prevention programmes), additional public costs following from rent inflation in the private rental sector

(due to low elasticity of supply) and 'labour market' costs following from the growing dependence of eligible households on housing benefit ('poverty trap'). These societal costs are, however, neglected when simple calculations of public savings (efficiency) are made. Another case is the 'capitalisation' of public subsidies to promote homeownership into house prices (in this case the efficiency of demand side subsidies is substantially reduced due to the inelastic housing supply).

From the methodological point of view the assessment of efficiency of subsidies is a difficult issue. Cost-benefit analysis estimating the level of public finance wastage or savings requires the use of profound econometrics. To be fully precise, I should simulate all the economic and social consequences of different subsidy alternatives in the long term. Such simulations of complex and mutually related markets are so complex that they can hardly be achieved for all types of selected subsidies. In this book, I will measure efficiency through econometric simulation of the broader economic and social consequences of alternative subsidy settings in only one, albeit very important subsidy in the Czech environment – the economic subsidy stemming from rent regulation. In all other cases I will check only whether short-term public savings could be achieved if the current subsidy rules are changed (with no regard for interaction with other housing subsidies and only weak attention for the broader economic and social consequences). This 'restricted' methodology results from the limits of econometrics itself and also reflects the subordinated position of the concept of efficiency in my book.

1.4.4 Methodological discussion on international comparison of housing systems

This section should answer the final preliminary question that relates to the quest for an appropriate methodology for the international comparison of housing systems or international comparison of state interventions in the field of housing consumption. Though the goal of this book is not comparative, as I mentioned before, we cannot fully understand the situation and changes in the specific Czech environment without at least partial comparison with the situation in other transition societies. This section should address the preliminary question:

4. *What relevant international comparison of interventions in the field of housing consumption can be used to better understand the process unique to the Czech Republic? What methodological features should such international comparison necessarily hold?*

After 1990 in most post-socialist countries there emerged an interest in discovering how housing systems in the prosperous West function and how oth-

er transition countries were dealing with the up to now unknown problems of transition. Comparative studies, articles and statistics soon followed. Some were prepared by international organisations (the World Bank, UN/ECE) or lobby organisations (CECODHAS, FEANTSA, IUT, EMF); others by national lobby associations (associations of tenants, landlords and/or homeowners). They produced a diverse array of information (and interpretations) that could easily lead to misunderstanding. Let me now demonstrate one such misunderstanding on the example of social housing tenure.

1.4.4.1 Case of misunderstanding – ‘social’ housing in transition countries

Before 1990, state interventions created the segment of mass public (public company) rental housing stock with rents and utility prices kept at very low levels. Rental dwellings were allocated freely and strong security of tenure guaranteed the occupancy title for both the beneficiary and his or her relatives.

What makes the description of social housing tenure in transition countries difficult is mainly the fact that social housing was not defined during socialism. We cannot simply apply this term to mass public (state) rental housing stock built in former socialist countries, especially because of actual dwelling allocation procedures. At the time the state was responsible for providing housing to all its citizens and not just to those who were financially worse off. The general right to housing was guaranteed by the state, and although it could take many years before that right was satisfied, everyone was entitled to register on various lists to await allocation of a rental (semi-rental) flat with a low regulated rent. State housing (state rental flats, state company flats, semi-state cooperative flats) should originally have replaced all other housing tenures as a part of the plan to liquidate private property (though later on this plan was changed due to its unrealistic nature). And because state housing was for everyone, it was particularly quickly allocated among those people who, through their clientele networks, or even straightforward corruption, were more skilful in the process of acquiring housing than others – that is, usually for people who did not rank in the category of the neediest. To use the adjective ‘social’ for the mass public rental housing in socialist countries would thus, even from today’s perspective, be inappropriate.

Sooner or later the transition states stopped their massive capital subsidies to public housing construction but price and salary liberalisation led to sharply increasing costs of housing production. As the logical consequence, overall housing output volumes dropped dramatically and newly established households (young people, recently divorced) found it more and more difficult to acquire affordable housing. Mortgage banking was undeveloped, especially due to high inflation, bad legislation and low competition. New institutional

and cultural patterns appeared: unemployment, homelessness, income polarisation, and market uncertainty. All of this required substantial reform in the exploitation of existing public housing and the establishment of a new system of housing subsidies, reforms that would direct public aid more to those who really needed help under the new market conditions. Instead, the governments in transition countries remained 'locked in' the institutional and ideological settings of the past.

With exceptions – such as Poland and the Czech Republic – most transition governments opted for the strategy of a quick mass sale of existing public housing to sitting public tenants under very advantageous price conditions. Such massive sale of housing could hardly take into account the criteria of need and social justice. As part of the decentralisation of power, the former state (state company) housing was often transferred free of charge to the ownership of municipalities. Despite that, the states gave public tenants the right to buy the flats that they occupied under the conditions set by the central legislation. The rights of municipalities were thus restricted by the will of central state to sell public dwellings at a very low price to the sitting tenants (in fact, free of charge in countries such as Estonia, Lithuania, Russia, Albania and others). Various motives lay behind this important institutional change – one of which was to protect existing public tenants from a future sharp rise in housing costs. In a few years the housing systems dominated by public rental housing transformed into the systems dominated by owner-occupied housing. Public rental housing for new or needy households practically disappeared; in contrast, a large portion of affluent public tenants received substantial public help in the form of cheap owner-occupied dwelling.

There were a few exceptions to the main stream. For example, in Poland and the Czech Republic right-to-buy legislation was not passed and public housing privatisation remained a possibility open to municipalities. Consequently, in these countries municipal rental housing remained an important part of the total housing stock. However, these states decided to preserve the original pre-1990 type of non-targeted centrally-controlled regulation of rents both in municipal and restituted private rental housing (as well as to keep most of the pre-1990 forms of tenure protection), and to allow only small and very gradual rent increases. Rent regulation, similar to massive sale of public housing, closed the doors of the affordable rental housing segment to all needy newcomers and once again distributed hidden subsidy in the form of cheap rent to a substantial portion of affluent households. Logically, these regulations also led to the creation of black markets with rights for regulated rents. Though not privatising public housing, governments tried, using different means, again to protect all existing public tenants from growth in housing costs.

In fact, the same part of the population in both groups of countries received hidden public subsidies – either in the form of an owner-occupied flat

gained at a very low price or free of charge, or in the form of rental housing with very low regulated rent. Income and/or social situations of eligible households were not important to the allocation. Institutional and moral patterns of socialism (assumptions of general equality and universal applicability) intervened thus in the market systems with growing income and social inequalities.

With regard to the social housing, considerable confusion may surround the figures used for international comparison. Whenever a country opted for the strategy of mass public housing privatisation, then in the course of several years the proportion of public (municipal) housing decreased to a marginal share. If a country chose the strategy of preservation of rent regulation, then municipal housing stock remained relatively large. According to a simple principle commonly applied in comparative studies of social housing, in the countries that opted for the first strategy, 'social housing' suddenly ceased to exist (e.g., according to Scanlon & Whitehead (2004), in Hungary 4% of the housing stock was in the category of 'social renting'), while in the countries that chose the second strategy, 'social housing' constitutes a significant portion of the total housing stock (e.g., according to Scanlon and Whitehead (2004), in the Czech Republic it was 19% of the housing stock). A fatal error of such approach is that it lacks the perspective of the flat-users, ignores the meaning of public housing during the socialism, hides the similar motives of transition states behind the allocation of hidden subsidies (no matter what type) and does not take into account the fact that rent regulation in municipal housing might increase (instead of decrease) social inequalities in society due to the preservation of original social structure of tenants. In the Czech Republic the rent-controlled housing sector is sometimes called 'quasi-homeownership' (Šmídová, 1996), as the official owner of the flat (municipality, private landlord) is not the same person as the one who exercises most of the property rights (tenant). This form of housing tenure is thus much closer to the homeownership tenure than it would arise from standard statistics.

If we take into account the imperative of allocation of social dwellings according to the principle of need, we could probably, label the remaining marginalised segment of municipal housing in the first group of countries as 'social housing' but we cannot do the same for municipal housing in the second group of countries. This also reflects the views of transition governments themselves. They often refuse to call municipal housing social housing (with some exceptions, such as Russia) or they use definitions which relate social housing to only a small part of municipal housing – only those dwellings with very basic standards and/or located in unattractive places that are explicitly allocated to those in acute housing need (e.g., Poland, Czech Republic) or to households with very low incomes (e.g., Romania); and/or new municipal dwellings built with the use of post-1990 public subsidies to target the housing needs of specific groups of households (social care housing, protect-

ed housing, pensioner housing, half-way housing, housing for war refugees, housing for households with an income below the living minimum, housing for Roma households and other vulnerable households). The number of such new municipal dwellings is low, however, with few exceptions (Czech Republic, Slovakia) due to limited public budgets.

Consequently, in all transition countries only a very small portion of rental housing stock explicitly serves those in housing and social need (Hegedüs, 2008). Social housing as the real policy concept thus largely remains only as an open possibility for the future. Such important specific contextual features are, however, often marginalised in general comparative housing discourse.

1.4.4.2 Methodological imperative – individual openness of researchers in comparative studies

In comparative studies generally, the various goals, the range of methods used, alternative definitions of indicators and specific approaches to generalisations all leave considerable room for an entire ‘market’ of comparative statements to emerge, for the competition and contrasting of statements in professional journals, studies and monographs. The social sciences long ago rejected the idea that there is just one true and correct statement on social reality (or one correct and applicable method with which to determine it); the understanding is that there can always be many statements, that they can be contradictory, and that they all have the right to compete with each other in the arena of scientific discourse. Knowledge of real scientific value emerges out of this competition, this institutional openness, which often broadens our understanding of particular phenomena in a very useful way. In other words, the diversity of perspectives, methodological approaches, the range of statements on a certain theme, and particularly the competition between them in open scientific discourse is the first guarantee for scientifically valuable knowledge to emerge.

The *institutional openness* and the competition of scientific statements is an essential precondition of scientific knowledge but is by no means in itself sufficient. I believe that it is not the ‘scientificity’ of the method (e.g., quantitative versus qualitative methodology), but the ‘scientificity’ of the work of the individual researcher that is the important condition for gaining valuable knowledge from international comparison which would avoid the above-mentioned type of misunderstanding. What is meant by the ‘scientificity’ of an individual scientist’s approach? Even using statistical ‘exact’ methods it is possible to arrive at the conclusions the researcher is looking for if the data are fittingly modified; most social relationships are not strong enough to withstand this kind of ‘modelled distortion’. Blaming qualitative approaches (narrative methods, contextual analyses, in-depth, non-representative focus group discussions and interviews, biographical sociology) for producing state-

ments that are more normative and subjective is usually just a 'blow below the belt' on the part of quantitative sociology and mathematical economics and simply an expression of intolerance. However, another matter altogether is how much scientists actually try – whether out of their own will or under pressure from the party commissioning the research – to prove a conclusion formulated beforehand.

The most important virtue of a scientist is perhaps the capacity for abstraction, and the desire to discover something new. But no less important a virtue of social scientists, especially those who conduct comparative studies, is their subtlety, sense of detail and context, openness to interpretations, which I would refer to as *individual openness*. This type of openness is not institutional in character, but individual and intellectual – as such it is difficult to recognise, criticise, or commend it. Attaining the full ideal of individual openness is practically impossible; it is not possible to execute a specifically human activity while eliminating every aspect that is so intrinsically a part of being human (language and cultural barriers). On the other hand, it is possible to work towards such an ideal, if the following imperatives on valuable comparative research are taken seriously:

- Always create an international network of researchers or at least find remunerable local informants that are as informed as possible about the subject in the comparison (rule of thumb: one country – one local informant);
- Draw up a set of indicators (interpretations) on the economic, social, and cultural context in the given countries, discuss it with local informants and adjust it according to their comments;
- Regard informants as sources of equal status by letting them prepare a part or the whole report for the given country.

These imperatives are followed in this book, though the international comparison forms only a supplementary part. I especially use the findings from a comparative housing policy-orientated project undertaken in six transitional countries between 2000 and 2002. The project was called *Local Government and Housing* and it was funded by the Local Government Initiative of the Open Society Institute in Budapest. Local housing researchers were hired in following countries: Czech Republic, Slovakia, Estonia, Poland, Bulgaria and Romania. All local researchers conducted their own research and prepared their own paper on the housing policy development in their own country though the main targets were agreed during the first team workshop. All local researchers were well remunerated by the Open Society Institute. The contributions of local researchers were then presented in common at conferences and summed up to the main conclusions; these were discussed during the second team workshop. Finally, all individual contributions together with the commonly accepted text of main conclusions were published in Budapest in 2003

in the book *Housing Policy: an End or a New Beginning?* parts of which were, later on, translated into local languages and published in local language editions (Czech, Slovak, Bulgarian and Estonian). Further details of this research can be found in Lux et al. (2003).

1.5 Research questions

Having tried to answer the preliminary questions I can finally define the main research questions that will target the goal of my book. The research questions will be addressed in the following chapters. They are, as follows:

1. *What was the background to the development of the specific housing policy and housing system in the Czech Republic? What were the ideologies (norms), traditional problem solution patterns and institutional as well as political structures that might influence the formation and development of the housing system (including the formation of general social policy and its history)?*
2. *How effective and efficient were state interventions in the field of housing consumption during the transition in the Czech Republic if the theoretical framework and methodological device of welfare economics is used for such assessment? How effective were such interventions from the point of view of both vertical and horizontal effectiveness? How efficient were such interventions if we narrow the wide concept of efficiency to the cost-benefit analysis of state interventions in the field of housing consumption (i.e., subordinate efficiency to effectiveness)? How efficient and effective were these interventions when assessed against the assumptions on efficiency and effectiveness of subsidies?*
3. *How efficient and effective were state interventions in other transition countries (if the imperative on individual openness of researchers during the international comparison of housing policies is met)? What explanations for particular levels of effectiveness and related (subordinated) efficiency of state interventions in the field of housing consumption in the Czech Republic can be found in a partial international comparison? Can such a partial international comparison help me to understand the specific situation in the Czech Republic?*
4. *What general conclusions can be drawn about the application of the role of 'understanding paternalist' by the Czech state between 1990 and 2005? What reasons for particular levels of effectiveness and related (subordinated) efficiency of state interventions in the field of housing consumption can be found from housing system evolution analysis? What influence did ideologies (norms), traditional problem solution patterns and institutional as well as political structures have on the development of specific state interventions in the field of housing consumption, and what effects did they have on the efficiency and effectiveness of these state interventions?*
5. *Do the main findings of the research conducted for this book show whether it is*

possible to increase efficiency and effectiveness of state intervention in the field of housing consumption in the Czech Republic? If so, what would be the policy recommendations?

1.6 Outline of the book

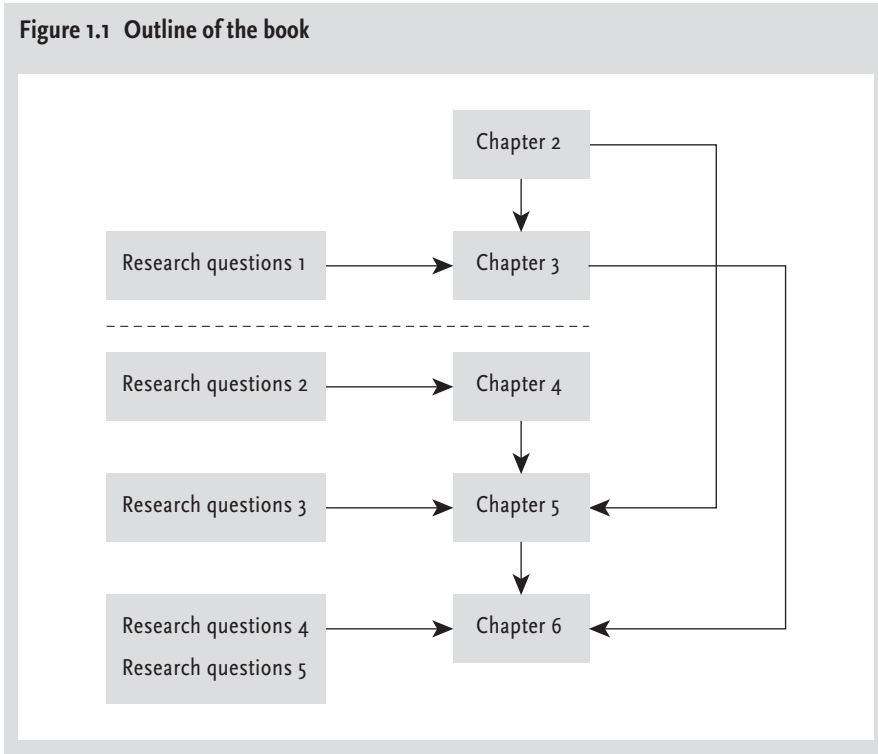
In the following, mainly descriptive chapter, I will focus on a partial international comparison of housing policies in the field of housing consumption in six selected transition countries. The purpose of this second chapter is to show what generally happened during transition in the field of housing policy and what similarities as well as differences among transition countries can be detected in this process. I will also provide details of two policies that illustrate the growing diversity among transition countries – the policy to support supply of rental housing in Poland and the policy to support homeownership in Hungary.

In the third chapter, again more or less descriptive, I will focus attention on one transitional country which represents the main subject of my book – the Czech Republic. I will try especially to answer my first research question and therefore will describe the context in which housing policy was formed and reformed during transition. This includes descriptions of the political, institutional, economic and demographic contexts as well as the history of both social and housing policies applied in the territory of the current Czech Republic in the past. This chapter will also comprehensively describe and discuss the changes in housing conditions (including tenure structure), housing policy, housing finance and housing affordability in the period 1990-2005 in the Czech Republic.

The main goal of the fourth chapter, analytical by nature, is to evaluate the effectiveness and subordinated efficiency of state interventions in the field of housing consumption (policies) introduced in the Czech Republic in the period 1990-2005. This chapter addresses my second research question. For this purpose I will employ data sets from a range of empirical surveys and apply statistical methods and econometric simulations.

The fifth chapter, again analytical, should answer the third research question, that is whether we can analyse and compare, albeit partially, the effectiveness and subordinated efficiency of housing subsidies among at least some of the selected transition countries, taking seriously into account the imperative of ‘individual openness’ in comparative research. This chapter builds on the information provided in Chapter 2, that is, a description of the differences and similarities in housing reforms among selected transition countries. The conclusions will help me understand the reasons for the application of specific policies in the Czech Republic, as well as the reasons for the particular effectiveness and subordinated efficiency of Czech housing

Figure 1.1 Outline of the book



subsidies. The purpose of this chapter is not comparative; the comparison is included to help understanding of the specific situation in the Czech Republic. The aim is to discover which specific 'national' factors are visible only via network of several 'out-national' reference points.

The sixth chapter attempts to answer the fourth research question and thus tries to complete the conclusions stemming from the previous chapter, especially by attempting to find other reasons (other than following from international comparison) for the introduction of particular types of policies as well as for the particular levels of effectiveness and subordinated efficiency of housing subsidies specific to the Czech Republic. For this purpose I apply the propositions of selected theories of housing systems, as well as the comprehensive description of the context presented in Chapter 3. The sixth chapter relates to both the fifth (analytical) and third (descriptive) chapters of the book. In its final part I also address the final research question and suggest policy recommendations.

The seventh and concluding chapter of the book summarises the main findings and provides an overview of the conclusions (answers) to all five research questions. The mutual relations between chapters and the relation of chapters to research questions are illustrated in Figure 1.1. The dotted line represents the subdivision of descriptive chapters from the analytical ones.

2 Housing policies and housing finance during transition in selected transition countries

Partial international comparison

2.1 Introduction

The purpose of this chapter is the partial international comparison of the reforms and development paths of housing policies in selected transitional countries. The aim is to show what generally happened during transition in the field of housing policy and which similarities as well as differences among transition countries can be detected in the process. This description may help me understand the specific processes that occurred in the Czech Republic and will especially help me with the partial international comparison of the effectiveness and subordinated efficiency of selected subsidies in transition countries provided in Chapter 5.

The question often put to housing researchers is: what similarities and differences arose in the reforms of housing policies and housing finance during the transformation of the economy and society of former communist countries? What did they share in common and where did individual approaches win on the way to a market economy? I will concentrate on those transition countries that decided to enter the European Union and succeeded in that in 2004 or 2007, namely, Hungary, Poland, Czech Republic, Slovakia, Slovenia, Estonia, Latvia, Lithuania, Romania and Bulgaria (always limited by the availability of information). I can hardly be expected to make an overall systemic evaluation of the whole transformation process or to set a new typology of housing systems here. The goal of this chapter is far less ambitious: to establish the relative position of the Czech Republic within the group of more developed transition countries to help understanding of specific policy changes applied in the Czech Republic. To this end I will use the conclusions of a project called *Local Government and Housing* which was conducted between 2000-2002 in six transitional countries. The following countries were included: Czech Republic, Slovakia, Poland, Estonia, Bulgaria and Romania.

The international comparison will be supplemented by two detailed case studies – the case of supply-side subsidies for construction of rental housing in Poland and the case of indirect subsidies to promote owner-occupied housing in Hungary. These cases should demonstrate large differences in policies influencing housing consumption among transition societies and help understanding of the specific position of the Czech Republic. The selection of cases is not random: specific supply-side subsidies to support rental housing were characteristic of Poland and specific subsidies to promote homeownership were characteristic of Hungary. In the region Poland represented the model supporting, very significantly, non-profit rental housing, whereas Hungary

represented the model favouring especially owner-occupied housing. Most of the information presented here relates to the period of 1990-2002.

After the collapse of the socialist regimes, most reforms in the field of housing were consequences of wider economic and political changes. The reforms of the wider economy led to the liberalisation of construction material prices and privatisation of construction firms where salaries were liberalised. Energy prices were also liberalised, although some weaker form of price regulation was established under anti-monopoly legislation. These reforms facilitated the growth of the private economic sector that was supposed to replace the former public companies and public subsidies.

The wider political changes led to the restitution of part of the housing stock back to the original owners or their relatives (part of general restitution of property expropriated by communists during the previous regime) and decentralisation of power over housing policy from the centre to the local level (part of the wider decentralisation policy). Decentralisation with regard to housing policy was often accompanied by the transfer of public rental housing from state to municipal ownership. Fiscal decentralisation generally went far more slowly.

As these actions were mostly part of the wider reform package we can say, with some caution, that though these steps appeared in most of the countries, they were not directly related to housing policies and were more the intended or unintended consequences of wider economic and political changes. On the contrary, when housing policy appeared on the scene, the differences became much clearer.

2.2 Privatisation of public housing and tenure changes

Table 2.1 shows the tenure structure changes in selected transitional countries between 1991 and 2001. A glance at Table 2.1 shows us that many countries completely changed their tenure structure in favour of homeownership. Both relatively well developed countries such as Hungary, Slovenia and Estonia, as well those countries with lower levels of GDP such as Romania, Lithuania are among those where political representatives of the state decided to radically change their existing housing model in favour of homeownership. In other countries, such as the Czech Republic, Poland and Latvia, public rental housing remained the important tenure even in 2001. In Bulgaria, homeownership was already common in the previous regime and so no substantial tenure change took place there.

In countries with substantial tenure changes, right-to-buy legislation was passed and therefore public housing tenants received generally favourable rights to buy the flat under the conditions set by the central government. (In-

Table 2.1 Tenure structure differences during the transition

Country	GDP per capita Purchasing Power Parity (PPP) (in % EU-25)	Rental housing (in % of total housing stock)		Homeownership (in % of total housing stock)		Other tenure (in % of total housing stock)	
		around 1990	around 2000	around 1990	around 2000	around 1990	around 2000
		2004					
Slovenia	77.8	39	9	61	84	–	7
Czech Republic	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	–	–

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

deed in some countries, such as Estonia and Lithuania, the transfer was almost free-of-charge as a part of a voucher privatisation process). No matter that at the time 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 entire process was only slightly delayed. Poland and the Czech Republic did not pass right-to-buy legislation and, in this sense, municipalities were respected as the full owners of housing stock. These countries left it to the discretion of municipalities as to whether and under what conditions they would privatise their housing. We can thus distinguish three groups among the selected countries: fast privatisers, slow privatisers and the special status of Bulgaria.

Fast privatisers

Hungary, Slovenia, Estonia, Lithuania, Romania, Slovakia and Latvia (with some delay) belong to this group. In Romania, for example, all households willing to buy their dwelling were offered a qualified loan from the Savings and Deposits Bank, with a 25-year maturity and 4% nominal annual interest rate (for married couples under 35 years of age, the maturity was 30 years with a 2% interest rate). The price was very low, dependent on the date of construction. All adults permanently living and working in Estonia received 'privatisation vouchers' (according to the length of time they had worked in Estonia since 1945) and the purchase of public apartments was achieved mostly through such vouchers. Direct financial costs consisted only of the legal transaction fees, not exceeding 1% of the total price. Lithuania had an almost similar situation. The Privatisation of Municipal Flats Act was one of the

first acts of the independent Slovak Republic; in 1995 and 1998 it introduced amendments that strengthened the power of tenants wanting to purchase their flats. Prices, regulated by legislation, were low.

Slow privatisers

In the Czech Republic the Ownership of Apartments and Non-residential Premises Act (1994) enabled privatisation of individual public dwellings and allowed the establishment of homeowners' associations, but it did not introduce tenants' right-to-buy. A look at the Polish situation gives the same picture: dwellings were privatised generally at market prices although various discounts were granted. The extent of the discount, as well as the selection of the stock to be privatised, remained under the competence of the individual municipalities.

Bulgaria

Unlike other transitional countries, Bulgaria started its democratic development with a high percentage of homeownership, consisting of 91% of the total housing stock. The privatisation and restitution processes caused no significant change in tenure structures. During the previous regime, housing initially built to be state or municipally owned, was later sold to the tenants. Each tenant had the right to buy the dwelling after occupying it for two years and could benefit from soft loans from the State Savings Bank with a 2% nominal annual interest rate. Construction of public housing was subsidised by the state and prices were thus widely affordable. A new regulation was adopted in 1994, supposedly to prevent further privatisation of municipal housing stock and introduce more stringent criteria for its allocation, but this moratorium was cancelled in 1996.

In some countries (such as Poland, Czech Republic, Slovakia) the housing co-operative sector still commands a significant share of the total housing stock. This sector is sometimes labelled a 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 – housing cooperative members received significant rights of disposal.

There were also important differences in rent control systems indirectly influencing the tenure structure: for example, Estonia and Bulgaria abolished their central (state) rent control regimes till the end of 2005, whereas in Poland and the Czech Republic the state decided to retain strong tenant protection and rent control for all running tenancies up to the present day. In both countries rent control affected not only public housing but also private rental housing created from the restitution of property, thus starting the long, painful and fierce battle between the state and both private and public landlords.

2.3 Supply-side subsidies

If we leave public housing privatisation and tenure structure changes aside and look more closely at new housing policy strategies, we see that the differences between countries are again more obvious than similarities. While some countries were characterised by the lack of any direct supply-side subsidies in the field of rental housing, either due to insufficient public budgets (e.g., Bulgaria) or the prevailing neo-liberal economic dogma (e.g., Estonia), some other countries started new supply-side subsidy programmes and proactive housing policies. Poland, the Czech Republic and Slovenia (Hungary and Romania later on), directed a part of the housing subsidies at the construction of rental housing. New non-profit housing associations with the goal of offering 'social' rental housing were legally established in Poland and Slovenia and became especially active in Poland (see below). In contrast, subsidies for new rental housing were allocated exclusively among municipalities in the Czech Republic (see the next chapter for a detailed description of the Czech situation).

2.3.1 Supply-side subsidies: the case of Poland

As mentioned above, Poland is an example of a country that explicitly did not stop its supply-side subsidies at the beginning of transition (continued in the generous support of cooperative housing till the middle of 1990s) and later transformed these subsidies into support for new non-profit housing (inspired mostly by the French system of HLM). The Polish supply-side subsidy system is unique in the region and this specificity may be of crucial importance for understanding the specificity (or conformity) of the system applied in the Czech Republic. In the region Poland represents the housing model significantly supporting non-profit rental housing. It is necessary to know more details of this kind of support to relate it to the particular situation in the Czech Republic.

In 1994 a complete reform of rental housing took place in Poland. From 1994, *gminas* (municipalities) have been able to set their own rents up to a maximum of 3% of the unit's replacement value. The replacement value is set quarterly by edict of the *voivoda* (chairman of the regional council) as the average current replacement value (based on current construction costs) in the region (*voivodship*). It has been argued that rent equal to 3% of replacement value per year would cover all maintenance and renovation costs. Under the reforms, part of the *gminas* rental stock would be designated social housing for the lowest income households and households with a high measure of social need (household incomes under the living minimum or in relative poverty). These flats should be of a lower technical quality and their amenities should be of a lower standard. The rental contract in social housing flats is

concluded for only a pre-defined time period (usually one year) and the rent is much lower than in other *gminas* flats.

The 1995 Act on Selected Forms of Support for Housing Construction created the National Housing Fund. The Fund is financed from subsidies from the state budget, interests on extended loans and credits, interests on Fund deposits held with banks, donations and repayments of credits. Its housing subsidies may have only the form of a preferential loan and may be allocated only among social housing associations (see below) and housing cooperatives for the construction of rental dwellings. The *gminas* can obtain the loan only for the installation of the technical infrastructure associated with housing construction but not for housing construction itself. The loans may cover maximum of 70% of the project costs. According to the Act the interest on the loan cannot exceed the discount rate of the National Bank of Poland. By further edict of the Ministry of Finance the interest rate for new rental construction was set at 50% of the discount rate. Dwellings in buildings constructed using a preferential loan from the Fund cannot be turned into private property. The Minister of Physical Planning in co-ordination with the Minister of Finance defined the specific rules and procedures for awarding preferential loans:

- construction costs cannot exceed the replacement value per m² set quarterly by edict of the *voivoda*, taking into account the size of the residence, the structure of the housing stock and other factors;
- the applicant must have a suitable guarantee (mortgage) of repayment;
- new rental flats must fulfil explicit provisions on the insulation of walls, floors and ceilings to conserve energy (heating), and the area of the flat must be higher than the normative area indicated in the edict;
- the National Housing Fund can amortise 10% of the construction costs if the building was constructed on time and according to the conditions set forth in the credit contract. (This is the only financial aid in the form of grant.)

One of the most important contributions of reform concerned the introduction of a new type of social housing operator. Social housing associations (TBS, *Towaryzystwa Budownictwa Społecznego*) were established by the above-mentioned Act of 1995. A TBS can take various legal forms: limited liability company, joint-stock company or cooperative of legal persons (but not physical persons who could set up the housing cooperative). In fact, more than 90% (probably more than 95%) of new housing associations operating in Poland now are in the form of limited liability companies. A TBS can be started by a *gmina*, and in fact more than 90% of currently operating associations were started by *gminas*. Even when a TBS is set up by another entity, the *gmina* or *gminas* on whose territory the TBS operates has/have the right to appoint representatives to the Supervisory Board. A TBS cannot make a profit (it does

not pay income tax), its status and rules (articles) and all its changes must be accepted by the President of the State Office for Housing and Urban Development. Its primary function lies in the construction and management of rental housing units. In addition to their main activity the association may also purchase dwellings, carry out repairs, lease commercial space in buildings operated by the association, administer buildings under commission for third-party owners (*gminas*), and carry out other activities connected with the construction of housing and associated infrastructure.

The rents in TBS housing are regulated and set by the Gmina Council. The rent cannot exceed 4% of the replacement value of a dwelling set by the *voivoda* in its quarterly edicts and the sum of rent payments from all dwellings owned by a TBS must cover all maintenance and repair costs, as well as the repayment of the qualified loan from the National Housing Fund (cost rent). There are explicit rules for allocating new rental flats too. A TBS can only rent a dwelling to someone if no member of the household has a legal title to another dwelling and if the total household income does not exceed the average monthly salary in the given region (set by the Chairman of the Central Statistical Office for every region biannually) by more than: (a) 20% in a single-person household, (b) 80% in a two-person household and (c) a further 40% for each additional household member in larger households. Moreover, the tenant household must present to the TBS a declaration of average monthly household income for the past year once every two years. If the declared household income exceeds the aforementioned coefficient, the association may charge a free market rent. Since a TBS operates as an independent association not receiving financial grants from the public budget and repays the loan from rents, it tends to allocate its flats to households with economically active members with permanent and secure incomes (i.e., middle income households). Each TBS thus sets internal rules concerning the minimum household income.

TBS housing has been constructed in Poland since 1996. Up to the end of 2004 the construction of some 50,000 dwellings had started. The rents are relatively low and the new dwellings serve families with middle and lower incomes (though not those with the lowest incomes). After several years of operation, evaluation of the system is not straightforward. While there is a clearly positive result in the growing number of new dwellings rented out at affordable rent, generous targeting and mainly high public expenditures give grounds for the criticism and discussion of the system reform. The state budget supported the Fund by more than PLN 3,000 m. (EUR 700 m. in current value) and the bank behind the Fund (BGK) services additional debt following from loans from EBRD, IMF and EIB. The indebtedness of the bank (and ongoing request for additional contributions from the state budget) and indebtedness of some TBSs have become an important financial problem. Moreover, many tenants view their rent as their own repayments of the loans and are

asking for the right to buy their dwellings for the residual cost price. Though privatisation is forbidden by the law some highly indebted TBSs would welcome a change to the regime.

2.4 Demand-side subsidies

Up until 2002, housing allowances had been introduced in, for example, Poland, the Czech Republic, Slovakia and Estonia (part of the subsistence benefit). Bulgaria introduced only a special type of energy allowance (extended during winter and covering part of heating expenditure) and Romania introduced no housing allowance in this period.

If the housing allowances of the selected transition countries at the beginning of the 21st century had some common feature, it was their marginal significance. Their role was limited to income maintenance for the lowest income families, rather than being an effective demand-side housing policy instrument. Many restrictive conditions demonstrate this. Two types of income ceilings can be distinguished: implicit and explicit. Implicit ceilings arise from the formula used for calculating the housing allowance, whereas explicit ceilings are set strictly by the Act. Housing allowances in Poland, Slovakia, the Czech Republic and Estonia included implicit or explicit income ceilings. In 2002 the explicit housing expenditure normatives (notional expenditures) were also applied in almost all the above-mentioned countries, except for Poland and Estonia. Notional costs were often set at a low level, reflecting the situation in the 'privileged' regulated rental sector. Households living in the free market rental sector (paying market price for their housing) were thus generally excluded from any effective help through the allowance. In Estonia, however, real housing costs were taken into account although they were limited by ceilings (maximum values); such ceilings were set by the municipalities. In Poland real housing costs were also included in the calculation of an allowance with only indirectly set ceilings (comparable costs in municipal housing).¹³

The normative rate of burden of a housing allowance is defined as the share of household income that a household is expected to spend on housing. In other words, it sets the minimum financial contributions of a household to its housing expenditures not directly (in absolute values) but indirectly in a form of a percentage of the total household income. In the Czech and Estonian models the normative rate of burden varied according to the compo-

13 Notional housing expenditures are rarely applied in EU housing allowance models. Instead, the ceiling (maximum costs) is often used while actual costs are taken into the calculation of benefit. Above the level of the ceiling the household must meet all other expenditures from its own resources.

sition and size of the household (due to their connection to the concept of a subsistence level). In the Polish model the coefficient varied according to income level. However, in all analysed CEE models, the rate did not increase with the level of housing costs (assuming constant income), which means that there was no differentiation according to the level of rent (being generally higher for better equipped and better located flats).

The 'taper' shows the amount by which housing allowance decreases when the income of a household increases by one currency unit. In most of the analysed countries, the taper was relatively gentle and only the Estonian model with its 100% taper was an exception. The Estonian allowance thus might lead to a substantial poverty/unemployment trap. With the exception of Poland, housing allowances were paid from the state budget. In Poland the *gminas* (municipalities) were mainly responsible for covering housing allowance expenses, but they obtained a grant from the state budget, calculated according to two relatively complex formulas. On average, they received a subsidy equal to 50% of the total payment duty. A brief comparison of the models is contained in Table 2.2 (Bulgarian energy allowance excluded).

2.5 Subsidies and role of the state in homeownership sector

Table 2.3 shows the outstanding residential mortgage balance as a share of GDP in selected countries in 2003. As it is clear from the level of mortgage debt the role of market-based housing finance varied greatly between countries and was not simply influenced by GDP per capita or national homeownership rate.

Until 2002, many countries established state housing funds to channel the international donations and budget contributions to support the purchase of owner-occupied housing or private housing construction (Slovakia, Slovenia, Estonia, Lithuania); various mediators appeared between the state and market, called the National Housing Agencies (Romania). The guarantees and preferential loans were extended, for example, by the Estonian Housing Fund (before its abolition in 2001) to young families with children and tenants in restituted housing; the *KredEx* fund provided loan guarantees to young and employed professionals. Slovakian State Housing Development Fund offered qualified loans (up to 80% of purchase/construction price) and grants (up to 50% of purchase/construction price). After its establishment (1996) the Fund fell quickly into the debt as many households were eligible for the support. In later years the conditions for the subsidy allocations changed.

Romania established the special legal person, the National Housing Agency, instead. The Agency acted both as a developer and loan-funding institution. As a public interest institution, it approved contractors, supervised the

Table 2.2 A comparison of selected CEE housing allowance models – situation in 2000-2002

	Housing allowance is a separate benefit in social system designed particularly to cover housing costs	All tenures are eligible for the housing allowance	Explicit or implicit income ceilings for housing allowance application
Czech Republic	Yes	Yes	Yes, explicit (as a multiple of the household's subsistence level)
Estonia	No (a common subsistence benefit was introduced to cover all primary needs)	Yes	Yes, implicit (as household's income after payment of limited housing expenditures must remain below the subsistence level)
Poland	Yes	Yes (but there are important limits in cases when household is not living in municipal rental housing)	Yes, explicit (as a percentage of the lowest retirement pension)
Slovak Republic	Yes	Yes	Yes, implicit (emerging from the formula used for housing allowance calculation)

construction process and, finally, sold the units to eligible households. Sales were made in cooperation with commercial banks that issued a 'solvency certificate' for each applicant showing that he/she is able to repay a loan. Special arrangements enabled the Agency to keep its dwelling prices lower than market prices (land is provided free of charge by municipalities, the occupier is exempt from property tax and building permit issue costs are covered by the Agency). Tax relief (on interests from mortgage loans) was introduced in the Czech Republic, Poland, Baltic States and Hungary but did not appear in Slovakia and Slovenia.

Another public subsidy coped with the 'old loan liabilities' of former state banks, mainly in those countries with larger volumes of private (Hungary) or cooperative (Poland, former Czechoslovakia) housing loans extended during the previous regimes. Solutions to the problem varied again in countries: in the Czech Republic, Slovakia and Poland the state covered fully or a substantial part of the difference between the new market and the original fixed interest on old loans, (in 2000, about 40% of Polish housing expenditures still addressed this problem), whereas Hungary applied a programme of preferential loan buy-down.¹⁴ The highest public expenditure to cover 'old loan liabilities' (expressed as a percentage of state budget) was probably in Poland, where the dominant state PKO BP bank subsidised housing lending till 1996.

The state had also another important role in this field: to undertake the

¹⁴ About three-quarters of the outstanding 'old' loan balances were paid off in Hungary (Struyk, 1996, p. 37).

Which form of income (net or gross) is used for the eligibility test or for the housing allowance calculation? Are other social benefits included?	What housing expenditures are taken into account for housing allowance calculation?	Who provides financial resources for housing allowance payments?	The share of households receiving housing allowance from total number of households
Net income, including illness and retirement benefits, unemployment benefits, parents' benefits, care benefits, child benefits	Normative housing costs (part of a subsistence level) differentiated by size of household	State	7.6% (December 2000)
Net income, including social benefits with a few exceptions: one-time benefits, certain benefits to disabled persons, child benefits	Real housing costs to the extent of the standard allotted living space and to the limits established by local authorities	State	12% (in 2001)
Net income, including social benefits, with a few exceptions: one-time benefits and social transfers for orphans	Real housing costs to the extent of the standard allotted living space (limits are applied mainly for households living in market rental sector)	Both state and municipalities	7.6% (in 2000)
Net income, including other social benefits with a few exceptions: one-time benefits, social assistance	Normative housing costs calculated on the basis of allotted living space for the household multiplied by average rent, maintenance and energy fees (per m ²)	State	4.2% (December 2001)

reform of the whole banking sector. Both gradual reforms (Hungary, Bulgaria, Romania) as well as radical reforms (Czech Republic, Estonia) led to unexpected financial crises. In some countries such as Slovenia¹⁵ and Lithuania, the state kept its decisive influence in the banking sector far beyond 2000; in other countries the banks were privatised. The countries generally enacted laws permitting mortgage lending (often under a Law on Collateral, Banking Law or as a part of the Civil Code) but some of them did so only partially or much later. Foreclosure and eviction of borrowers-in-default with no requirement to offer them alternative housing was passed, for example, in Romania as late as 1999.

There were substantial differences among transition countries in their solutions to the 'tilt problem'.¹⁶ The Czech Republic mainly used interest subsidies (only very occasionally loans denominated in foreign currency appeared); Hungary deferred payment mortgages alongside interest subsidies; Poland introduced and extended indexed mortgage loans (dual-index mortgage) while in most other countries (including partially Hungary and Poland) loans denominated in foreign currencies became very popular. 'Exclusive' mortgage

¹⁵ About 45% of the economy remained in state hands and 40% of housing loans were allocated by the national Housing Fund in Slovenia in 2004.

¹⁶ Due to high inflation, lenders charge high nominal interest rates. This creates the affordability barrier in the case of annuity mortgage – high initial payments – but as time passes the loan repayment is eroded by inflation forming a still lower share of borrower income. High real value of payments at the beginning prevents many households from qualifying for mortgage loans.

Table 2.3 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)
Czech Republic	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)
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 the computation of balance though the figure was verified via the Estonian Statistical Office.

Source: European Mortgage Federation, World Bank, Eurostat, Housing Statistics in EU 2004, UN/ECE

banking (the establishment of special mortgage banks with the right to issue mortgage bonds) was introduced in Hungary and Poland. The legislation on mortgage banking was also introduced in some other countries (Latvia, Estonia, Czech Republic, Slovakia, Bulgaria and Romania) but without the requirement for the establishment of a separate specialised institution. This means that universal banks can obtain a license for mortgage bond issuance so long as mortgage banking operations and assets are kept in separate legal and accounting records.

In 1993 Poland established a special institution, the Mortgage Fund, in cooperation with USAID, EBRD and the World Bank; its goal was to provide additional liquidity to universal banks through securitisation of loans. However, as there was little demand for such a service the project did not gain much success and later on the World Bank and EBRD withdrew their resources. Other selected countries did not introduce secondary mortgage market facilities (although they were discussed in Romania).

The main differences among the countries appeared in the field of state support to housing saving schemes. The Czech and Slovak Republics introduced the housing saving schemes closed to the German *Bausparkasse* in 1992, Hungary in 1997, Romania in 2003 and Bulgaria in 2004 and though the law on *Bausparkasse* was passed in 1997 in Poland too, it has not yet been applied in practice. There are many variations to the system in the countries: systems differ in the premium bonus paid to savers, the minimum saving period to obtain the bonus, minimum saving period to withdraw savings, etc. In the

Czech and Slovak Republics the scheme became very popular with the public (and expensive for the state), but the opposite was true for the same system in Hungary, and in Poland the system existed only on paper. In Slovenia the National Housing Scheme was also established in 1999 but it operated within the existing banking system, interest rates on savings and loans were variable and a very low interest margin was left to meet the operational costs of banks so it was effectively a non-profit scheme.

2.5.1 Subsidies to promote homeownership: the case of Hungary

The Hungarian system of support for the acquisition of owner-occupied housing was unique in the region and this may help understanding of the specificity of the support for owner-occupied housing applied in the Czech Republic. Hungary represents the model of a housing policy mainly favouring owner-occupied tenure; it introduced special subsidies to promote homeownership and market-based housing finance.

In Hungary mortgage lending was relatively widespread even under the previous regime (though dissimilar to the mortgage loans commonly seen today). In 1989 the outstanding mortgage balance for residential housing represented 17% of GDP. In 2000, the mortgage debt fell considerably to just 1.5% of GDP. This decrease was due to a state programme aimed at motivating borrowers to pre-pay 'old loans', to the slow development of a new system of market-based housing finance, and also to the fall in house prices in the 1990s(!). The Hungarian housing market stagnated in the first phase of transition – in 1998 the average real house price was almost one half of what it had been in the final years of socialism (1989), a unique phenomenon in comparison with the situation in other transition countries.

At the start of 2000 the mortgage industry in Hungary was still marginal in significance, the mortgage credit portfolio equalled 130 million HUF, and outstanding mortgage debt constituted only 1.5% of the country's GDP. However, four years later, in 2004, the portfolio of unpaid mortgage loans equalled almost 2 billion HUF and the share of outstanding mortgage debt out of GDP had risen to 10% (!) despite the fact that in 2000 inflation in Hungary was still at the level of 10%, and in 2003 at the level of 5%. What was the cause of such accelerated growth? The efficiency of the mortgage industry, Hungarians' previous experience with financing housing through long-term loans, or the sudden increase in housing demand that had just been deferred for a time?

Admittedly, the macro-economic situation stabilised, inflation gradually decreased, housing prices, which had been falling for many years, began to grow again, and some form of competition appeared in the mortgage credit market. However, the country's GDP had already grown in the second half of the 1990s, inflation remained relatively high even in the first years of the new

millennium, and in 2002 the largest savings bank, OTP, still had a two-thirds (66%!) share of newly granted mortgage loans. Unfortunately, it is likely that the decisive cause was none of the above-mentioned reasons, but rather more the generous state subsidies. In 2000 the Hungarian government introduced several important state subsidies that signified a major incentive for mortgage financing. The constant political debate over the financially untenable nature of these subsidies, and the threat of their being abolished, created an increased demand for mortgage loans on the part of people who otherwise may not have been planning to buy or build housing, but did not want to lose out on the very favourable terms of the subsidies.

The first subsidy was a very generous interest subsidy on loans (called a subsidy to increase the demand for mortgage loans). It was equal to the yield from government bonds minus four percentage points (approximately 7.5% in 2000). In order for a borrower, and implicitly for a bank, to be able to participate in the subsidy programme, the interest on a loan could not exceed the government bond yield plus four percentage points. The margin for mortgage lenders (defined as the difference between the rate on government bonds and rate on mortgage loans) was thus limited to 4%, which, compared to the average profit margin of lenders in the Czech Republic (Sunega & Lux, 2007) was very generous. The interest subsidy was provided for the full term of credit repayment. The terms of subsidy enabled a flexible response to the change in market interest rates, while the client (creditor) at all times made repayments with a maximum annual interest rate of 8% throughout the entire repayment period.

The second subsidy was an interest subsidy on mortgage bonds, at 3% in 2000. It was eligible only when interest on a mortgage loan financed from the subsidised bond did not exceed the market bond interest rate by more than 1.5 percentage point. If, for example, the market interest rate on mortgage bonds was 11%, the maximum interest rate that could be set on a mortgage loan covered by the bonds was 12.5%. In such case the bank could request a 3% interest subsidy, which effectively reduced the bank's costs to 8% (and increased the margin to 4.5%). This interest subsidy was increased in 2001 from 3% to 6% and through a new mechanism it reached a record 10% in 2002! This subsidy is one of the factors behind the enormous boom in mortgage banking and large emissions of mortgage bonds in Hungary.

The third programme was a tax relief programme. First, it was possible to deduct annually 20% of the mortgage payments (both interest and principal payments) from income tax, but only to a limit of 35,000 HUF (around 180 USD). In 2001 it became possible to deduct 40% of the mortgage payments and the maximum limit rose considerably. In 2002 it became possible to deduct interest payments up to 240,000 HUF (around 1,000 USD), that is seven times more than in 2000.

The entire subsidy system was financially untenable in the long term and

contributed a substantial increase to the state debt and budget deficit. In December 2003 the government made the expected cuts. The interest subsidy on loans was reduced to 60% of the yield from government bonds, and the interest subsidy on mortgage bonds was reduced even more to 40% of the yield from government bonds. The maximum limit for tax deductions was reduced to half and a tax deduction was generally allowed only for the first four years of mortgage loan repayment. Although it was expected that there would be a radical decline in the interest in mortgage loans after these changes, the decrease was not that sharp – loans denominated in foreign currency substituted subsidised loans in HUF. In 2004 one half of newly granted mortgage loans were denominated in foreign currency. An interesting conclusion to the development of the mortgage market in Hungary is the fact that even in the mortgage loan sector miracles just do not happen. There was nothing more behind the ‘miraculous’ boom in the mortgage market in Hungary in 2000 than the state and the ‘visible’ hand of regulation.

2.6 Was anything shared among transitional countries?

Clearly, there were very different approaches to housing privatisation, rent regulation, the establishment of new supply-side as well as demand-side subsidies, housing finance tools and state support of owner-occupied housing. What, then, were the similarities? What did these countries on their way to EU share in common in housing reforms, if we suspend those changes that were the logical outcomes of wider economic and political reforms?

One fact is generally marginalised in comparisons of transition housing systems. Most international comparisons of state interventions in the field of housing consumption focus only on explicit subsidies, whether they are direct or indirect. Such subsidies are often well documented in public expenditure sheets, national budgets, and macro-economic statistics. However, one group of subsidies generally left unmeasured and definitely not demonstrated in official statistical figures comprises the economic (hidden) subsidies. These often concealed (and uncounted) subsidies are equal to the difference between the market and actual price for goods and services. In other words, people pay for a service (housing) less than they would pay under market conditions.

I have shown that there was no common shift in tenure structure during the transition among the selected countries. Although the mass privatisation of former public housing prevailed in the region at least two countries (Poland, Czech Republic) did not apply a right-to-buy policy. However, in all the countries analysed here, a substantial part of population received the same housing economic subsidy, either in the form of an owner-occupied flat pur-

chased for a very low or at no price, or in the form of rental housing with very low regulated rent. This hidden economic subsidy probably formed the main financial subsidy in the field of housing during the transition and its marginalisation may lead to a distorted picture of housing reform in those countries. The allocation of huge economic subsidies became the common feature of housing reforms in all the analysed countries; it is one of the detectable similarities.

Also evident is that central governments were reluctant to surrender control over the main levers that decisively influence the form of housing consumption. In spite of the proclaimed decentralisation of policy to municipalities, central governments did not want to be compromised by the reform programmes 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. In spite of the common rhetoric on the decentralisation of housing policy at the beginning of transition, in all the analysed countries this field remained decisively influenced by the state (central) policies. Later, this dominant central role weakened but the dominance of central decision makers in housing policies of 1990s was another common similarity among transitional countries (though poorly visible behind the decentralisation rhetoric and some legislative activities).

Taking it another step reveals another outcome. In the field of housing consumption the dominant states decided to allocate huge economic subsidies but eligibility for these subsidies had to be, logically, restricted. The state could not give the same level of economic subsidy to all existing and newly created households as then the state budget would end up bankrupt. Only the existing tenants, and especially existing tenants of former public housing, were those who could be labelled as the winners of housing policy transitions. The income and/or social situation of the eligible household was not important in this allocation process; the only criterion was the occupancy title. As the allocation of huge economic subsidies was not means-tested these subsidies probably increased the income and social inequalities in transitional societies (note, however, that this conclusion is not verified for all selected states).

There is another clear and now proven outcome of policies in selected transitional societies: the economic subsidies divided households into two very different groups. The 'insiders' enjoyed low housing costs and tenure protection (with no regard of their social needs or income levels) while the 'outsiders' were often left to the uncompromising market forces. Additional subsidies directed at outsiders (if any) were marginal, when compared to the hidden economic subsidies to insiders. This insider-outsider tension was, in fact, even more substantial because market housing was inflated by the lack

of incentive for insiders to move or rationalise housing consumption. Though this problem did not overflow into significant social conflict thanks to the traditional inter-generational transfer of housing privileges, it is obvious that the costs and benefits of housing reform were unequally distributed.

3 Housing conditions, housing policy and housing affordability in the Czech Republic during the transition

This chapter follows the international comparison of policy changes in selected transitional countries presented in Chapter 2 but it focuses on a more detailed description of the particular situation in only one of the countries included: the Czech Republic. The purpose of Chapter 3 is to describe the context in which housing policy in the Czech Republic was formed and reformed during the transition. The description derives from the theoretical framework specified in the first chapter; especially from the intention to look at the ideological (normative), institutional (path dependence), political and economical factors behind the evolution of the housing system. This chapter thus includes a description of the political, institutional, economic and demographic contexts as well as a description of the history of both social and housing policies applied in the territory of the current Czech Republic in the past. I also describe and discuss the changes in housing conditions (including tenure structure), housing policy, housing finance and housing affordability in the period between 1989 and 2005 in the Czech Republic.

The purpose of this chapter is to answer the first research question elaborated above. This question is as follows:

1. *What was the background to the development of the specific housing policy and housing system in the Czech Republic? What were the ideologies (norms), traditional problem solution patterns and institutional as well as political structures that might influence the formation and development of the housing system (including the formation of general social policy and its history)?*

By nature, this chapter is more descriptive than the previous one. The detailed information provided here will, however, be useful in the analyses of effectiveness and subordinated efficiency of housing policy in the Czech Republic provided in the next chapter and they will be especially crucial in detecting the factors that influenced state interventions in the field of housing consumption provided in the last chapter of this book. The context described here and the assessment of the efficiency and effectiveness of housing policy presented in Chapter 4 will be put together in the last chapter of the book.

3.1 Political and institutional context

At the very beginning of transition the political system based on one-party

dominance¹⁷ changed completely in favour of a multi-party system and democracy. As the 'leading role' of the Communist Party of Czechoslovakia had already been mentioned in the pre-1989 Constitution, such radical change included the preparation and introduction of a new written Constitution and Declaration of Human Rights; introduction of the new electoral law; and the establishment of new political (state) institutions (such as the new chambers of Parliament, the Constitutional Court and others). The Parliament of the Czech Republic (after the 1993 division of the former Czechoslovakia) is composed of two chambers – the Chamber of Deputies and the Senate (the Senate remained vacant for the whole legislative term and the first elections to the Senate were not held until 1996). "The Czech Republic has a parliamentary regime. This is by no means a banal assertion, at the very least for two reasons. The overwhelming majority of present-day Western consolidated democracies have a parliamentary regime, while by contrast the majority of the former communist countries have a semi-presidential regime. Generally, in a parliamentary regime, the formation of a government constitutes the fundamental link between the result of a legislative election and the policy of the executive power" (Novák et al., 2005, p. 10).

According to the Czech Constitution, following the parliamentary election a newly formed government is required to appear before the Chamber of Deputies within 30 days of its appointment and ask for a vote of confidence (Article 68). If the government fails to win the vote, it must submit its resignation (Article 73). "We may then say that the Czech Republic is one of the countries where an incoming government must necessarily have an explicit, formal legislative investiture... [this] makes the process of forming minority cabinets much more difficult" (Novák et al., 2005, p. 11). The parliamentary (and not semi-presidential) character of political system, the proportional electoral system to the main chamber (see below) and the necessity of investiture of the incoming government all have important consequences on political stability (especially the stability of executive power) and are, in my opinion, important in understanding the role that housing policy played during transition in the Czech Republic.

The electoral system for elections to the chamber with decisive legislative powers, the Chamber of Deputies, is founded on the principle of proportional representation. Only parties that pass the legal threshold of 5% of the votes on a nationwide basis can be allocated seats. Until 2002, seats were distributed on the level of the eight voting regions using the Hagenbach-Bischoff For-

17 Besides the Communist Party of Czechoslovakia (KSC), which led the political power pre-1989, several other political parties were officially permitted to exist during the previous regime. However, all of these parties had to agree to the leading role of the Communists and functioned under the control of Communist *nomenklatura* (known as the National Front framework); they were there more to mask the *de facto* one-party communist system than to represent any effective political opposition.

mula. The electoral regions were identical to regional government territories, that is seven regions and the capital city Prague. The unused votes for parties from the first scrutiny were carried over into the second scrutiny, which was calculated in a single nationwide constituency. Here the remaining votes cast for the individual parties from the regions were calculated and further seats allocated, once again using the Hagenbach-Bischoff Formula. If not all the seats in the Chamber of Deputies (200 seats) had been allocated after the first calculation of the second scrutiny, the remaining seats were allocated to the parties with the largest share of the remainder of the vote.

This system, with its five-percent legal threshold, prevented very small parties getting into the Chamber of Deputies. The legal threshold, however, was the only element that had a reductive effect on the party system. The system secured a relatively high level of proportionality among the parliamentary parties that managed to exceed the five-percent legal threshold. “This was the effect of at least three favourably adjusted variables. The electoral districts (regions) were very large, and so distortion of proportionality was kept to a minimum. If a small disproportion occurred in the allocation of the seats in the regions, it was reliably compensated for in the second scrutiny. As a result there were no instruments to enable easier formation of governments” (Lebeda, 2005, p. 109).

There was only one significant attempt at electoral reform. In 2001 the leading right-wing party and leading left-wing party (ODS – conservatives; ČSSD – social democrats) jointly produced an electoral reform bill in order to substantially strengthen the majority-forming effects of the electoral system. Ultimately it was not implemented as a consequence of a ruling by the Constitutional Court, which annulled the key parameters of electoral reform. Instead, in 2001 we saw the achievement of some ‘cosmetic’ amendments to the electoral system. The first change to the mechanism of seat allocation was the replacement of the original Hagenbach-Bischoff Formula with the D’Hondt divisor. The second reform variable was the legal threshold for the entry of parties into parliament. In the new system, however, the threshold for individual parties remained unchanged at 5% and the changes related only to the levels for coalitions (this meant that parties were not longer motivated to enter into pre-election cooperation). The third reformed variable was the number of scrutinies. As I mentioned above, the original electoral system used two scrutinies. Dropping the second scrutiny was related to the choice of voting formula – the D’Hondt divisor distributes all the seats directly at the basic level of the voting districts. Therefore there is nothing left to be carried over to a second scrutiny. The last primary variable to be changed was the magnitude of the districts. Instead of the original eight electoral districts, fourteen new districts were established, identical in borders with the new self-governing regional authorities.

“From the point of view of the overall impact on the proportionality of the

electoral results and the representation of individual parties, the new system has changed very little. There have been a few small shifts bringing marginal advantages to strong parties at the expense of the weak" (Lebeda, 2005, p. 120). For over ten years (1996-2006) the Czech Republic lacked an executive that was stable, enjoyed a majority and was capable of effective action mainly as a consequence of the prevailing proportional electoral system, the parliamentary character of the political regime and the necessity of government investiture. Since the elections of 1996 there have been eight successive governments, but not single one has fulfilled all three conditions.

The first Czech government, with Mr. Vaclav Klaus as prime minister, was installed on the 3rd of July 1992. After the federation ceased existence (January 1993) Mr. Klaus' government led the new independent Czech Republic. It was a coalition of leading right-wing conservatives (ODS) and small right and centre-orientated parties – Christian Democrats (KDU-ČSL, KDS) and liberals (ODA). At the time the coalition had a majority of 105 seats in the Chamber of Deputies. The main opposition was the Communist Party of Bohemia and Moravia (KSČM). The communists refused to convert to social democracy (as did former communists in other transition states like Hungary or Poland). "The communists were unacceptable to the other parties, and their coalition potential was almost non-existent ... The Czech Republic was in fact the only country in Central Europe where a comparatively strong and to a certain extent dogmatic Communist Party prevented a healthy alternation of governments for quite a long time" (Novák et al., 2005, pp. 47-48).

The year 1995 saw a substantial increase in support for the other left-wing party (social democrats, ČSSD). The 1996 parliamentary elections had put important changes onto the political map – growing support for social democrats who replaced the communists in the role of the main opposition party; and the end of stable majority Czech governments. The elections of 1996 ushered in the first two-year period of unstable and ineffective government. The minority coalition government of Prime Minister Klaus (ODS), again formed by the ODS, KDU-ČSL and ODA with a narrow minority of 99 deputies in the Chamber of Deputies, held on for about 18 months. The crisis at the end of 1997 effectively brought down the government. It was replaced by a second minority government headed by Mr Josef Tošovský as prime minister (independent, former governor of the Czech National Bank), which included a number of non-partisan members and representatives of new small right-wing orientated party (US) and the KDU-ČSL, and was supposed to be a caretaker government to bridge the period up to the early elections at the beginning of the summer of 1998. Not even these elections, however, led to a solution. A majority government could not be formed nor a stable executive established for the following four-year term. Politicians responded to this situation with the somewhat unconventional 'Opposition Agreement' concluded between the governing ČSSD and ODS, the strongest opposition party.

This was the basis for the third minority government, this time headed by Mr. Milos Zeman (ČSSD); it was also the first government led by left-wing political party (social democrats) since 1992. While stable thanks to the agreement, it was hardly capable of any effective action.

The 2002 elections once again resulted in a stalemate. While it proved possible to form a majority government coalition of three parties (ČSSD, KDU-ČSL and US, led again by left-wing social democrats), the majority in question was the smallest possible (101 deputies). This government survived for two years. Its prime minister, Mr. Vladimír Špidla (ČSSD) resigned following the extreme failure of the ČSSD in the European Parliament elections. In the summer of 2004 a new government was formed under Prime Minister Stanislav Gross (ČSSD) composed of the same three parties and once again with the smallest majority possible (101 deputies). At the beginning of 2005 this government was replaced by the same coalition under Prime Minister Jiří Paroubek (ČSSD) with the same majority of 101 deputies.

The parliamentary election of 2006 led once again to an unstable political situation. No political party had been able to establish a majority coalition government and due to growing tensions between two main political parties (left-wing ČSSD and right-wing ODS), there was only a little space between them for mutual agreement in the minority government. In fact, after the 2006 election, the Czech Republic had no government for six months, though in that time there was an attempt to establish one (by ODS members). This attempt failed when the government did not get the necessary majority support in the Chamber of Deputies. Only thanks to two former ČSSD deputies, who decided to support another right-wing oriented coalition government of ODS, KDU-ČSL and Green Party, was it possible to establish the new government with a weak majority of two votes.

Since 1996 the lack of effective and powerful government (i.e., a government that can effectively fulfil its political programme) has been the main feature of the political situation in the Czech Republic. Right-wing ODS led the governments in the period 1992-1998; left-wing ČSSD led the governments in the period 1998-2006. Due to the proportional electoral system, the governments were always coalitions; for example, the relatively small centre-orientated party of Christian Democrats – KDU-ČSL – has participated in all governments since 1992 with no regard to whether these governments were led by ČSSD or ODS.

Another characteristic feature concerns ideology. As Matějů & Vlachová (1998) have confirmed, the vast majority of Czech adults have been able to place themselves on the political left-right scale. Novák comments, “Most importantly, with gradual crystallisation, this left-right orientation is acquiring content. Research has shown that in Czech society self-placement on the left-right scale has been quite stable in a bell-shaped distribution with a slight deflection to the right since 1991... Behind this stability of self-declared po-

litical leanings, however, a significant development of attitudes related to the left-right axis has taken place. In their attitudes and values, Czechs have been leaning slightly to the left for several years” (Novák *et al.*, 2005, p. 52).

The transition has also been connected with profound reforms of existing institutions. Even if we put aside those substantial institutional changes connected with economic reform (end of planning economy and establishment of markets, stock exchange, private economic subjects of different legal form, transfer of production of industry and services via privatisation and restitution from state to private hands), dozens of formal changes touched all fields of public administration and intervention: local government (establishment of local governments – municipalities and regions – and decentralisation of power to the local level), the police (fundamental reform of police and secret services), the army (substantial reform of army structure leading, finally, to an establishment of professional army), central administration (closing some ministries and establishment of new ones), education (reforms of secondary and university education), research (cessation of many research institutes and partial reform of scientific research), and health care policies (social policy, tax policy, etc). Besides many other goals, these changes were aimed at ‘clearing’ the public administration of former collaborators of the communist secret service (especially in high posts in police, army, secret service, science, education, public administration) and ‘freeing’ industry, the public administration, education, research institutes and others from the ballast of communist ideology (by dismissing people whose posts were especially related to the assurance of appropriate communist morale). A description of all these institutional changes would be enough for a full historical monograph; as this is not the goal of this book, I will concentrate only on those changes that were connected with housing.

As mentioned above, the former ‘hard-line’ communists did not transform themselves into a more democratic left-wing party and remained organised as a political party, embedded by rhetoric and day-to-day politics in the past (praising the former communist regime; reflecting the nostalgic yearning for communism present among many retired people). Though they received at the beginning of transition, a relatively high share of parliamentary election votes and until 1996 they always ranked in second place after the winning political party, thanks to this they were paradoxically cut off from real political power. Among the important goals of institutional reform this one goal (exclusion communists from political power) was fulfilled more successfully here than in countries such as Hungary or Poland (though some institutions, namely courts, are often denoted as unreformed even today). This does not mean that the communists disappeared. They were only relatively successfully (bearing in mind that there are always some exceptions) cut off from the work in public administration, army, police and other public institutes as well as in the educational structures and central government. They often

used their former contacts (social capital) as well as their wealth stemming from their considerable legal and illegal incomes acquired during socialism to become influential economic actors in the first phases of transition. In many ways, the communists were best prepared for changes in the regime and often successfully used their accumulated economic and social capitals under market conditions.

However, institutions in the broader sense also include social norms, patterns of behaviour and expectations; not only those institutions that have a clear material existence and hierarchy. Change in the less visible institutions can hardly be expected to be achieved just as quickly. The most common strategy regular people employed to survive the socialism of 1970s and 1980s (economic shortages, low incomes) is reflected by the following proverb: ‘Those who do not prey on the state prey on the family’. A commonly held norm during the communist regime was that one could barely survive without ‘preying on the state’, or taking part in illegal ‘black markets’ and informal networks (clientelism) or often without straightforward corruption. Social networks and bribes were essential for getting a good job, a higher standard of health care, a state rental flat, for ensuring a good education for children, even for such mundane things as being able to buy oranges or bananas in the shops. Unfortunately this sad proverb characterised the personal ‘strategies’ people employed in most transition countries even long after the change of the regimes. Clientelism (influential informal networks, the establishment of powerful lobbying networks with significant influence in the political decision-making process), the culture of breaking laws (illegal incomes, black markets, shadow economy, ‘preying on the state’) and wide-scale corruption are still main barriers to the improvement of efficiency of the functioning of the entire social and economic system in the Czech Republic. The Transparency International CPI Index 2006 measurement of perception of corruption in 163 countries ranks the Czech Republic ranks at 46th – 48th position, far behind the overwhelming majority of ‘old’ EU member states (with the exception of Greece or Italy). The judicial process is still time-consuming. In 2005 civil disputes took on average 15 months compared to six months in 1989 (*Statistický přehled soudních agend*, 2006).

3.2 Economic context

The economic context of the early transitional period has been accurately characterised by politologist J. Rupnik in the introduction to one of the most influential evaluations of the first decade of transition in the Czech Republic (Večerník & Matějů (eds.), 1998, pp. 13-14):

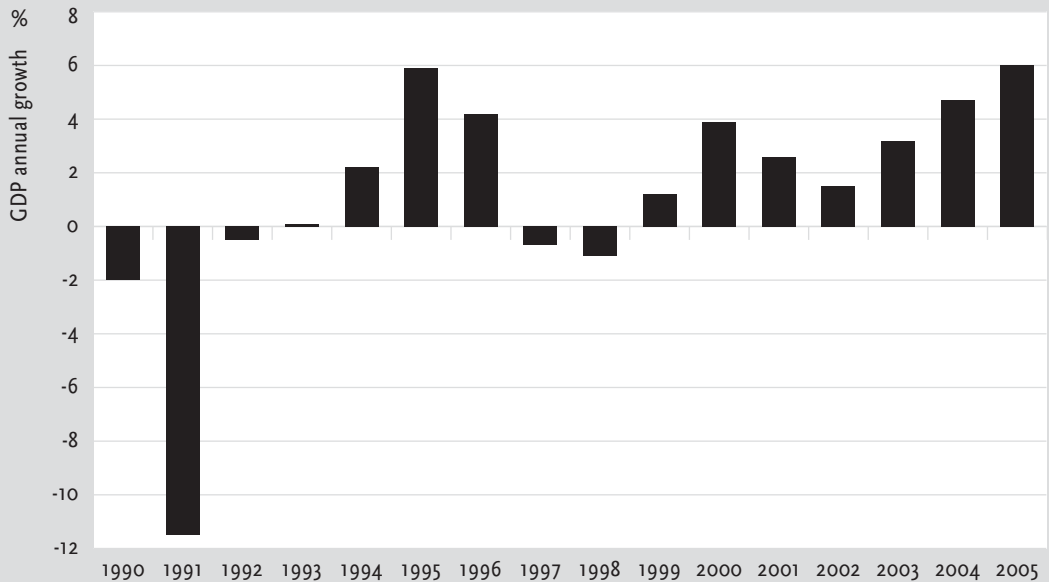
“The Polish and especially the Hungarian left enforced a truly liberal eco-

conomic policy whereas the Czech right got stuck in social-democratic, consensual politics, the consequences of which are today well-known. This policy, together with radical free market rhetoric was economically counterproductive but highly successful politically...An absolute majority of Czechs are in favour of a strong and socially generous state. In other words, 'right-wing liberalism' was acceptable to Czech society only when it was limited to rhetoric and accompanied by social-democratic practice. The *bon mot* of Jiří Večerník from 1996, 'think left, vote right', accurately captures the Czech situation of the 1990s."

After 1989 the denationalisation of the entire economy took place. Privatisation of enterprises and services was divided into 'small privatisation' of shops and business premises, and 'large privatisation' of state enterprises. The restitution of property expropriated by the communists since 1948 (for small firms since 1955) represented the third form of factual privatisation. The most striking feature was a form of 'large privatisation' called voucher privatisation. Voucher privatisation began in 1992 when all adult Czech citizens received equal numbers of vouchers to use for the purchase of stocks in former state enterprises. It was the reflection of the ideals about equality (and also populism) of the early Czech transition governments – everyone should be given the same opportunity to become successful on the emerging stock markets. From the very start there was strong public support for this specific form of privatisation, including from highly educated people. However Večerník & Matějů (eds., 1998) state that "voucher privatisation has undoubtedly shaken up the structures of ownership, but has remained far from achieving the desired state...Those most successful in privatisation were those individuals who, thanks to their 'revolutionary ethics' did not hesitate to capitalise upon legal loopholes and were able to profit by avoiding the entanglement of ownership rights".

Most vouchers were invested through different private investment funds which, in the course of time, were often transformed in such a way that allowed abuse of the invested capital for the enrichment of individual funds' managers. Moreover, fragmentation of the enterprises' ownership structure established by 'millions of investor' during voucher privatisation gave a key position in privatised enterprises to the managers who also often began following their own selfish interests (i.e., contrary to the interests of fragmented inactive owners). The 'large privatisation' of some enterprises was not done solely through vouchers but often through a combination of various methods. However this combined 'privatisation strategy' was again prepared by the managers themselves. Večerník and Matějů state, "We can only speculate as to what extent the chosen method was based upon an open and sincere reliance on essentially blind economic laws and to what extent the tacit transfer of state property into the hands of its previous direct or indirect

Figure 3.1 GDP annual growth in the Czech Republic, 1990-2005 (in %)

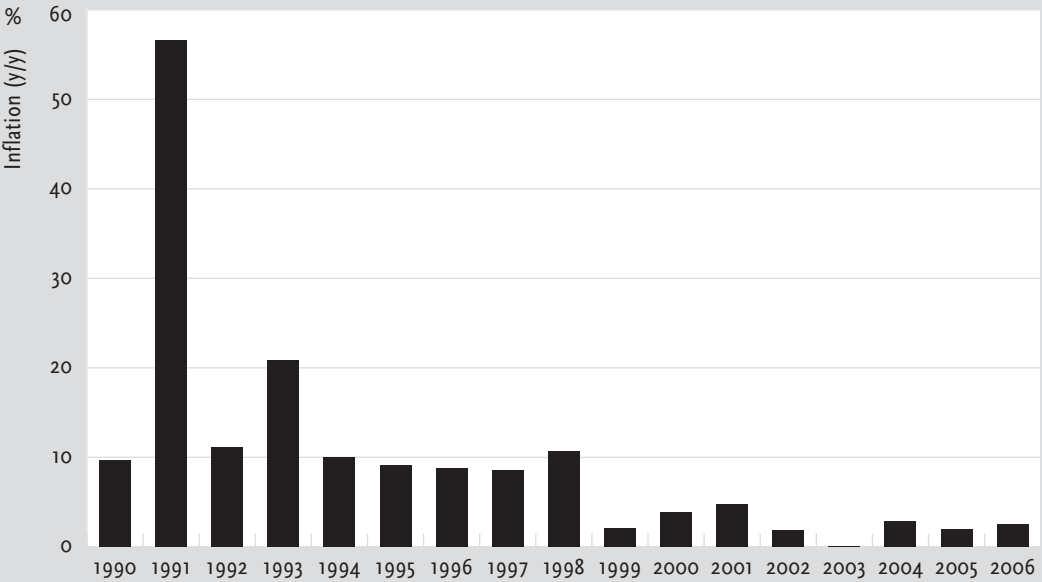


Sources: Czech Statistical Office, Ministry for Labour and Social Affairs, World Bank

managers had been expected.... Rather than human capital and high ethical standards, previous positions, contacts and information, detailed knowledge of the given organisation, or simply belonging to certain closed networks of people were more decisive for the success of a proposed privatisation project" (Večerník & Matějů (eds.), 1999, pp. 77, 84).

Another important feature of the first decade of transition was, on the one hand, the effort to privatise state enterprises in private entities as soon as possible but, at the same time, to keep the majority state portion of ownership in the banking sector, which owned many private investment funds active during voucher privatisation. This system has been called 'state capitalism' (Mlčoch, 1997, p. 110) or 'banking socialism' (Večerník & Matějů (eds.), 1999, p. 78) and it had, in the first instance, especially important consequences for the labour market and wealth redistribution (see 'social policy' below), and, in the second instance, on the sustainability of economic growth in the Czech Republic. After the first necessary economic recession in early 1990s, a short period of economic growth was interrupted by another economic recession in 1997-1998 (Figure 3.1). Though there is no consensus on the causes of the second unexpected economic recession (it did not appear in any neighbouring countries such as Slovakia, Hungary or Poland), the crisis in the unsustainable soft system of 'banking socialism' is often mentioned in this context (Večerník & Matějů (eds.), 1999; Večerník, 1998). The following two figures (3.2 and 3.3) show the development of rates of inflation and unemployment during transition in the Czech Republic.

Figure 3.2 Inflation in the Czech Republic, 1990-2006 (in %)



Source: Czech Statistical Office

3.3 Social policy

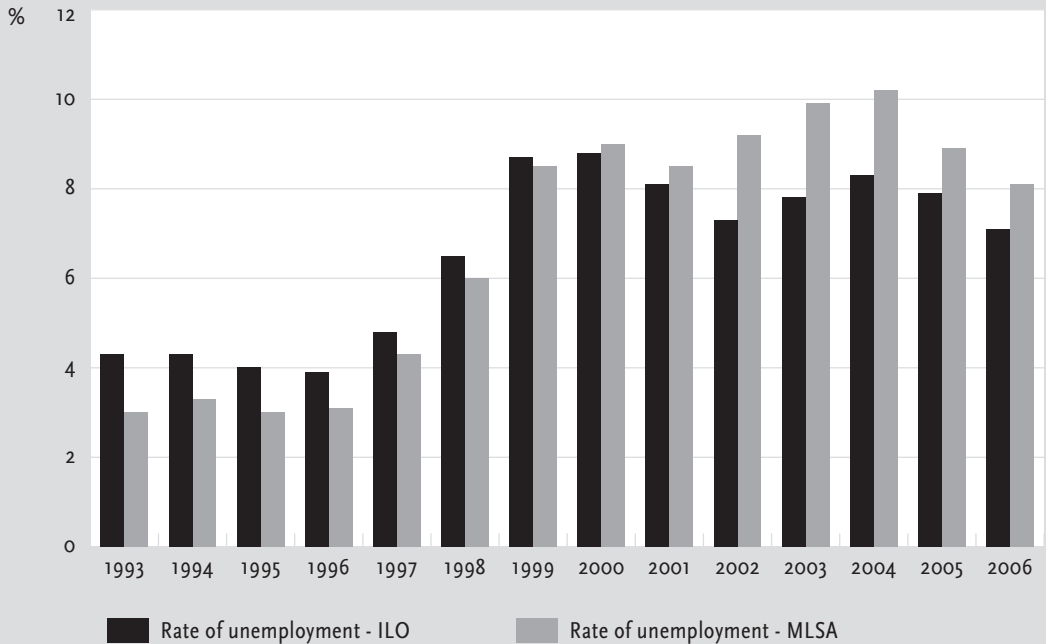
Knowledge of social policy and its development, including the long-term social norms incorporated in policy systems is crucial for understanding the development of housing policies, housing systems. As housing policy forms, in fact, part of social policy, here I will provide a description of the development of social policy in the territory of the Czech Republic that delves more deeply into the history; since the end of WWI and the establishment of the 'first' independent Czechoslovak Republic.

After the Russian Bolshevik revolution (1917) and WWI (1918) there was a clear general shift of political preferences to the left throughout the whole of Europe, including the new independent Czechoslovakia. However, 'socialism' in Czechoslovakia also had other roots: a general disregard for nobles closely related to the former Austrian-Hungarian Empire who were mostly of non-Czech nationality¹⁸ and a general ill feeling towards the Catholic Church, the religion closely connected with the Habsburg dynasty. Both the nobility and the Church owned significant portions of Czech land.

The so called 'social question' also formed a significant part of the dis-

¹⁸ During the 30-year religious war, the original, mostly protestant Czech noble class was fatally decimated after the Battle of White Hill in 1620 when it was defeated by foreign arms supported by the Catholic Church; later on the representatives of Czech nobility were executed or forced into exile and their property was distributed among the 'new' foreign Catholic nobles arriving with the intervention army.

Figure 3.3 Rate of unemployment in the Czech Republic, 1993-2006 (in %)



Sources: ILO – International Labour Organisation; MLSA - Ministry for Labour and Social Affairs

course provided by the new political elite long before 1918: the first president of Czechoslovakia, former professor of sociology at the Charles University – T. G. Masaryk – wrote a monograph entitled ‘Social Question’ and the same title was used by future minister of Finance K. Engliš for his own monograph written during the WWI. Shortly after the establishment of the new republic in 1918, the eight-hour working day had already been introduced. The first political election in 1919 was won by left-wing parties (Czechoslovak Social Democratic Party and Czechoslovak Socialist Party). The right-wing Agrarian party also took part in the first Czechoslovak government but only due to the effort to exclude all German political parties from executive power (Germans formed about 25% of population of the new independent state). A number of strikes were organised by radical workers of the time and the General Strike of 1920 was suppressed only through violent interventions by the army and police. In 1921 the Communist Party of Czechoslovakia was formally established.

Land reform was orientated mainly against the nobles (e.g., Schwarzenberg, Czernin, Colloredo-Mansfeld, Lichtenstein or Habsburg) and the Catholic Church (the biggest land-owner in the territory of Czechoslovakia with about 500,000 hectares of the land). Several reforms with hidden nationalistic goals (directed *de facto* against landowners of German and Hungarian origins) were passed between 1919 and 1920; all agricultural land with an area more than 150 hectares was ‘annexed’ by the state (almost 30% of the total area of the new state). ‘Annexation’ did not mean expropriation but the disposal rights of

land-owners were greatly reduced. Afterwards the annexed land was gradually purchased from the landowners by the state for the usual prices of 1913-1915 (i.e., at pre-WWI prices). Due to the fact that in the post-WWI period of hyper-inflation land prices were much higher, such a 'purchase' was, in fact, an expropriation of land (Průcha *et al.*, 2004, p. 85). The purchase of annexed land had not finished even 15 years after the law had come into force and in the mid-1930s large parts of annexed land (about 56%) remained in the ownership of the original owners; purchases stopped and further progress was postponed for another 20 years (i.e., up to the 1950s).

Collective agreements between representatives of employers and employees (trade unions) became common after 1918 though they had no legislative basis. The power of trade unions grew quickly. The membership of the most influential trade union (OSČ) increased from 75,000 in 1918 to 856,000 in 1920. The trade unions asked for larger 'socialisation' of the economy, expropriation of private industry, and even the first president of Czechoslovakia, T.G. Masaryk did not oppose this idea in 1919 (although he stressed the pre-conditions). The social insurance system was improved by reducing the share of insurance premium paid by the insuree, by aggregation of small insurance companies into financially stronger groups and by extending the period of eligibility for illness benefit. By 1918 the state unemployment benefit had been legally introduced to meet the challenge of the poverty of unemployed people (but the benefit was not universal as it was allocated to only about 50% of the unemployed). Rent regulation for all current rental contracts was also introduced in 1918. The state debt quickly increased, partly due to this new social legislation.

After the 'deflation crisis' of 1921-1923, the 1920s were a period of significant economic boom and this helped to blunt revolutionary aspirations (though the communists, especially in the Czech territory remained very powerful, often coming in second in parliamentary elections). Only a few new social laws were passed during the boom (the right to equal leave for all workers, pension insurance for workers) and, generally, social policy began getting less generous. The economic depression (1933-1938) meant a return to substantial state interventionism – support for monopolisation, *numerus clausus* in many industries, economic protectionism, export subsidies as well as higher wealth redistribution (especially in the field of unemployment benefits). However, with the exception of a reformulation of unemployment benefits there were no additional programmes to target the growing unemployment, poverty, income differentiation, and housing foreclosures (in villages). This was also due to the growing state budget deficit (Průcha *et al.*, 2004). The social and economic consequences of the economic recession remained very painful and became an important part of the collective memory in Czech society.

As Krebs *et al.* (2005, p. 90) mentioned, in post-WWII socialist Czechoslovakia (1948-1989) there was no social policy whatsoever. In general, there were

only the activities of the monopolistic state in all fields of human life – including social matters. As Krebs mentions (p. 91), the term ‘social policy’ disappeared from official vocabularies at the beginning of 1950s because from the ideological point of view under the new socialist order there would be no social problems that such policy could potentially address (of course in reality those problems did exist but they were hidden by propaganda or over-employment). The wide-scale and non-transparent redistribution of wealth reflected the officially proclaimed egalitarianism (not social justice) and this led to the confusion between the economic and social spheres. As Krebs explains, “Social policy has been deformed especially by the fact that these were only activities of the state that had a monopoly on any interventions in the social field. The role of other actors has been suppressed (family, citizen) or completely suspended (charity, church, non-government organisations). The whole system was centralised and was broadly undemocratic” (Krebs et al., 2005, p. 91).

The state had total monopoly. It controlled all economic activities and all activities in the social field. This was a tool used to make people completely dependent on the state and to create in them a mood of ‘adoration of the state’. Social paternalism was an instrument of both social security and political control (Večerník & Matějů (eds.), 1999, p. 198). Only the state could give people such ‘gifts’ as employment, low-priced milk or bread, low-cost housing, low interest loans on buying furniture or a car, free education or free health care. The state became a substitute for other religion symbols; it accumulated all powers in social, political and economic life (and consequently also in the social field) and was vindictive to any other competitors, especially those coming from underneath. Official egalitarianism did not, however, exclude distribution of certain important privileges to people who represented important pillars of the state and the communist party hegemony (the policy, army, secret service, ideologists, *apparatchiks*, *nomenklatura*).

Financing for all of this was provided exclusively by the state budget. Therefore after two decades of socialism (starting in the 1960s and continuing especially in the 1970s and 1980s) the system became increasingly characterised by shortages, a decrease in service quality, corrections to original goals; in short: crisis. Although equal, people began being equal more in their poverty than in their affluence. For most families it was barely possible to cover household expenses on one salary (and therefore women were forced to return to the labour process very soon after the birth of their children). Allocation of state rental flats took longer and longer (and the numbers of people in forced cohabitation grew, especially during the population boom of the 1970s). Meanwhile, the consumption of goods increasingly perceived as standard in the West were more often considered a luxury in communist Czechoslovakia (e.g., quality meat, tropical fruits, an unpolluted living environment or poor quality cars).

During communism it had become almost folklore to blame the state for any type of shortcoming (it was logical – the state was everywhere so who else could you blame?) and the dependence on paternalistic and monopolistic ‘omnipotent’ state had actually become a powerful social norm. The communists succeeded in transforming large numbers of free and independent individuals with personal ambitions and values into a highly state-dependent submissive mass that ultimately sold out to a demonic contract. This contract said that the people’s tolerance of ideological, cultural and political suppression would be given in exchange for the other party to the contract, the communist state, promise to continue providing them with ‘gifts’ – employment (where the work was more pretence than real), free housing, free education, free health care and others.

This powerful social norm, dependence on the ‘omnipotent’ state, has been shown to play a significant role during the post-1989 social and housing policy reforms. As noted by Krebs *et al.* (2005), “Such systemic change cannot be realised in a short term. It is the process in which the elements of old and new systems coexist together: the old system lost its original function but at the same time the new system does not function in the whole its integrity.” (p. 93). Since most Czech citizens had no experience of anything other than the communist type of administration of social matters, any truly profound and quick reform in social policy was hardly possible. However, this was no excuse for the long time it took for reforms to take place, as was finally the case.

During at least the first 16 years of transition (until 2006) the role of social policy was to create a safety net for the shocks stemming from liberalisation and privatisation of the economic system (loss of Eastern European markets, competition for national production with goods imported from Western markets, the banking crisis, unemployment, the rise in income differentiation, cuts in public spending, tax reform, price liberalisation, etc.). The transitional governments did not come up with any general long-term concepts for social policy. The first ‘scenario of social reform’ came about in 1990, followed by the Subsistence Minimum Act No. 463/1991 Coll. in 1991. The next ‘reform’ of social support, the State Social Support Act No. 117/1995 Coll. of 1996 targeted the most probable social risks stemming from economic reforms and especially defined a safety net aimed at keeping social order in the event negative consequences of economic reforms appeared. In this manner the act set the minimum wage, the subsistence minimum (minimum income guaranteed by the state), allowances to compensate for price liberalisation and other social benefits.

The Czech Republic established three basic pillars of social policy: social insurance, social support and social assistance. Through social insurance citizens put aside part of their consumption in the event of any uncertain social circumstance in future, which could result in partial or full loss of income. The possible reasons for a loss in income include maternity, the care of a fam-

ily member, illness, disablement, old age, loss of provider, or loss of employment. The aim of the insurance, in such cases, is to maintain the reasonable standard of living attained by the insured and their families. Social security premiums and the state employment policy at 12.5% are deducted from employees' gross wages. The employers cover a further 35% and transfer the total premium sum to the relevant authorities.

Social support contributions help families to cover increased costs due to the presence of persons still not (or not yet) earning an income and help families to cope with specific life situations in which they lack the ability or resources to do so for themselves. Social support contributions may be divided into two sub-categories according to the method in which financial resources are redistributed. If this concerns redistribution from families with and without children, then it is called horizontal redistribution. Contributions belonging to this category include: family, birth, and guardian allowance. Payment of these allowances may be terminated depending on the achieved income level. If this concerns redistribution from high to low-income families, this is called vertical redistribution. The level of allowances in this category is based on examining the real income situation of a family and this includes: child allowance, additional social allowance, housing allowance and transport (travel) allowance. The level of allowance decreases as income rises, so the moment a family achieves a certain income level, its claim to benefit is terminated. Virtually the entire structure of social support allowances was based on the subsistence minimum concept – this minimum amount is used, particularly in the second sub-category of social assistance, to determine the income ceiling (*n-multiple* of the subsistence minimum) so that an applicant may become entitled to a specific allowance.

Social assistance is designed for people (families) unable to secure their basic living requirements. In other words, social assistance is designed for families whose income is beneath the subsistence minimum limit. The basic level of this assistance in practice in most cases usually corresponds to the difference between the level of the household's income and its subsistence minimum. When examining a household's claim, its property circumstances and possibilities of increasing its income are also considered.

The subsistence minimum is defined as a socially recognised minimum income level under which a state of material emergency occurs. It defines the level of necessary funds for a household to temporarily secure the basic living requirements of its members at a very modest level. The subsistence minimum in the Czech Republic consists of two components: the sum required to secure the needs of each person in the household and the sum required to secure the necessary expenses of the whole household. The first part of the subsistence minimum therefore applies to the basic personal requirements of each household member, which includes food, clothing, footwear, other industrial consumables, services and personal development. Five different lev-

els are determined for the sums to secure personal requirements; four for unprovided children of various ages, the fifth for other citizens. The second part of the subsistence minimum serves to cover other common household costs, that is, mainly housing costs and related services.

The subsistence minimum has been regularly valorised by a government decree provided that the consumer price index rises by at least 5%. The goal of social policies up to 2006 – create a relatively soft social policy to cushion against social disorder and political instability during economic transformation – is reflected by such system features as highly progressive income taxing, high social insurance payments (in fact, social insurance dues represented more tax than the insurance), regular valorisation of subsistence minimum (and all related social support benefits), a two-component structure for the subsistence minimum and relatively generous additional social benefits.

At the beginning of transition there were efforts to escape the redistributive model of social policy (known, for example, from Scandinavian countries) and move towards a meritocratic (corporatist) model (using Titmus's classification of 1974) and the rhetoric of the first right-wing governments was even in favour of a third – residual – model of social policy. However, no government (including those led by the right-wing conservative ODS political party) was brave enough to make its rhetoric a reality. The system remained firmly embedded in the past, highly redistributive, with an especially high redistributive burden put on the middle classes (Večerník & Matějů (eds.), 1999, p. 149). The social security system was so generous that it created a significant unemployment trap situation (especially when connected with economic subsidies stemming from rent regulation) and prevalent abuse of social contributions (shadow labour market). The lack of real reform led to unsustainable growth in the state's social expenditures. As Krebs put it, "Solidarity is not just a matter for those who gain from solidarity funds, it is also a matter for those who contribute to those funds.... Distribution of tax burden and excessive redistribution may become in the long term as significant problem as the problem of welfare versus poverty.... It is necessary to reduce excessive 'paternalistic' solidarity, which becomes an unbearable burden for payers (especially the middle classes) and naturally increases state social expenditures.... Excessive solidarity or excessive redistribution by the state respectively worsen social problems in some way: work-dodging, maternity without marriage, rent arrears, alcohol and drug addiction" (Krebs et al., 2005, pp. 454-457).

That the role of social policy during the first decade of transition was mainly to keep social peace and the public support for economic reforms had very important consequences. The profoundly long-term orientated reforms of economic and political systems were given preference to reforms in the field of social policy. The reform of social policy especially followed the short-term goals (safety net during the transition). It was not in the interests of the early transition governments to immediately and directly challenge the

powerful social norm prevailing from communism, the general dependence of people on the state. The imperatives of efficiency, effectiveness and long-term sustainability in policy interventions were not taken into account when the governments established their relatively comfortable 'welfare state pillow' based on relatively high wealth redistribution and the ideology of egalitarianism. This helped to achieve the necessary economic reform changes but, at the same time, it strengthened the false inherited social norm of people's high dependence on the state.

Thanks to the large public income from enterprise privatisations the state could afford to make such generous social policy at the beginning of transition. However, later on, when the spring of privatisation incomes had dried up, such 'generous gifts' were necessarily beginning to be distributed unequally. After a decade in action, this generous system was revealed by a substantial lack of public resources (kept topped up by the governments in power after 2000 only by fast growth in state debt), huge inefficiencies in redistribution, free-riding as well as significant social justice problems (insider-outsider tensions stemming from the unequal redistribution of 'gifts', as one in the field of housing described below).

However, this does not mean that the generous social policy was totally negative. The Czech Republic has the second lowest at-risk-of poverty rate in EU-25 (SILC, 2005); people enjoy free university education and largely improved health care services; the problem of social segregation and exclusion still remains more a potential threat than actual reality. However, the prolongation of the false social norms of egalitarianism and dependence on the state might have increased the power of such norms – the people have learned that considerable social security can still be attained even under market economy conditions and they do not understand why these should be reformed in the future.

The Czechs have already experienced one example of such disillusionment, in the case of unemployment. In the early years of transition (till 1996) the unemployment rate was very low (under 4%, see above) in contrast to other transition and even developed countries. This is the result of many factors. In the early 1990s the majority of employed pensioners left their jobs and many entrepreneurial people left employment to start their own business (supported by privatisation of services). There was a favourable educational structure, but the most important factor was probably the influence of the state on employment policies in major (though often privatised) industrial enterprises. The government (again the 'omnipotent' state) not only directed huge amount of *ad hoc* subsidies to save many private enterprises in economic problems, often unsuccessfully, but thanks to the majority state holdings in almost all Czech banks the government was able to force those unreformed banks to extend risky credits to enterprises in economic problems to sustain over-employment.

At the time preserving social order was the main government goal so long-term concepts were put aside. Možný (1994) wrote that new political elite inherited the misfortune of the previous elite: social peace is no less important to the feasibility of economic transition than it had been in decades of 'building socialism' for the maintenance of the communist regime. Under such conditions the dream of a 'never-ending' high employment rate could last only a few years, only till 1996. After 1997 the unemployment rate began growing rapidly, and many state-owned banks found themselves close to bankruptcy due to their soft credit policies of the past (the widespread banking crisis of 1997 demanded huge additional state subsidies to prevent a total collapse of the banking sector). Economic growth was unprecedented (in comparison with the neighbouring transition countries) interrupted by the recession of 1997-1998. The government was dissolved and preliminary parliamentary elections took place.

3.4 Demographics

For the purpose of describing the demographic context I used the range of studies *Population development in the Czech Republic* published annually by the Department of Demography and Geodemography at Charles University (English versions). The baby boom typical of the majority of European countries after WWII was followed in the former Czechoslovakia by a decrease in fertility rates that continued until 1970. The beginning of 1970 saw a temporary rise in fertility (a second baby boom) and population growth stabilised during the 1980s (zero population growth). 'The demographic revolution' began after 1989 when natality and nuptiality rates substantially decreased and since 1994 the population has shown negative natural growth. Compared to the situation in 1989-1991 (130,000 births on average), in 1996-1998 the number of births fell to only 90,000 (by 30%) and remained at this low level till 2001. Just for the comparison, in 1974, during the second baby boom, 194,000 children were born.

The total fertility rate fell to less than 1.14 children in 2001, which was one of the lowest in the world. This drop is all the more surprising because in this period the large number of women born during the second baby boom reached the age of maximum fertility. The period of maximum fertility also shifted from 20-24 years to the group aged 23-27 years. Since 1997 the Czech Republic has had more inhabitants over the age of 60 than children under the age of 15 and this predominance of older people rises every year. The fall in fertility rates after 1989 is closely related to the decline in the nuptiality rate.

Another important demographic aspect of transition concerns nuptiality – the average age at marriage was relatively low before 1989 (24.5 years for men, 21.8 years for women in 1989) but it substantially increased during the transition (29.3 years for men, 26.9 years for women in 2001). Before 1989,

about 90-95% of men and 96-97% of women were married at least once in their life but in 2000 the probability of being married at least once in a lifetime decreased to 65-70% among men and 72-75% among women. The percentage of married people up to the age of 60 dropped to the lowest level since WWII. In the younger age groups the percentage of single persons has risen, though cohabitation (with children) did not become as popular as it has in many Western countries. Worsening housing affordability, and new employment, travel and educational opportunities as well as new forms of self-fulfilment are cited as the causes for the drop in nuptiality.

For a long time the Czech Republic had one of the highest divorce rates in Europe (similar to levels in Scandinavian countries or the UK). In 1997-1998 42% of marriages were expected to end in divorce, annually more than 13 divorces per 1,000 marriages. In 1996 the number of divorces reached its peak: 33,000 divorces were granted, almost three times more than in 1950. Various social factors are mentioned as the causes: ease of divorce (legislation), social norms (marginal influence of the Church, atheism), low social prestige of the family, and living conditions.

In 1998 life expectancy at birth reached 72.1 years for men and 78.4 years for women, an increase of 4.3 years and 3.3 years respectively since 1987. The substantial improvement in general state of health and the level of mortality during the transition was caused by more attention paid to own health; lifestyle changes (particularly in nutrition habits); liberalisation and demonopolisation of the health care system (considerable investments, rapid spread of up-to-date drugs); reductions in environmental pollution; improvement in work conditions; and low poverty rate.

3.5 Immigration

According to the yearbook 'Population Development in the Czech Republic' the number of foreigners in the Czech Republic grew sharply until 1999. These were both foreigners with permanent residence status and foreigners with temporary 90-day visas. Since then, owing to tighter visa restrictions, the number slowly decreased until it rose sharply again after 2005. In 2000 there were roughly 67,000 foreigners with permanent residence and 134,000 foreigners with temporary residence in the Czech Republic, thus a total of approximately 200,000 people. Out of the total number of foreigners in the country the largest proportion was made up of Ukrainians (50,000), Slovaks (44,000), Vietnamese (23,000), Poles (17,000) and Russians (13,000). The proportion of immigrants from advanced countries was relatively small. The majority of foreign nationals living in the Czech Republic were (and still are) thus people from Slovakia, the former Eastern bloc, and Asia. The number of people residing in the Czech Republic under political asylum was till 2005 negli-

gible. To these figures must be added foreigners living in the Czech Republic illegally – of which there were an estimated 100,000 in 2000. In the case of illegal residence these were again primarily people from the former Eastern bloc. The highest concentration of foreigners is in the capital city, Prague and its environs. In the year 2000 more than 30% of foreigners were living in and around Prague. Immigration (which in comparison with advanced countries over such a long period was relatively low) was made up predominately of people with temporary residence. The number of highly qualified immigrants from advanced countries employed in management positions in various international firms was marginal, though not for Prague.

In the housing market, immigration thus comprised the major portion of the demand for rental housing of mid-level and lower quality (including pre-fab flats), located mainly in Prague and its surrounding areas. Given the scope and type of residence of foreigners in the Czech Republic, immigration has not had a substantial direct effect on the prices of owner-occupied housing. The effect could have been indirect – a growing demand for cheap rental housing could limit the supply of cheap flats in the owner-occupied sector. However, the strength of this effect is debatable considering the scale of immigration.

A much more significant factor affecting conditions in the housing market was the domestic migration of Czech citizens. Since 1996 there has been a clear trend of people migrating from larger towns to municipalities with a population ranging between 50 and 5,000 people, mainly municipalities with between 500 and 2,000 inhabitants, in the wider environs of larger towns. The number of people living in the largest towns has decreased; most of all in Prague (although the population of Prague began to grow again in 2005). Suburbanisation has also been considerable in Brno and in Pilsen, and less so in Olomouc, Liberec, Hradec Králové, and České Budějovice. Over the course of the 1990s out of all Czech towns and cities, Prague lost the most inhabitants in absolute and relative figures, with a corresponding increase in population in the Central Bohemia Region.

3.6 Housing conditions and housing policy

The changes in housing conditions during the transformation period will be described here with a brief outline of housing policy prior to the transformation period, that is, between 1918 and 1990.

3.6.1 Housing policy between 1918-1948

The independent Czechoslovak Republic was established in October 1918. Pre-1918 housing policy had been provided by the Austrian-Hungarian Empire

and it was, generally, marginal till the middle of the 19th century. In 1860 the law allowed the establishment of non-profit housing cooperatives (already present in England since 1809), but the idea of housing cooperatives was not very popular at the time. In 1892 another law created substantial tax incentives for factories building flats for urban workers (exemption from house duty for the period of 24 years for all new apartment houses with floor areas of flats under 75 m²); this tax incentive was connected with soft rent control (maximum yield from investment set at 5%). In 1908 the Franz Joseph I Fund was established. Fund resources were used for preferential credit (3% annually) to housing cooperatives of state employees. In 1910 another fund, the State Fund for Small Flats, began extending preferential credit for construction of small flats. This was an incentive for the establishment of housing cooperatives as well as the construction of municipal housing (though the scale of housing output provided by both of them remained marginal till the end of the Empire).

Real housing policy appeared after the WWI when the newly created Czechoslovak Republic struggled with a housing shortage. Firstly, the municipalities received the power to regulate local housing markets by the following means: rent control, restrictions on mobility, private landlords were bound to conclude new rental contracts with people needed by the municipality (state employees) and they were not allowed to unite flats or use them for any other purpose than housing without the consent of the municipality. Only newly built flats (built after 1917) were exempt from rent control at the start; since 1924 this exemption was also extended to larger flats (four or more rooms), higher-income tenants, flats in houses owned by legal person and flats in municipalities with less than 2,000 inhabitants. Due to the housing construction boom of the 1920s and the first half of the 1930s (peaking in 1928 with almost 100,000 flats finished in one year) the share of flats exempted from rent regulation quickly grew and soon overtook the share of 'protected' older flats with controlled rents. Secondly, the state had the power to expropriate vacant land that could be used for housing construction if the owner of the plot did not start his own housing construction within a set deadline.

The state supported the housing construction boom mostly by indirect subsidies. Based on the Law on Housing Construction (first passed in 1919 and then amended almost every year) the state mainly offered:

- *state guarantees* on part of mortgage loans extended on new housing construction; firstly only on the construction of small rental flats (up to 80 m² of floor area) built by municipalities and non-profit construction associations (in fact, housing cooperatives) and between 1921-1927 on construction of small rental flats built by all persons (including the private for-profit orientated ones) as well as on the construction of small family houses for low-income households. Since 1927, in the case of apartment buildings state guarantees were once again provided only to municipalities and non-

profit associations and only on flats to low-income households.

- *interest subsidy* covering the whole or part of the interest payments from mortgage loans extended on the construction of new small flats for a period of 25 years. Interest subsidy was originally allocated (since 1919) only among municipalities and non-profit construction associations and in the period 1921-1927 was allocated among all apartment housing builders. The interest subsidy was abolished in 1927 and a new state allowance on repayment of annuity of mortgage loans was introduced in 1930 (allowance covering maximum of 2.5% of loan value annually for maximum of 10 years); this allowance was allocated, in the case of apartment buildings, only among municipalities and non-profit associations for the construction of small flats for low-income households. In 1936 the state allowance was replaced once more by the interest subsidy.
- *exemption from property tax* for the period of 20 years for all new housing.
- *one-off direct state grants* covering a maximum of 40% of all construction costs of apartment rental houses begun in the years 1920 and 1921 (this subsidy lasted only two years) among all builders of apartment rental housing (including private ones), if the building was situated in a town (above 15,000 inhabitants); it had to comprise at least 4 flats; the commercial area of the house could not exceed 30% of the total floor area; construction costs need to be approved by the Ministry of Public Works; and the state must have received the first option.

The most effective incentive of the time appeared to be the exemption from house duty for private investors (including exemption from a number of other taxes and charges connected with house duty). Thanks to this indirect support and the non-existence of rent control for vacant and newly built flats the housing boom (mostly provided by private investors) saturated the housing need already at the beginning of the 1930s (though many flats were of low quality). Such a stable market situation remained only till 1938 when the Munich Agreement led to the loss of substantial Czechoslovak territories and the flow of Czech and Slovak migrants from those territories created tensions on the housing markets in the remaining territory of the Czechoslovak Republic. The housing shortage increased during the WWII due to the depression of housing construction after 1941 and much stricter rent control on the occupied territories of the former Bohemia and Moravia.

Generally, during the period 1918-1938 (called the First Czechoslovak Republic), housing in urban centres was mainly provided and constructed by private investors (private landlords) viewing residential markets as profitable and safe investments. Though more active than during the Austrian-Hungarian Empire, state housing policy was characterised by a lack of long-term strategy, *ad hoc* subsidies and frequent (almost annual) amendments of the main legislative framework. It concentrated on indirect state subsidies (tax

exemptions) for private rental housing construction.

In 1945-1946 the housing need created by war was partially satisfied by expropriated housing left by Germans expelled from Czechoslovakia soon after the war. However, in main urban centres with the most employment possibilities (mainly in the capital Prague) the housing shortage prevailed (besides the housing surplus in cross-border territories) and, moreover, the new baby boom began shortly after the war ended. Rent control was therefore preserved and a new central plan (for the period of 1946-1948) counted on state support for new housing construction. Due to the lack of resources and political instability these plans were not realised. In 1948 the Communist Party succeeded in its *putsch* against the democratic regime and Czechoslovakia entered the period of totalitarian one-party political regime and centrally planned economy.

3.6.2 Housing policy between 1948 and 1989

After 1948 state housing policy was based on the principle that a home is such an important good in the life of a person that rising costs of building, repairing and maintaining housing should not be reflected in household expenditures, or in other words, in a rise in the costs of housing. In Eastern bloc countries, including the Czechoslovakia, this policy resulted in an almost total expropriation of private apartment housing and in the attempt to apply an egalitarian approach to satisfying housing needs. At the time the state took on responsibility for ensuring the provision of housing for each member of society – especially by the state rental housing.

The consequences manifested themselves in the untenable burden on the state budget. The general lack of sufficient financing led to a substantial deterioration in the quality of housing stock; the suppression of market relations led to the emergence of inequality in access to housing (protectionism and bribery over the allocation of new and vacated flats) and to the generation of a false ‘collective memory’ that it is the state’s job to ensure that everyone has a roof over their head.¹⁹ Extensive state-financed housing construction was increasingly confronted by limited resources, thus despite the continual declarations of ideological viewpoints, later on other forms of housing construction were also permitted – enterprise, cooperative, and individual housing forms.

When it existed, enterprise-based housing construction was financed part-

¹⁹ Mainly budgetary pressures as well as the ideological principles of the pre-war avant-garde functionalists later led to the more widespread use of pre-fab construction for housing settlements in the 1960s and especially in the 1970s and 1980s, which owing to poor quality control soon revealed substantial technological shortcomings.

ly from the resources of the state enterprises, partly from the state budget, and partly from long-term bank loans. This system was, however, abolished in 1981. Cooperative housing construction had been organised since 1958 by housing cooperatives and its costs were covered by contributions from the cooperative's members, state subsidies, and low-interest bank loans. Individual housing construction primarily involved the construction of family houses, financed primarily from the resources of the individuals, supplemented by contributions from local branches of state administration and long-term low-interest loans from banks.

In the case of state rental flats, rent was determined by bureaucrats who set it at an unrealistically low level (e.g., until 1991 rent was frozen at the level set in 1964). The management of state flats was the responsibility of public management enterprises that operated on the community level. As mentioned above, flats were allocated through administrative procedure, which despite the officially declared adherence to the principle of equality and need in reality resulted in injustice, bribery and protectionism. Paradoxically, state flats with low rents were often allocated on a priority basis to the members of communist nomenclature, top staff in the state and political apparatus, and members of the armed forces, that is, to people who held functions with higher incomes anyway.

Households chosen from the waiting list and assigned a flat usually received something called a 'decree to a flat', which was the socialist analogy to a lease. Tenants that held such a decree acquired not only the right to low rent, but also broad legal protections securing them the right effectively to use the flat for their entire lives, the option to exchange their flat with someone else if necessary (wherein the same terms applicable to the original tenant would apply also to the new tenant) and in particular the option to pass the flat on to their children for use after their own death. Consequently, a relationship to the property emerged that is often referred to as 'quasi-ownership' of the rental housing (Lux & Burdová, 2000; Šmídová, 1996).

Housing cooperatives, unlike the public management enterprises, had to maintain balanced budgets. Given that the payments made by tenants for occupancy of a cooperative flat had to defray the full costs of the operation, maintenance and repair of the building and cooperative members also had to repay bank loans, cooperative members spent more on housing than tenants in state flats.

Housing cooperatives differed from their counterparts in democratic countries. The pre-war housing cooperatives were forcibly merged into cooperative 'giants' (e.g., in the 1950s, one housing cooperative emerged in Prague to manage the entire stock of cooperative housing built in the pre-war period within the territory of the city). New housing development (renewed at the end of the 1950s) was also conducted by large Building Housing Cooperatives, which over time in large towns were managing flats sometimes numbering in the

thousands. Cooperative statutes were required to be uniform and deemed by rule that the cooperative members be nourished in the spirit of socialist and by extension communist morality. Differences were not tolerated, and owing to the massive numbers of members of these cooperatives, the initially democratic procedures of the cooperative members were replaced with proceedings among 'delegates'. The 'nationalisation' of cooperative movement resulted in particular in the destruction of the original idea behind cooperative associations as independent 'self-help' entities and it extinguished the notion of individual initiative and cooperative democracy. Cooperative housing became perceived as simply a more expensive form of state rental housing.

Part of the solution to the shortage of housing was an attempt to limit the migration of the population to larger towns by creating a dense, state-subsidised public transit network, which allowed rural residents to commute daily to urban centres. Pre-fab technology and uniform residential development plans were also used to remedy the discord between the demand for flats and limited public resources. The construction of large pre-fab housing estates became a characteristic feature of the majority of socialist countries, the Czech Republic included. In 2001, 31% of the Czech population was still living in pre-fab flats and in bigger towns even half the population lived there. Ultimately, at the cost of massive state subsidies and adherence to the principles of mass pre-fab housing construction, the housing shortage was overcome prior to 1990.

A very specific feature in the Czech Republic was the widespread existence of secondary homes (cottages, summer houses). Vágner (Bičík *et al.*, 2001, p. 44) indicates that the "massive expansion and popularity of secondary homes stemmed primarily from middle or even lower-class backgrounds", which is one important and distinctive feature in the Czech Republic in comparison with the majority of countries in the world. Ownership of a secondary home gradually gained in prestige and became a fashionable social matter, indicating a person had attained a certain social standing. Vágner (Bičík *et al.*, 2001) indicates that an important milestone for the further development of the phenomenon of secondary housing was the events of the 1968 (occupation of Czechoslovakia by the Warsaw Treaty armies), after which many people, having been forced to change their employment, sought an escape into their own, private environment, where they could be themselves. In 1971 there were over 156,000 buildings in the territory of the Czech Republic used for personal recreation. In 1980 the number had increased to almost 225,000, and in 1991 it reached almost 268,000 (Bičík *et al.*, 2001, p. 49).

3.6.3 Housing policy between 1989 and 2005

3.6.3.1 Housing conditions

As in other sectors of the economy, after 1989 the housing sector began to undergo a transformation from an administrative flat allocation system to a system based on market principles. According to the initial housing policy plans (*Proposal for a State Housing Policy in the Czech Republic*, 1991; *Foundations and Principles of the State Housing Policy*, 1993), based on neo-liberal economic principles, the role of the state should have been limited to that of establishing the conditions in which a housing market could emerge.

Key events in housing policy during the transformation period were the restitution of part of the housing stock, the free-of-charge transfer of the unrestituted portion of the housing stock to municipal ownership, the privatisation of municipal housing, the introduction of new housing policy instruments, in particular the housing allowance, state premium to housing savings, interest subsidies to mortgage loans and tax relief.

The revenue subsidies for existing state rental dwellings and capital subsidies for new state rental housing construction practically disappeared soon after the change of the regime; prices of construction materials were liberalised and quickly increased. Both factors led to the sharp decrease in housing construction volumes; housing construction output started to grow again after 1994, and especially after 1996 (Table 3.1). In the first period of transition “the market could not react in an environment of huge disparities between housing need and demand and the government was not willing to bridge the gap between the high need (but low purchasing power) of households and the sharply increased costs of housing production” (Sýkora, 2003). This situation changed in the most developed regions (especially in the capital Prague) after 2000 where real household incomes started to grow rapidly and the ratio of prices for existing dwellings to construction prices of new dwellings substantially increased (new housing supply started to compete with the existing housing stock). Private capital became dominant in new housing supply and the share of municipal housing construction on total housing starts steadily decreased (Table 3.2).

Just as the share of municipal housing construction out of total housing construction fell significantly, so did the share of rental housing construction of the total new housing construction (new rental flats comprised only 7% of the total volume of housing construction in 2005, the rest was built as owner-occupied housing). Nevertheless some small investors buying their flats into ownership could lease them soon after their finalisation, so this piece of information may be slightly misleading.

In spite of the moderate scale of house construction, the number of permanently inhabited dwellings per 1,000 inhabitants increased from 360 in

Table 3.1 Housing construction in the Czech Republic (number of dwellings), 1990-2005

Year	Number of dwellings		
	Started	Under construction	Completed
1990	61,004	158,840	44,594
1991	10,899	128,228	41,719
1992	8,429	97,768	36,397
1993	7,454	72,356	31,509
1994	10,964	62,117	18,162
1995	16,548	66,172	12,662
1996	22,680	74,726	14,482
1997	33,152	90,552	16,757
1998	35,027	103,191	22,183
1999	32,900	112,530	23,734
2000	32,377	118,785	25,207
2001	28,983	121,705	24,759
2002	33,606	129,609	27,292
2003	36,496	139,132	27,127
2004	39,037	146,801	32,268
2005	40,381	155,202	32,863

Note: Apartments in extensions of existing buildings, houses for the elderly with social services and those adapted from non-residential premises have been included since 1996.

Source: Czech Statistical Office

1991 to 372 in 2001 (Table 3.3). Other dwellings serve residential purposes, but their inhabitants do not have permanent residency there. If we take all habitable dwellings, the Czech Republic had 427 dwellings per 1,000 inhabitants in 2001 (Table 3.3). In comparison with other developed and transition countries (Figure 3.4) this result leads to the conclusion about relative housing sufficiency; the ratio is even higher than in some old EU member states.

The housing shortage question is however more complex. As mentioned above, the housing market is regionally and locally specific. As in other countries, in the Czech Republic there are regions (the Northern Bohemia region) where vacant flats are starting to appear and the surplus supply is forcing housing prices to fall to a low level. Conversely, there are regions with accelerated economic development (Prague and surrounding areas) where there is still a high demand for housing and prices are disproportionately high. Regional deficits, which can be found in all advanced countries, are not however a justification for claiming a housing crisis. This issue has been addressed in greater detail by Kostelecký & Lux (Lux *et al.*, 2004) using several standard ap-

Table 3.2 The number and share of started and completed municipal housing from the total number of new dwellings in the Czech Republic, 1990-2005

Year	Started total	Started municipal	Share of started municipal (%)	Finished total	Finished municipal	Share of finished municipal (%)
1990	61,004	10,411	17.1	44,594	8,516	19.1
1991	10,899	1,524	14.0	41,719	9,610	23.0
1992	8,429	1,864	22.1	36,397	7,086	19.5
1993	7,454	1,920	2.6	31,509	6,213	19.7
1994	10,964	1,477	13.5	18,162	4,224	23.3
1995	16,548	3,015	18.2	12,662	1,689	13.3
1996	22,680	3,165	14.0	14,482	2,727	18.8
1997	33,152	4,123	12.4	16,757	2,835	16.9
1998	35,027	3,407	9.7	22,183	3,216	14.5
1999	32,900	3,246	9.9	23,734	2,925	12.3
2000	32,377	3,679	11.4	25,207	2,897	11.5
2001	28,983	2,585	8.9	24,759	2,686	10.8
2002	33,606	4,393	13.1	27,292	2,612	9.6
2003	36,496	3,782	10.4	27,127	2,605	9.6
2004	39,037	2,012	5.1	32,268	3,641	11.3
2005	40,381	1,968	5.4	32,863	2,430	8.4

Source: Czech Statistical Office

Table 3.3 Number of dwellings in the Czech Republic in 1991 and 2001 (census data)

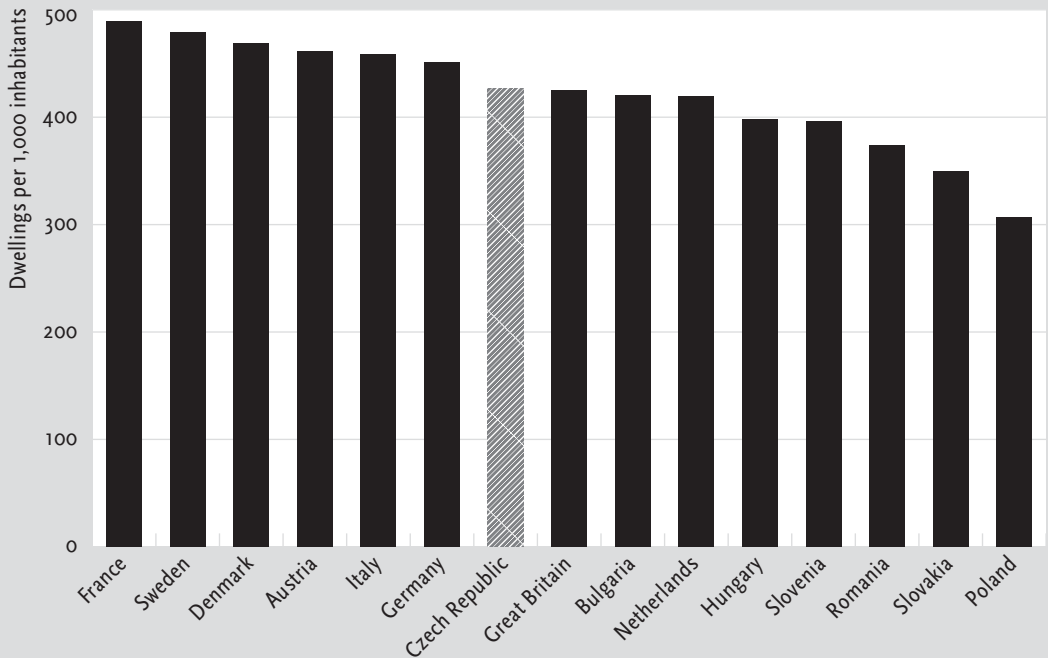
	Number of dwellings 1991	Dwellings per 1,000 population	Number of dwellings 2001	Dwellings per 1,000 population
Permanently inhabited	3,705,681	360	3,828,912	372
Inhabited (incl. temporary)	n.a.	n.a.	3,951,345	384
Habitable	4,039,738	392	4,304,084	418
Total	4,077,193	396	4,369,239	427

Note: 1991 population: 10,302,215 and 2001 population: 10,292,933.

Sources: Czech Statistical Office, Census 1991 and Census 2001

proaches, and the findings show that it is not possible to speak of a housing shortage in the Czech Republic. The authors state, "The indicators used do not confirm the widespread idea that in the Czech Republic there is a physical shortage of flats, and that because of this the situation in this country differs significantly from that in other countries in the European Union. The relatively good position the Czech Republic has within the EU is to some extent

Figure 3.4 Number of dwellings per 1,000 inhabitants, around 2000*



* The majority of figures refer to the situation in 2000, for some countries they refer to the situation in 2001, for Slovenia to the situation in 2002 and for France to the situation in 1999.

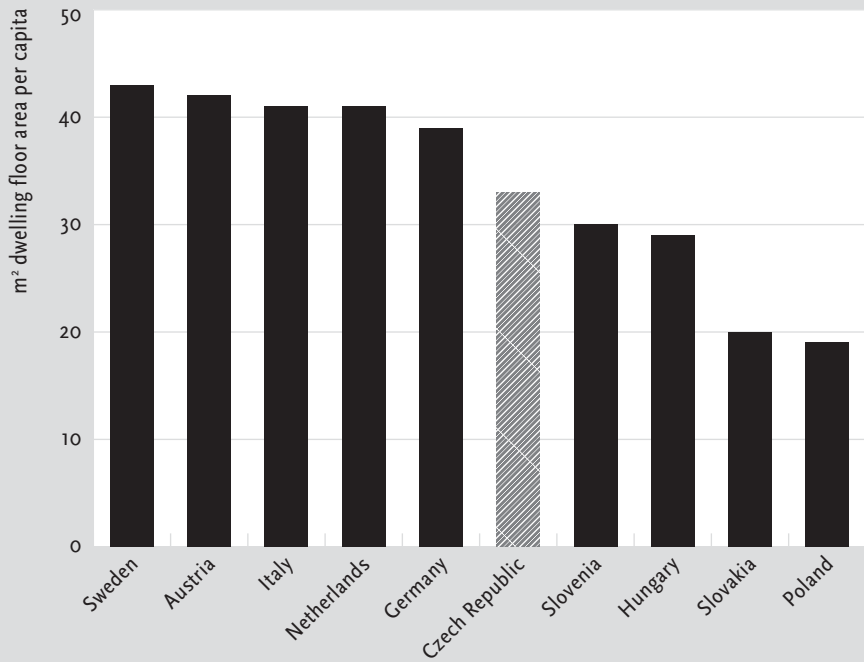
Sources: Housing statistics in the European Union 2002; Czech Republic, Slovakia, Hungary, Slovenia, Bulgaria, Romania: www pages of national statistical offices

‘improved’ by the fact that the ten new member countries caused the European average to fall slightly, but nonetheless even in comparison with old EU member states the Czech Republic is in this regard not doing that poorly” (Lux *et al.*, 2004, p. 30).

Figure 3.5 shows an international comparison of the values of another indicator measuring the housing conditions, which reveals the real deficit that the Czech Republic was and still is facing in comparison with other advanced countries. The indicator is the average size of total dwelling floor area per inhabitant.

The average floor area per inhabitant is higher in the Czech Republic than in other selected post-communist countries (especially compared to Poland and Slovakia) but the value of this indicator shows how far behind the advanced countries of Western Europe it is still in this regard. In other words, it is not the physical lack of flats but the quality of the housing stock (floor area, the quality of pre-fab housing technology, the quality of the residential environment on large housing estates, the long-term deficit in repairs and modernisation of housing stock) that appeared to be the real challenges for the housing policy makers in the changing socio-economic environment of the Czech Republic.

Figure 3.5 Average dwelling floor area in m² per capita, around 2000*



* The majority of figures refer to the situation in 2000, for some countries they refer to the situation in 2001, for Slovenia to the situation in 2002 and for France to the situation in 1999.

Sources: Housing statistics in the European Union 2002; Czech Republic, Slovakia, Hungary and Slovenia: www pages of national statistical offices

3.6.3.2 Tenure changes

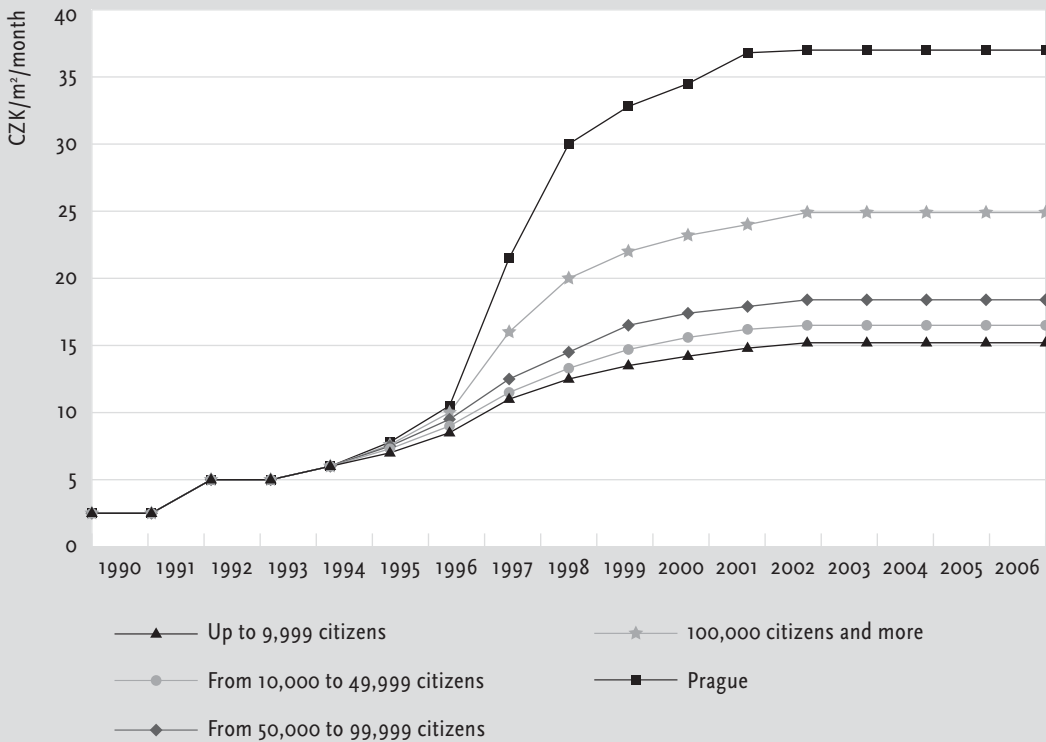
Restitution began in April 1991 and applied to the portion of the housing stock that had been expropriated by the state or became the property of the state between February 1948 and January 1990 under circumstances disadvantageous to the original owner. If the legal terms for the restitution of property were satisfied, the property was returned to the original owner, or to their heirs or immediate relatives, as long as they were citizens of the Czechoslovak Federal Republic (later the Czech Republic) and possessed permanent resident status in the country. Sýkora (2003) shows that the majority of restitution claims were settled by the end of 1993. There are no exact statistical data on the volume of the housing stock returned to the original owners as part of the restitution process, though it is estimated that it was around 6-7% of the national housing stock. Restitution represented a significant form of intervention in the ownership structure, especially in large town centres, for example, in the centre of Prague, where 70-75% of all buildings were returned to the original owners (Sýkora, Šimoníčková 1994). Restitution entailed the creation of a private rental-housing sector and the formation of an important lobby group of private landlords.

In every country with a private rental sector there has always been tension between landlords and their tenants. After the WWI, when owing to a shortage of flats rent regulation was gradually introduced, this tension was transformed from 'hallway' arguments to a fully fledged social conflict reinforced by the extensive rent regulations introduced after WWII in virtually all advanced countries. (This was followed by a sharp decline in the share of private rental units on the total housing stock in advanced countries). However, sometimes as early as the 1960s, sometimes in the 1970s, rent prices in the private sector were gradually deregulated to acceptable levels allowing for landlord profit in most developed countries. At least private sector rents were less regulated than rent prices in the sector of social housing, thus partially abating the intensity of social conflict between private landlords and tenants.

Although original owners or their descendants were returned the buildings that had been unlawfully taken from them, the rent for running tenancies in those buildings remained, however, regulated by the state to the same degree as in state (later municipal) rental housing. Moreover, the central government decided to maintain the system of old-styled (or 'first-generation' in Lind, 2001) state regulation of rents (untargeted, flat, with rent prices deeply below market levels and substantially below cost rent) inherited from the communist period. The strong tenant protection legally introduced in the Civic Code during the previous communist regime also remained almost unchanged till 2006. Judicial procedures slowed down during the transition (due to the increased number of cases and slow performance of courts) and, for example, the eviction process of tenants not paying rent could linger on for several years. Despite rent regulation no revenue subsidies were introduced to cover the difference between low regulated rents and costs of maintenance. In practice a paradoxical situation arose when private owners could not increase the rent to a level sufficient at least to cover the necessary maintenance costs and received no subsidies from the state to cover the difference between the costs and income. The legislature (1993) only allowed the charging of market rent if the tenant was not a citizen of the Czech Republic and if the flat had been vacant before renting (new tenancy).

The first phase of very gradual rent deregulation in the Czech Republic was launched at the beginning of the 1990s. Since then the maximum monthly rent has increased every year according to the quality of a flat (four categories), size of a municipality and inflation coefficient. As a result, the limits of maximum rent per month per m² of dwelling floor space in a Category I flat increased from the original CZK 2.50 in 1991 to CZK 37.07 in 2006 in Prague, CZK 24.76 in cities with a population over 100,000, CZK 18.31 in cities with a population of more than 50,000 and less than 99,999, CZK 16.42 in towns with a population between 10,000 and 49,999 people and CZK 15.23 in towns and municipalities with a population below 10,000. In 1999 the government policy led to a freeze in nominal rent values (rents were increased only with infla-

Figure 3.6 Maximum controlled rents (CZK/m²/month) in the Czech Republic, 1990-2006 (Category I quality)



Source: Ministry for Regional Development

tion) and after 2002 the rents were frozen both in nominal and real values. Figure 3.6 illustrates the rise in the rates of maximum regulated rent for Category I flats according to municipality size categories. The difference between regulated and market rents remained high even in 2006, especially in prospering cities; in Prague, regulated rents were still about three times lower than their market counterparts for the same dwelling.

The process of decentralisation of power and the renewal of regional self-government included the transfer of the housing stock from state to municipal ownership. This transfer was initiated in 1991, and it affected 1.44 million flats (approximately 39% of the housing stock in the Czech Republic). The municipalities were cast in the role of administrators of the housing stock, responsible for creating local housing policy, and were forced to bear the costs of the operation, maintenance and management of their newly acquired property. However, the transfer of housing stock was not accompanied by any increase in the contribution of supplementary financial resources to municipal budgets, and the municipalities did not possess the procedures and systems to cope with their new role. In the majority of municipalities in the 1990s the income collected from rent was not enough to cover management and maintenance costs, which meant an additional burden was put on municipal budgets. This led to a continuation of long-term under-investment in the housing fund, and even to an attempt on the part of the municipalities to

privatise at least part of the housing stock in an effort to alleviate the burden on the municipal budgets.

In 2000 the Constitutional Court decided that Decree No. 176/1993 Coll. regulating the level of rent in regulated rental housing contradicted certain articles of the Charter of Basic Human Rights and Freedoms, Article 1 of the Constitution of the Czech Republic and some other superior legal regulations. It justified its decision, among other things, by the fact that the equality of entities (the landlords on the one hand and the tenants on the other) had been breached and the proprietary rights of certain groups of owners had been limited. By the Court's decision, the decree should have become null and void by the end of 2001 and new terms and conditions when negotiating the level of rent should have come into force as of the beginning of 2002. However, no new act was accepted by parliament up to the end of 2001 and a new edict introduced by the Ministry of Finance was again declared null and void by the Constitutional Court in November 2002. Interestingly, at the time the government was willing to employ somewhat substandard legislative tricks in order to prevent the second edict being overruled. Once the Ministry of Finance learned that the edict was likely to be thrown out by the Constitutional Court it immediately issued a new one, which was an exact copy of the first one. Ministry representatives were hoping that while the Constitutional Court would overturn the original edict it would not extend that decision to the second edict issued under a different number. The Constitutional Court did not acquiesce to this governmental trick and abolished both edicts (including the copy).

Between 2002 and 2006 rents were nominally frozen (depreciated in real values!) as no further legislation was passed in parliament and rents could not be increased unilaterally by landlords (without the consent of the tenant). In the closing months of 2005 parliament passed the Rent Act allowing for gradual increases in regulated rents from the beginning of 2007 (the start of the second phase of deregulation was postponed due to the elections). The goal of the Act was to increase regulated rents to their market values up to the end of 2011; however there is a fear that under the conditions incorporated in the Act regulated rents will not reach their market values in this time. The act stipulates that over a five-year transitional period regulated rent is to increase differentially in different regions to a level that approximately corresponds to the level of market rent, and then a new, 'second generation' system of rent regulation (Lind, 2001) is to be set up – the system of 'locally relevant rent' used, for example, in Germany.

Despite this proposal private landlords and many representatives of municipalities with thousands of charges turned to the European Court for Human Rights in Strasbourg and asked for state compensation for the loss caused by the regulations. In 2006 the Constitutional Court of the Czech Republic decided that the state should compensate landlords for the losses

incurred by regulation because the state had postponed the solution of the problem for such a long time.

Municipalities acquired the right to manage, rent and sell public housing. Unlike the right-to-buy policies used in the UK and most other transition countries, no Czech law set forth any method of price calculation by which the municipal council should sell flats to the tenants, nor were the tenants given the right to buy as well. It was left entirely to the consideration of the municipal council to determine the price and the dwelling stock for privatisation. Thanks to the chaotic course of privatisation, many municipal rental flats, at least in the initial stage of transition, were 'saved' from privatisation (unlike the situation in Hungary or Estonia) and rental housing still formed a substantial part of the Czech housing stock in 2001.

However, insufficient fiscal decentralisation, the large inherited debt on housing maintenance, rent regulation and strong tenant protection all created incentives for the privatisation of municipal housing. Unlike in other transition countries, Czech municipalities were not asked by the state to sell their stock but the incentives mentioned above (along with the fact that privatisation was generally popular among tenants and may have ensured better local election results) led to an acceleration in housing privatisation, especially in the second half of the 1990s and after 2002. Despite the gradual increase in the price of privatised housing units, purchasing a flat through privatisation was always several times less expensive than the cost of purchasing a flat of equal quality on the open market.

The decentralisation of power in this field was truly substantial. For example Prague (with a population of 1,169,000 of inhabitants) is divided into 22 administrative districts and 57 independent municipalities. Each of the 57 municipalities has its own elected council, board and mayor. Act 172/1991 transferred originally state housing stock to the ownership of the city of Prague. But based on the Act on the Capital City of Prague and Status of the Capital City of Prague, the overwhelming majority of the housing stock is managed independently by 'municipalities' (municipalities decide on privatisation, rent setting, allocation criteria, etc.). There is, therefore, a variety of privatisation approaches within the city. Some municipalities (e.g., Prague-Řepy) decided not to privatise even one dwelling till 2001, others (Prague 1) decided in the same time to privatise almost all public housing stock. The same applies for the whole territory of the Czech Republic that has been divided into more than 6,000 independent municipalities; when taking into account the size of population (about 10 million inhabitants) the Czech Republic belongs among countries with the highest level of decentralisation in Europe.

Municipalities usually privatise housing only by offering it to sitting tenants. Precise statistics on scale, forms of privatisation or price discounts are missing entirely. The municipalities are not obliged to provide any such information to the central administration or to the Czech Statistical Office. The

Table 3.4 Privatisation of municipal housing in the Czech Republic, 2001

Privatisation stage	Share of municipalities
Already finished	22.5%
Continuing	71.9%
In preparation	2.2%
Has not happened and is not planned	3.4%

Source: LGHS

Institute for Land Development (UÚR) conducts regular surveys among 50 selected Czech cities and in large cities they conduct additional surveys in several small boroughs that are free to dispose of municipal housing; the institute sends the questionnaire to some 114 municipalities and independent boroughs. According to the results of this non-representative survey 39% of all original municipal dwellings were privatised by 2000, 45% by 2001 and 51% by 2002. Therefore municipalities owned only about 30% of their original housing stock by 2006.

Another source of data is the *Local Government and Housing Survey* (LGHS, see above) conducted among all municipalities with a population above 5,000 inhabitants, but only in the year 2001. From the respondents of this survey, nearly all the municipalities were involved in the privatisation of municipal housing. Nearly one quarter of the municipalities had already finished their sales while over 70% of the local governments intended to continue with privatisation in the future (Table 3.4).

Up to 1994 public housing privatisation was in the form of the sale of whole buildings into the ownership of housing cooperatives established by building tenants for the specific purpose of privatisation. Since 1994 the new Act allowed the division of buildings into separate housing units and common areas and thus allowed the privatisation of separate housing units directly to tenants. The Act on Ownership of Apartments and Non-Residential Premises (Act No. 72/1994) that allowed the creation of a condominium form of privatised apartment houses was amended often (in 1994, 1996, 1999, 2000, twice in 2001, 2003 and 2005). The amendments of 2000 and 2001 were substantial. The high number of amendments shows how fragile the legislative framework was that dealt with the management of condominiums. The main reason for legislative changes was the inappropriate framework for effective management of the newly established Homeowners Associations. The original Act in 1994 did not even include the obligation to establish a separate legal person after the privatisation of individual housing units. The management form of building and even the fact whether any kind of housing management would appear was left completely to the will of the new homeowners. The Act lacked regulations on how to make common decisions among various homeowners, regulations for specifying who would represent them with third parties and the procedural options for solving problems arising if a full consensus among homeowners concerning management or modernisation of the house were not achieved.

The Act did not presume that municipalities would start using it as their main legislative framework for further public housing privatisation or that the condominium form would expand. The authors of the Act assumed that municipalities would continue privatisation in the original manner – by sell-

ing whole buildings into the cooperative ownership of tenants. The consequences of the incomplete legislative framework to the management of houses after the privatisation were highly significant. Many privatised houses were left unmanaged, the achieving agreement among homeowners was very difficult, there were no legal prescriptions for dealing with 'free-riders', those in breach of effective management or in arrears. There was a clear need for a substantial amendment to the Act.

This amendment came about with Act No. 103/2000 (passed in 2000) that first defined a duty to establish (by notary deed) a separate legal person – the Homeowners Association – and register it in the Business Register, if there were more than five housing units and more than two homeowners in the building. The Homeowners Association is not, however, established by its registration but automatically *ex lege* when a third privatised house homeowner is registered as a new dwelling owner in the Cadastral (real estate) Register. Though in such cases (registration of the building's third homeowner in the Cadastral Register) homeowners were also obliged to establish the association formally, the Act did not state any terms for doing so or sanctions if it did not happen. Thus, new homeowners often remained passive for years, thus sustaining the problem of ineffective house management.

Moreover, following registration in the Business Register the associations began to be perceived as businesses and therefore also had to register with the Tax Office and pay income tax. Another unintended consequence of the registration was that homeowners started to be responsible for the liabilities of the association by their full wealth (not just limited to the value of their dwelling), and therefore homeowners could lose not only the dwellings they own, but also their other wealth and property in the case of an association's insolvency. The next amendment of the Act in 2001 removed the problem of tax registration and income tax payment but did not set forth other needed amendments concerning the duty to establish an association formally with due time.

According to Act No. 103/2000 the Assembly of Homeowners is the main body of the association and it consists of all homeowners in the building. Each homeowner has the right to vote in meetings of the Assembly according to his or her ownership share – the size of a share is generally computed as the proportion of the floor area of the dwelling in the sum of the total floor areas of all homeowners (or owners of commercial premises) in the building. In general, the Assembly may pass the resolutions if half the homeowners are present at the meeting (more precisely, homeowners possessing more than half of the total sum of shares) and approval of a resolution needs only a simple majority of those homeowners present. However, the Act explicitly specified that in the case of any change to some parts of the Association Charter a quorum of three-quarters of all homeowners would be required. Full consensus among all homeowners was required for resolutions dealing with mod-

Table 3.5 Tenure structure change in the Czech Republic, 1991 and 2001

	1991		2001	
	abs.	%	abs.	%
Living in own family house	1,367,027	36.9	1,371,684	35.8
Living in own flat	31,164	0.8	421,654	11.0
Rental housing	1,465,231	39.5	1,092,950	28.6
Cooperative housing	697,829	18.8	548,812	14.3
Tenants cooperative	–	–	103,216	2.7
Others	144,430	3.9	289,362	7.6
Total	3,705,681	100.0	3,827,678	100.0

Sources: Census 1991, Census 2001, Czech Statistical Office

ernisation, refurbishment, and reconstruction (mostly interpreted as ‘substantial’ decisions) or in the case of taking a loan. As this was shown to be an overly restrictive and ineffective regulation (many homeowners did not live permanently in their flats or one homeowner could block a decision agreed upon by all other homeowners in the association), full consensus in the case of modernisation or reconstruction was replaced by the three-quarters quorum in the last amendment of the Act in 2005 (Act No. 171/2005). Since then several governments have prepared a new Act that should completely replace the original Act (No. 72/1994) and all its later amendments. The proposals have been discussed several times in parliament but have not yet been passed.

Privatisation also had a significant effect on the cooperative housing sector. The basic objective of the Transformation Act No. 42/1992 (which regulated the transformation of all types of cooperatives, especially agricultural cooperatives), was to increase the ownership entitlement of cooperative members to used cooperative flats. Cooperative members occupying cooperative flats, unlike occupants of municipal flats, acquired the right to ‘sell’ their flats (in reality, to transfer cooperative ownership share together with the right to occupy particular cooperative flats) on the free market (i.e., at a market price) and in particular the right to the free-of-charge transfer of a cooperative flat into their full ownership. Cooperative housing thus became virtually part of the homeownership tenure though formally remained part of the rental sector.

All the aforementioned processes (restitution, free-of-charge transfer of the housing stock from state ownership to municipal ownership, cooperative and public housing privatisation) were reflected in a significant change in the tenure structure. This change can best be demonstrated by comparing the results of the censuses conducted in 1991 and 2001. Table 3.5 clearly shows a marked increase in homeownership rate (by more than ten percentage points) between 1991 and 2001 and conversely a reduction in the share of rental flats by almost 11 percentage points. The share of cooperative housing also decreased, by more than four percentage points.

Table 3.6 provides the tenure structure in Prague in the years 1991 and 2001. The table clearly indicates that while the percentage of people who

Table 3.6 Tenure structure change in Prague, 1991 and 2001

	1991		2001	
	abs.	%	abs.	%
Living in own family house	53,732	10.8	55,893	11.2
Living in own flat	4,236	0.9	54,796	11.0
Rental housing	327,360	66.0	234,599	47.2
Cooperative housing	96,574	19.5	64,737	13.0
Cooperative of tenants	-	-	60,646	12.2
Others	13,902	2.8	26,269	5.3
Total	495,804	100.0	496,940	100.0

Sources: Census 1991, Census 2001, Czech Statistical Office

owned their family house in Prague remained almost unchanged between 1991 and 2001, there was a significant increase in the percentage of privately owned flats (by 10%) and a significant decrease in the percentage of rental flats (by almost 20%) out of the total number of permanent-residence dwelling units. The percentage of cooperative flats also decreased noticeably (by more than 6%).

3.6.3.3 Demand-side subsidies

At the start of the economic transition households received an aggregate social benefit – the state compensatory subsidy, which was designed to offset increases in the cost of living and especially the increase in food prices. After 1993 a new social benefit was created for tenants of rental and partially also cooperative flats – the rent subsidy. Households were entitled to this subsidy if their household income was less than 1.3% of the subsistence minimum level. In January 1996 the Act on State Social Assistance came into effect and defined the form of the housing allowance for a long period of the transition (till 2007). This housing allowance was intended for households with incomes lower than 1.6 times the subsistence minimum (up to 1998 only 1.4 times the subsistence minimum); the amount of allowance thus depended on household income, size and composition. The allowance (*HA*) was calculated using the following equation:

$$HA = TC - \frac{TC \times Y}{SM \times 1.60}, \text{ where}$$

TC - notional 'tariff' housing costs;

Y - household income;

SM - subsistence minimum.

The housing allowance did not take into account the real but only notional (tariff) housing costs that were set at a relatively low level (with reference to regulated rents). It was tenure neutral, that is, allocated among both tenants

and homeowners. In general some 7-9% of households were the recipients. The level of housing allowance and notional housing costs did not reflect existing regional differences in market rents or house prices or the difference in housing costs between households living in rent-controlled housing and households paying market rents. In 2007 a new housing allowance was introduced that overcame many drawbacks of the first housing allowance concept. However, the inadequate reflection of both housing market segments (regulated versus market rents) and large regional disparities in level of rents remained. There is no necessity to provide details on this new allowance as it was introduced after the period my book concentrates on.

3.6.3.4 Supply-side subsidies

Neither social housing nor non-profit housing associations were legally defined in the Czech Republic. The government however started to support new municipal rental housing construction in 1995 through subsidies amounting, a bit later on, to CZK 400,000 per new dwelling (EUR 14,200 in current value; about one third to one quarter of the average dwelling construction costs in the second part of 1990s). The output equalled to 62,000 housing starts between 1995 and 2002. Due to the fact that there were no bidding cost or income ceilings (targeting) for dwelling allocation and mainly the fact that the programme was transformed in a way that allowed speculation and abuse, it was highly criticised and, ultimately, amended considerably in 2003. The original programme allowed for the creation of cooperatives between municipality and participants (future 'tenants'): a municipality, with the help of a commercial developer, often secured only the state subsidies and the remaining costs of house development were covered from down-payments by future 'tenants' and commercial mortgage loans. Though the right to buy was allowed only after 20 years from the year of completion, the share in the housing cooperative could be liquidated immediately under valid legislation.

Many cooperative flats constructed from by this form were therefore soon sold or rented out by participants profiting from state subsidies; moreover, some flats were constructed only as secondary homes and some as luxurious dwellings. The cooperative form was forbidden in 2003, when cost and income ceilings were also introduced; on the other hand, the subsidy was increased to a maximum of CZK 630,000 (EUR 22,500) per dwelling. The abuse of the original system was criticised by the National Control Office in 2005 when it was discovered that high political representatives were also engaged in the programme.

The supported housing programme (introduced in 2003) was aimed at supporting the construction of supported municipal rental flats for people with disadvantages in access to housing, particularly owing to health reasons (people with disabilities) or age (the elderly). Supported flats include special flats

for citizens with disabilities and flats in buildings with care services for the elderly, and also flats in halfway houses (for citizens living in some sort of conflict situation, risk environment or other special circumstances. This refers for example to young people leaving children's homes, people released from therapeutic and psychiatric care, shelters, social care institutes, prisons, or people living in segregated localities or dysfunctional families). It also refers to start-up flats (for citizens who having tried all other social and housing policy programmes still found housing inaccessible, young people who on reaching adulthood left children's homes, people who were undergoing re-socialising programmes in halfway houses or shelters, people with refugee status, etc.).

The capital subsidy in the form of a grant was allocated for the construction of the supported housing. The recipient of the subsidy was a municipality or group of municipalities. They were only allowed to combine financial resources with legal entities that were not engaged in commercial activities and were founded for the purpose of providing health or social services (with the exception of start-up flats, in which case financial resources could not be combined); the municipality had to however retain a majority share and was not allowed to ask for any financial contribution from future tenants. The privatisation of flats into the tenants' ownership, the subleasing of flats, the sale of flats to a third party, or the mortgaging of flats for credit (with the exception of credit to acquire flats) were banned in the programme. The rental price was regulated but not at the low level of regular regulated rent.

3.6.3.5 Subsidies to promote homeownership

Owing to the sharp withdrawal of the state from financing new housing construction in the early 1990s, which manifested itself, among other ways, in a decline in housing construction, it became necessary to establish conditions conducive to the introduction of standard financial market-based housing finance instruments. The first such instrument was the housing savings scheme, introduced as early as 1993, which represented a combined savings and credit product. The state supported the savings part of the scheme by state premium – its amount has decreased since 2004 when the Amendment to the Act on Building Savings was approved. The value of the state premium amounts to 15% of the annual deposit up to the limit of CZK 3,000 (approx. EUR 105 nowadays²⁰), 25% of the sum of the annual deposit up to CZK 4,500 (EUR 158) between 1993 and 2004. The housing savings scheme became a popular general savings product; as a consequence, payment of state premiums

²⁰ The average exchange rate for the period from January to September 2006 published by Czech National Bank (Central Bank) was used for this calculation (1 EUR = 28.441 CZK).

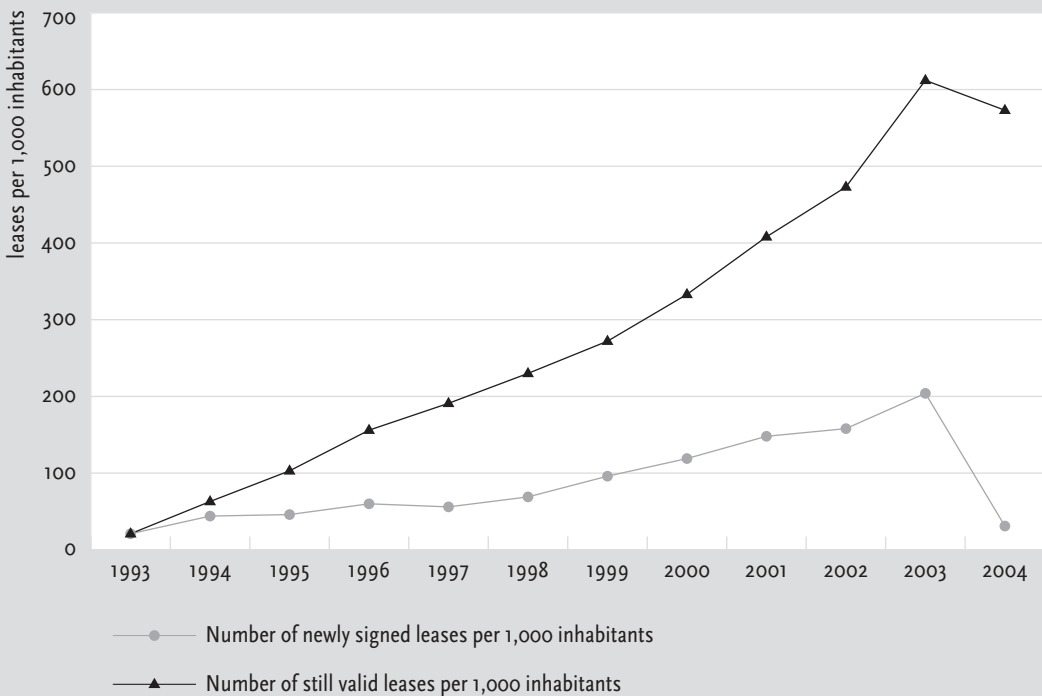
became a substantial financial burden for the state budget. The amount of state support grew from just under CZK 0.3 billion (EUR 10.5 million) in 1993 to CZK 15 billion (EUR 527.4 million) in 2004. The cost of state premiums represented in 2004 and 2005 more than half of all state housing expenditure.

The housing savings scheme operated as a 'closed' system as in Germany or Austria (*Bausparkasse*), where loans were funded from deposits of banks' clients. In other words, housing savings banks did not use additional funding (except the yields gained on the financial market due to investments of free financial resources into secure assets specified by law). Participation in the housing savings scheme could be divided into three basic phases – savings, granting of loan and repayment of loan. In the first phase clients accumulated deposits on their accounts in housing savings banks. If the client didn't want a loan, the minimum savings period for eligibility for the state premium (calculated as stated above) was six years. If the client wanted a loan from the scheme, the minimum savings period was two years (but the client had to meet further conditions set by the housing savings bank if he/she wanted a loan so early). The client could also obtain a 'bridging' loan sooner than the regular loan (i.e., even immediately after starting to save). The difference between the deposit interest rate and the regular loan interest rate (the interest margin for housing savings banks) could not exceed three percentage points. During the third phase the loan was paid back in annuity instalments and the interest rate was fixed for the whole maturity of the loan. There was the legal right of early repayment anytime during the maturity without prepayment penalty. Interests paid from building savings loan could be deducted from income tax base (tax relief).

After 2004, the housing savings bank began using the potential of mortgage financing by offering special mortgage products – extending loans with long maturity to clients immediately, that is, even if the client does not have a saving account with the bank. In fact, these 'mortgage' products are combinations of a 'bridging' loan and a regular loan from the housing savings scheme. The 'bridging' loan is usually granted at a higher interest rate than the regular loan. In the beginning, the clients paid back only the interest of the 'bridging' loan and at the same time saved deposits to meet the criteria for being granted the regular loan. When the granting criteria for the regular loan are met, the principal of the 'bridging' loan is paid off by the regular loan.

As Figure 3.7 shows, housing savings scheme became very popular especially for household general savings. The system played a very important role at the beginning of transition when mortgage legislation was missing or loans were unaffordable for most of the population. Annual inflation was high while the standard fixed interest rate on housing loan from the scheme was equal only to 6% p.a. However, the comparative advantages of the system, clearly visible in the 'high inflation-high interest rate' environment, gradually disappeared. The product remained popular among the public but only as an ad-

Figure 3.7 Number of newly signed and still valid leases per 1,000 inhabitants of the Czech Republic, 1993-2004



Source: own computation, Association of Czech Building Savings Banks

vantageous savings vehicle (thanks to state premiums); the reality of the system thus departed from its original goals. Moreover, state support for housing savings led to a very high public financial burden: the biggest explicit housing subsidy. It is sometimes argued that the entire programme is not a part of housing policy but more a form of state support for general household savings.

Mortgage loan is clearly the most common means used to finance the construction or purchase of a flat or house in developed countries. In the Czech Republic the necessary legislation for the extension of mortgage loans was passed in 1995. Mortgage financing did not spread as quickly as expected. This was mainly due to the macro-economic situation, particularly inflation and high nominal interest rates on mortgage loans (in 1995 the nominal mortgage interest rates were around 11% and in 2000 they were still around 8.5%), but there were also psychological reasons: people were wary of taking on a large debt for a long term (and unsure about their capacity to repay in the future), the future course of interest rates was uncertain, and there was still a feeling that living in debt is somehow immoral (Lux et al., 2005).

Since 1995, the state had provided *interest subsidies* for mortgage loans extended to physical persons for the purpose of acquiring their own housing (at first this applied only to newly constructed housing, but later it was extended to acquiring older housing by young first-time buyers) to tackle the 'tilt' prob-

lem. The subsidy was directly linked to the development of interest rates in the economy. More precisely, the value of the interest subsidy was set for a given year according to the average nominal interest rate from newly granted mortgage loans to physical persons during the previous year. From 1995 to January 2001 the interest subsidy on mortgage loans extended to new housing construction or purchase of new housing amounted to four percentage points, from 2001 to January 2002 it amounted to two percentage points and from 2002 to January 2003 to one percentage point.²¹ There has been no such subsidy since 2003. The amount of mortgage loan that could be subsidised was limited (the aim was not to subsidise luxury houses or flats). In 2002 the interest subsidy on mortgage loans for young first-time buyers was also introduced. The applicants for the subsidy could not own another flat or house (except the flat or house that would be subsidised) and the subsidy could only be used to acquire older housing (at least two years on from the date of official approval of a flat for use). The subsidy amounted to three percentage points from 2002 to January 2003, to two percentage points from 2003 to January 2004 and to one percentage point from 2004 to January 2005. The next section will show that the influence of the interest subsidy on the volume of mortgage loans granted (and volume of outstanding mortgage debt) was quite limited.

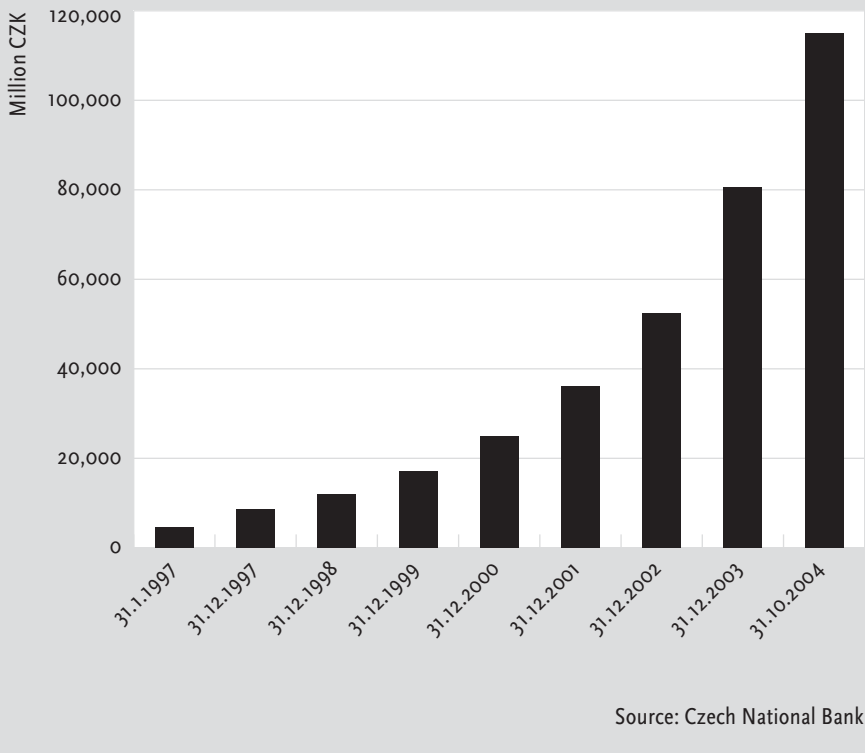
Borrowers were also entitled to *tax relief*. They could deduct the volume of annually paid mortgage interests (up to the limit of CZK 300,000 or EUR 10,548) reduced by the potential state subsidies from their tax base (for the purpose of personal income tax).

3.6.4 Housing finance

The market-based housing finance system in the Czech Republic can generally be classified as deposit-based housing finance system comprising both universal and housing savings banks. Under current legislation the universal banks can also issue mortgage bonds (be active in mortgage banking) and they use this option. In summary, the lenders use retail banking (deposits), housing savings and sales of mortgage bonds to raise funds for mortgage (housing) loans. In 2005 eight universal banks in the Czech Republic were licensed to extend mortgage loans and an additional two banks were licensed and specialised exclusively in mortgage banking (mortgage banks). Altogether there were ten mortgage lenders. There were another six housing savings

²¹ The interest subsidy amounted to four percentage points in the years when the average interest rate from newly granted mortgage loans was higher than 10%; to three percentage points when the average mortgage interest rate was equal or higher than 9% but lower than 10%; to two percentage points when the average mortgage interest rate was equal or higher than 8% but lower than 9%; and to one percentage point during periods when the average mortgage interest rate was equal or higher than 7% but lower than 8%.

Figure 3.8 Volume of mortgage credit extended to households in the Czech Republic, 1997-2004 (million CZK)

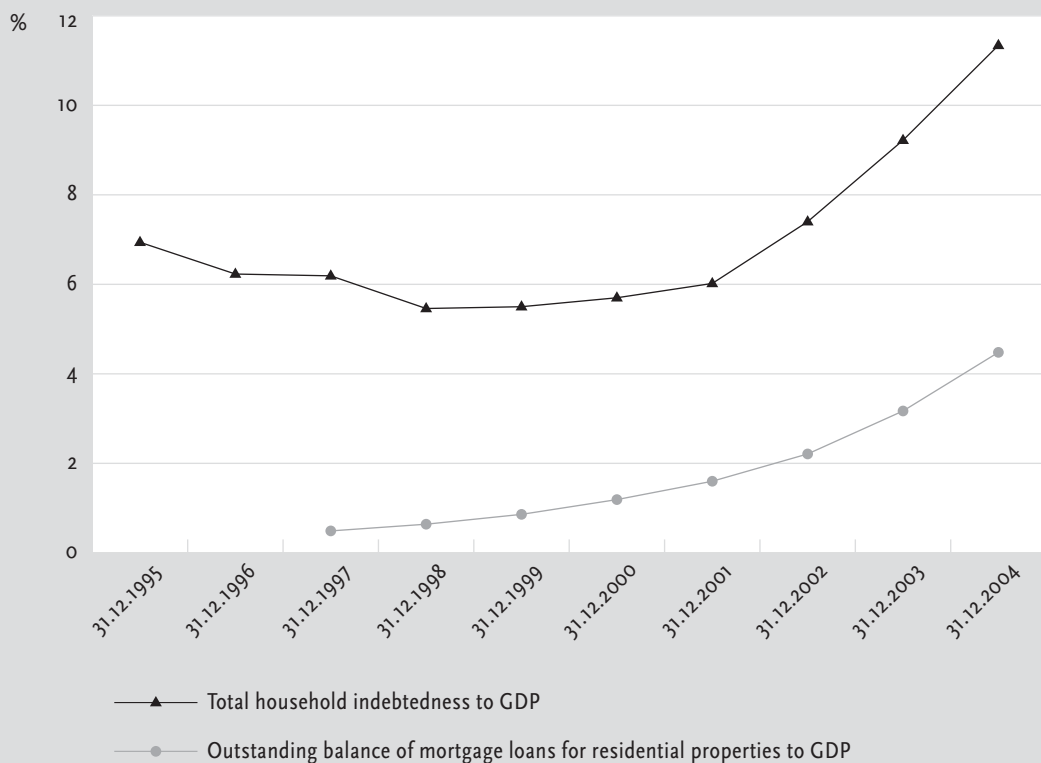


banks that extended fixed-interest rate housing loans.

According to the official statistics (see Figure 3.8) the level of Czech household indebtedness started to grow sharply from the beginning of 2000. The increase in household debt was closely connected with the growing volume of outstanding housing loans. In January 1997 the outstanding mortgage balance amounted to only 4.4% of total volume of outstanding loans. In February 2005 this share (including the outstanding balance of housing savings banks) was already equal to 67.4%. The rapid increase in levels of outstanding housing loans was especially connected with the economic upturn, that is, falling nominal interest rates, inflation, growing household disposable income and growing GDP (see Table 3.7).

Figure 3.9 shows the total household indebtedness to GDP and the ratio of outstanding mortgage balance to GDP in 1995-2004. Despite the fact that household indebtedness in the Czech Republic has risen quickly since 2000, final values were still low in comparison with the situation in other developed EU countries (Table 3.8). The share of outstanding loans for residential purposes from the total outstanding loans granted to households almost doubled between 2002 and 2004 but it was still quite far from the average ratio known in EU-15 member states. It is necessary to mention that in the Czech Republic mortgage loans could not have been used for anything other than housing purposes up to 2003, whereas in EU countries equity withdrawal mortgages were already common for almost a decade. The residential debt on

Figure 3.9 Total indebtedness of households and outstanding mortgage balance to GDP in the Czech Republic, 1995-2004



Note: Figures represent the ratio of outstanding household loans to GDP in current prices in a given year. The outstanding buildings savings loans are not included.

Sources: Czech Statistical Office (GDP), Czech National Bank (volumes of outstanding loans)

GDP in comparison with the situation in selected European countries (Figure 3.10) was relatively low even in 2005 (7.6%). Figure 3.11 shows the structure of main sources used by the Czech mortgage lenders in 2004; clearly mortgage bonds were a very popular source of loan financing.

The spread between the average cost of mortgage loans granted in 2004 (i.e., the average mortgage interest rate) and (weighted) average costs of funding of mortgage loans (i.e., rates on mortgage bonds, deposits, own capital) has been surprisingly low – equal to between 1.07 and 1.35 percentage points.²² The average gross margin, calculated as the difference between the

²² We used two methods to calculate the spread between the price of funds used by banks for financing mortgage loans and the average cost of mortgage loans (i.e., average interest rate). In the first case, cost of deposits was approximated by a five-year interest swap – IRS (here the spread was 1.07 percentage points). In the second case we used an approximation of the (alternative) cost of deposits average yield to maturity of five-year government bonds (the spread was 1.35 percentage points in this case).

Table 3.7 Basic macro-economic indicators in the Czech Republic, 1996-2005

Indicator	1996	1997	1998	1999
GDP growth (% , y/y, real terms)	4.0	-0.7	-0.8	1.3
CPI (% , y/y, average)	8.8	8.5	10.7	2.1
Average interest rates, new credits (households, in %)	12.96	12.51	11.46	9.99
Average interest rates, residential loans (households, in %)	n.a.	n.a.	n.a.	n.a.
ILO unemployment rate (% , average)	3.9	4.8	6.5	8.7
Gross disposable income (CZK bil., constant prices in the year 2000)	2,068.3	2,054.9	2,107.0	2,121.8
Gross disposable income (EUR*, bil., constant prices in the year 2000)	58.1	57.7	59.2	59.6
Net disposable income (CZK bil., constant prices in the year 2000)	1,677.3	1,650.9	1,688.8	1,688.6
Net disposable income (EUR*, bil., constant prices in the year 2000)	47.1	46.4	47.4	47.4

* Average exchange rate for 2000 published by Czech National Bank was used for calculation (1 EUR = 35.610 CZK).

Sources: Czech Statistical Office (Macroeconomic indicators, http://www2.czso.cz/eng/redakce.nsf/i/macroeconomic_indicators), Czech National Bank (interest rates)

average weighted²³ interest rate from mortgage loans granted by lenders in 2000-2004 and the average annual gross yield of government five-year bonds during the same period, was 1.44 percentage points, with the margin falling over time to a value below one percentage point in 2004. Since 2004 the Czech mortgage industry has also started offering a relatively wide range of products characterised by a broad variety of repayment methods, maturities, LTV (loan to value) ratios, interest rate settings, etc. The mortgage loan could be used until 2003 only for a limited set of purposes connected with the housing needs of the applicant; these purposes had to be proved by the client. In May 2004 the mortgage loan was defined as every loan secured by real estate; equity withdrawal mortgages were allowed and limits on maximum LTV were relaxed (this new legislative framework was sometimes called the 'mortgage revolution'). Maximum loan maturity was 30 years by 2004. The interest rate could be fixed at 1, 3, 5, 10 or 15 years according to the client's wishes and the variable interest rate was linked to financial market interest rate developments (usually annual Prague Interbank Offered Rate – PRIBOR).

The maximum LTV ratio reached 100% by 2004; repayment options included annuity instalments (most often used option), progressive payments (offered usually to persons younger than 36 years) or degressive payments. In

²³ The weights were the banks' shares in the total amount of residential loans granted to citizens up to 31 December 2004.

2000	2001	2002	2003	2004	2005
3.6	2.5	1.9	3.6	4.2	6.1
3.9	4.7	1.8	0.1	2.8	1.9
9.51	9.38	8.83	9.13	n.a.	n.a.
n.a.	n.a.	n.a.	n.a.	5.24	4.51
8.8	8.1	7.3	7.8	8.3	7.9
2,152.6	2,217.0	2,277.0	2,361.5	2,429.5	n.a.
60.4	62.3	63.9	66.3	68.2	n.a.
1,701.1	1,750.7	1,790.7	1,858.8	1,907.3	n.a.
47.8	49.2	50.3	52.2	53.6	n.a.

Table 3.8 Household indebtedness in the Czech Republic and EU countries, 2002-2004 (%)

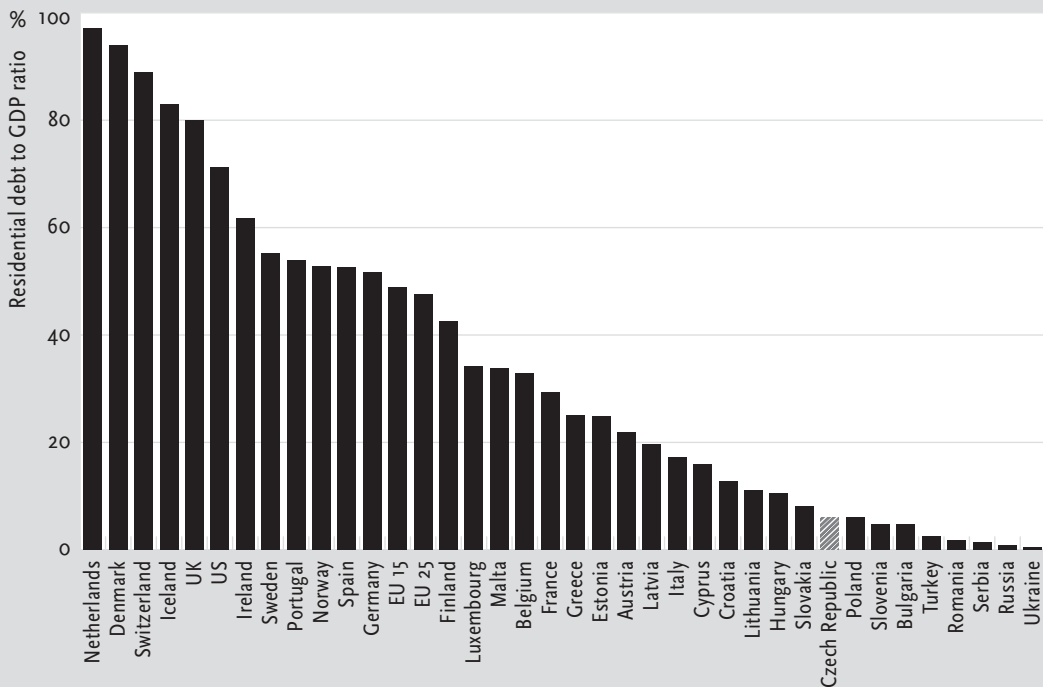
	2002		2003		2004	
	CR	EU	CR	EU	CR	EU
Household loans / total loans	19.9	44.8	24.7	45.5	30.8	47.1
Household loans for residential properties / total loans	11.0	27.2	15.1	27.9	20.4	29.2
Consumption household loans / total loans	5.8	6.5	6.4	5.7	6.8	5.8
Household loans / private consumption*	14.6	89.2	18.4	92.5	22.9	96.2
Consumption household loans / private consumption*	4.3	12.8	4.8	11.6	5.1	11.8

* In the case of Czech Republic expenditures on individual household consumption in current prices.

Sources: Own computations according to Monthly Bulletins of European Central Bank, Czech Statistical Office data and Czech National Bank

2005 'special' products appeared: a mortgage loan without additional fees connected with setting up and administering a loan, a mortgage loan combined with housing savings or life insurance ('interest-only' mortgage) and mortgage loans without proof of income (sub-prime). From 2003 there was an option to use mortgage loans for equity withdrawal. The default rate re-

Figure 3.10 Residential debt to GDP ratio in the Czech Republic, 2005



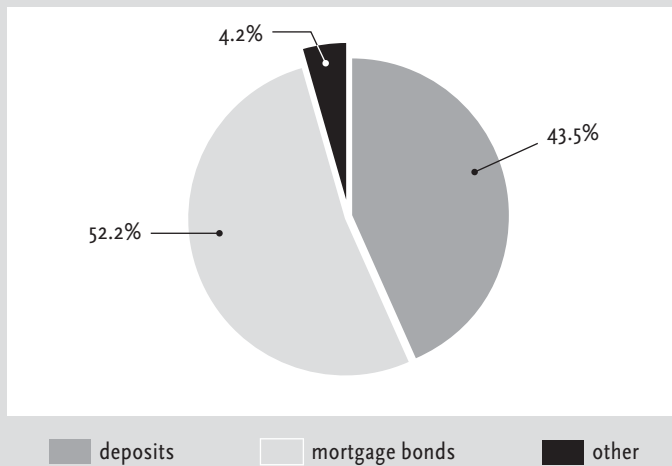
Source: European Mortgage Federation (<http://www.hypo.org/content/default.asp?PageID=202>)

mained low (in the period between 1995 and 2005 it was quite stable, around 1%) and there was a continuous decrease in average mortgage loan interest rates (Figure 3.12).

However, Czech mortgage lenders, unlike the situation in countries with advanced markets, offered no advantages targeted at first-time buyers. The solvency criteria were applied more or less across the board to all applicants. The market in 2005 still lacked some specific loan products (flexible mortgages, reverse mortgages, etc.) combined with a more elaborate supply of consultancy services on the part of specialised institutions (this changed after 2005). Another problem concerned relatively high pre-payment penalties (about 1% of the pre-paid amount annually till the end of the fixed interest rate). Taking into account the additional fees connected with setting up and administering a loan the average nominal interest rate would increase by up to 0.4 of a percentage point for a standard CZK 1 mil. loan. This increase was perceived as quite substantial and means that at the time a substantial portion of the interest costs remained, from the client's perspective, 'hidden' in the fees (this has changed, especially since 2007).

There was a relatively high degree of mortgage market concentration. The five largest mortgage lenders (measured by their share on total volume of outstanding mortgages at the end of 2004) controlled 96% of the market, and the

Figure 3.11 Structure of financial sources used for financing of mortgage loans in the Czech Republic (weighted average), 2004



Note: The weights were the banks' shares in the total amount of residential loans granted to citizens up to 31 December 2004.

Source: Mortgage loans in the CR survey, own computation

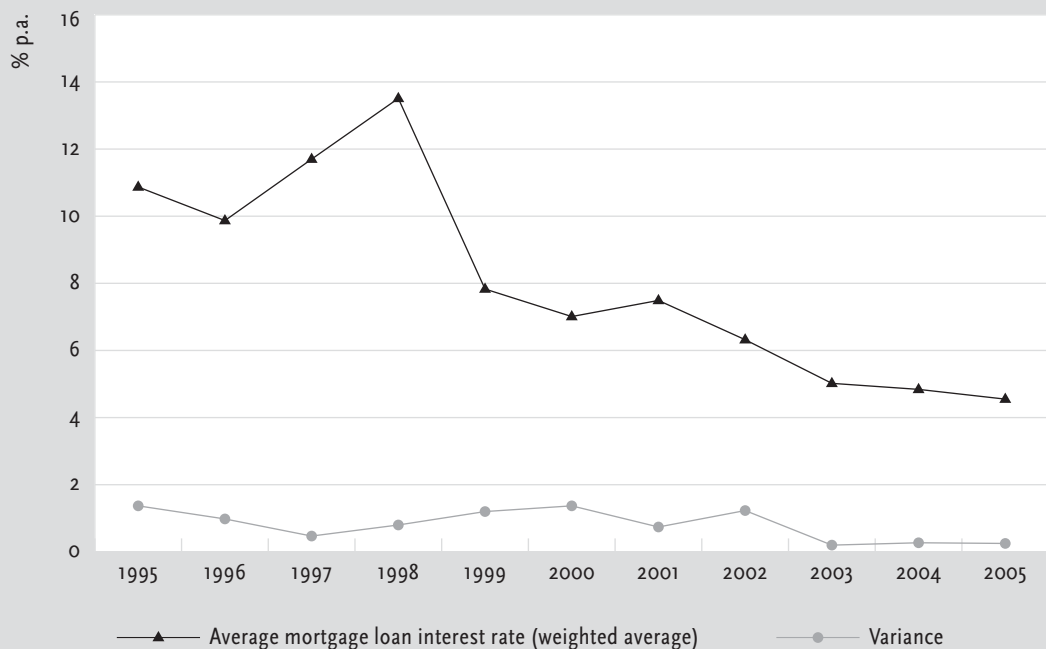
value of the Herfindahl index²⁴ (2,359 points) was and still is relatively high in comparison with Western countries. However, it can be claimed with a dose of caution that the mortgage market in the Czech Republic is not, given its size, seriously negatively affected by monopolistic or oligopolistic behavioural features.

3.6.5 Housing affordability

The aim of this section is to draw attention to the specific nature of measuring housing affordability in transition countries, which requires the use of special modelling techniques. As I will attempt to demonstrate, primary data analysis can produce a distorted image of what the real scope of the problem of housing affordability or unaffordability is, and which groups of households are truly at risk of a high housing expenditures burden. Although such specific modelling techniques proposed here are unusual within the context of housing studies and are not used in advanced countries, I believe that owing to the specific nature of the economic transformation in the former communist countries and the inadequate, poor quality statistics available in these countries, the use of the techniques described herein could produce useful supplementary information.

²⁴ The Herfindahl Index (or Herfindahl-Hirschman Index, HHI) is defined as the sum of the squares of the market shares of each individual bank.

Figure 3.12 Average mortgage loan interest rate in the Czech Republic, 1995-2005



Note: The weights were the banks' shares in the total amount of residential loans granted to citizens up to 31 December 2004.

Source: Mortgage loans in the CR survey

3.6.5.1 General problems connected with measuring housing affordability

There are three basic approaches to analysing housing affordability (Garnett, 2000): the indicator approach, the reference approach, and the residual approach. The indicator approach uses indicators to measure the household expenditures-to-income ratio. Indicators usually represent the share of expenditure on housing out of household income. Hulchanski (1995) has pointed out that housing affordability becomes a problem for households when the share of their expenditure on securing adequate housing out of their total net income exceeds a certain limit. The indicators used may vary according to how housing costs and household income are defined. Housing costs may include just the expenditure on rent (in the case of households in the rental housing sector), or they may also encompass expenditure on energy or other services connected with housing, such as the repayment of loans secured to purchase or maintain housing (in the case of households in the owner-occupied sector), etc. Housing costs entered into the calculations may or may not be decreased by the amount of the housing allowance that a household collects. Household incomes can also be calculated as gross or net (i.e., after taxes and other mandatory insurance payments). The indicator most commonly used in evaluating the financial affordability of rental housing is the share of

net rent or housing expenditure reduced by the amount of the housing allowance out of total net household income – called the rent-to-income ratio or housing expenditures-to-income ratio.

There is no fixed maximum value of ratio used in the reference approach. Instead, the reference approach refers either to the situation in another sector of housing (e.g., the level of rent is fixed according to the level of rent in the sector of private rental housing) or to the need to secure housing for certain groups of the population (e.g., rent should be set at a level that is affordable to families of employee households with a number of children and with low wages). More commonly used is the residual approach, which starts out by evaluating the level of residual income, which is the amount of total net household income, reduced by expenditure on housing and the amount of the subsistence minimum, necessary to cover the other essential living costs of the individual household members.

However, none of the above approaches fully sheds the need for a certain normatively set maximum limit that when exceeded indicates that a household's current housing is unaffordable – for example, a set maximum housing expenditures-to-income ratio or minimum residual income (hereafter affordability limit). Like any other normative judgement, it is difficult to scientifically justify a fixed affordability limit. The definition of affordability used by The National Housing Federation in the United Kingdom and applied to social rental housing states that “rent is affordable if the majority of working tenants do not fall into the poverty trap as a result of their dependence on the housing allowance or are not spending more than 25% of their net (household) income on rent” (Lux & Burdová, 2000). According to information from Bramley (1991), the Housing Corporation (an institution that monitors the activities of housing associations in the UK and also distributes state subsidies among them) used an affordability limit of 33% of the rent-to-income ratio for the rental sector that is covered by housing associations (the rule of ‘rent at 33%’, Bramley, 1991, p. 21). Except for some general housing-policy provisions, the British government does not explicitly stipulate any affordability limit. In the Netherlands the umbrella organisations of independent housing associations applied an affordability limit that equals 25% of the housing expenditures-to-income ratio in the (predominant) social sector of rental housing, while in the United States the US Department of Housing and Urban Development (HUD) applied the principle of ‘fair market rents’ in the sector of rental housing at a 30% rent-to-income ratio (Kaufman, 1997; Mulroy & Ewalt, 1996). As for Switzerland, Thalman states, “The generally accepted affordability limit for rental housing in Switzerland, like in many other countries, is such that basic expenditures on housing should not exceed 25% of household income” (Thalman, 1999, p. 1941).

Some countries did not explicitly set an affordability limit, but it was implicit in the policy the state develops for its targeted housing allowance. Hills

has noted that the “idea behind the German model of the housing allowance is that rent for adequate housing should not exceed 25% of total household expenditures; though it may be as much as 30% for single-member households” (1990, p. 160). There is always a normative and even subjective judgement involved in setting an affordability limit, and it would be difficult to determine such a limit by ‘objective’ means, as any method selected for this purpose can easily be questioned from a scientific perspective. A certain development in this regard is the ‘quasi-normative’ approach to housing affordability (Lux, 2007), used in this book for the assessment of efficiency of rent regulation in the Czech Republic.

The normative aspect of determining the affordability limit is moreover just one of the problems connected with measuring and evaluating housing affordability. Every indicator used to measure how affordable housing is for various groups of households must also be able to address the fact that an analysis of housing expenditures alone does not sufficiently take into account the quality of housing, the size of the housing inhabited, the protection of tenant rights, and other costs connected with housing (e.g., the costs of commuting). The main disadvantage to the concepts of housing expenditures-to-income ratio and residual income is that they do not adequately take into account the individual attributes of housing, especially quality and location. A high housing expenditures-to-income ratio (which at first glance looks like a problem of housing affordability), for instance, need not necessarily result from low household income or a generally high level of housing costs, but may instead derive from the fact that these households are living in flats that are too luxurious and/or too large in relation to their household size (e.g., a two-member household living in a four-bedroom flat). Were such households to move to more appropriate housing (which, again, can only be defined normatively), then the housing expenditures-to-income ratio might decrease to a level that is not defined as unaffordable. A simple unadjusted calculation of the housing expenditures-to-income ratio may therefore give a distorted picture of how many households are genuinely struggling with housing affordability. Consequently, many studies further refine the housing expenditures-to-income ratio so that it better takes into account so-called housing over consumption (or under consumption) and housing quality.

An inspirational contribution to improving the measurement of the affordability of rental housing was made by Thalmann (1999), who tried to include the physical condition of the housing and the amount of housing consumption directly in the calculation of the housing expenditures-to-income ratio (and thus in the calculation of housing affordability). “Some households expend a large part of their incomes on housing because they wish to live at a high level of comfort ... on the other hand, the conventional index of affordability overlooks needy households that are spending less on housing than the affordability limit. Many of those households are living in housing that is

insufficient in size or quality, not because they would prefer to spend their incomes on other goods, but simply because they cannot afford adequate housing” (Thalmann, 1999, p. 1933). In order to determine what ‘adequate’ housing is, it is again necessary to apply certain norms. Thalmann applies a rule where an adequately sized flat is one in which the number of habitable rooms equals the number of inhabitants. His findings reveal widespread housing over-consumption in Switzerland, that is, the high standard of housing demanded by individual households. The data show that “85.4% of households in the sample over-consume housing” (Thalmann, 1999, p. 1938). His results indicate that while 18% of households have a housing expenditures-to-income ratio higher than 25% (i.e., higher than what is normatively regarded as affordable), a full 13% of households (73% of the households whose housing expenditures-to-income ratio is above the affordability limit) would be able to afford housing that is adequate for them; in other words, if they lived in adequate housing, their housing expenditures-to-income ratio would be below the affordability limit. Thalmann’s findings and his methodological approach are extremely useful for an analysis of housing affordability in the Czech Republic.

3.6.5.2 The methodology of measuring the affordability of housing in the Czech Republic

Given that the indicator approach to the analysis of housing affordability is one of the most commonly used methods in international comparisons, it will also be used in my analysis of housing affordability in the Czech Republic. The housing expenditures-to-income ratio will be especially used to observe the affordability of rental housing. In conformity with the points outlined above regarding the use of the housing expenditures-to-income ratio, the method was modified (see below) and defined as follows:

*Housing expenditures-to-income ratio = monthly expenditures of a household on housing (rent, basic expenditures, aggregate expenditures) / monthly total net household income * 100 (%)*,

where:

1. basic expenditures of the household on housing = the sum of expenditures on rent, central heating, hot water, electricity, gas, energy, water and sewage charges, and other municipal services;
2. aggregate expenditures of the household on housing = the sum of basic expenditures on housing and expenditures on structural and home maintenance, construction requirements, and the maintenance of household installations, loan repayments on the house or flat, and property taxes.

Housing affordability is analysed separately for households living in rental housing (municipal, state, and private rental flats) and households living in owner-occupied housing (privately owned flats or family homes). For the purpose of monitoring the developments in the affordability of rental housing the calculation of the housing expenditures-to-income ratio logically encompasses only the basic expenditures of the household on housing; aggregate expenditures are included only in the analysis of affordability of the owner-occupier housing.

The values of the indicators of the affordability are calculated using data from the Family Budget Surveys 1990-2003 (FBS 1990-2003) conducted annually by the Czech Statistical Office (CSO). This is an annual in-depth survey, which aims at monitoring the flows of cash and other assets in the budgets of a sample of selected households. The FBS's respondent unit is the household, that is, a group of persons who live and run a household together. Every household included in the survey maintains a survey log, in which it records its incomes and expenditures over the course of a year. In the FBS the distribution of households representing individual social categories is not designed to correspond to the distribution of such households in the population, so in my analysis weights are applied to the FBS data in order to overcome this deficiency. To do this I used coefficients derived from data from the representative Microcensus 1992, 1996 surveys conducted by the Czech Statistical Office (data files FBS 1990-1997) or weights recommended by the Czech Statistical Office (FBS 1999-2003).

The FBS does not distinguish between expenditures on secondary housing (cottages or recreational homes) and expenditures on primary housing. In 1990 14.3% of all households in the FBS indicated they also owned a recreational home (according to the results of the 1991 Census – the percentage was 12.5%), while in 2001 the percentage, according to the same source, had decreased to 12.4% of households (according to the results of the Census 2001 11.3% of households). Expenditures on secondary housing thus artificially increase the officially indicated housing expenditures-to-income of Czech households.

When calculating the housing expenditures-to-income ratio in EU countries, housing expenditures are usually purged of the sum of housing allowances intended mainly to cover a household's costs connected with housing. In the FBS up until 2003 the housing allowance was not monitored as a separate item but together with other forms of social income included in the total household income. But the fact of whether the allowance is deducted from total household expenditures or, conversely, is included to increase total income actually has a fundamental effect on the housing expenditures-to-income ratio. The following example demonstrates how: consider a household that spends CZK 5,000 a month on housing, while its total net monthly income is CZK 15,000. The housing expenditures-to-income ratio is 33.3%. As-

suming that the household is entitled to a housing allowance of CZK 1,000, if the allowance is included as part of household income, that ratio decreases to 31.3%, but if it is deducted from expenditures on housing the ratio decreases to 26.7%. This departure from an otherwise customary practice outside the Czech Republic can, especially in international comparisons, also artificially increase the officially indicated housing expenditure-to-income ratio of Czech households.

In addition to the problems mentioned here, which are specific to the work with statistical data in the Czech Republic, it is also necessary to take into account some of the shortcomings of the indicator of the housing expenditures-to-income ratio itself – especially the problem of housing over-consumption identified by Thalmann (1999). Therefore, in the analysis of housing affordability in the Czech Republic the resulting data on the housing expenditures-to-income ratio will be purged of housing over-consumption in order to avoid the Swiss situation, where households paying too much for their housing (or more exactly, whose housing expenditure-to-income ratio is above the affordability limit) also include households that are over-consuming housing but could otherwise afford adequate housing.

Becoming the owner of one's own home or flat tends to involve very high, albeit often one-off costs, which are connected with the process of property acquisition and therefore, in addition to analysing the housing expenditures-to-income ratio based on aggregate housing expenditures, the affordability of owner-occupied housing is measured using an alternative indicator – the price-to-income ratio (the ratio of the average transaction price of housing to average net household income).

Finally, housing affordability is analysed separately for various segments of the housing market. As mentioned above, two basic segments of the housing market evolved during the transition period connected with access to housing. The housing policy of the previous regime and the continuation of rent controls and the application of privatisation of public dwellings at advantageous price terms during the period of the economic transition are the main causes of the division of Czech society in terms of access to housing and ultimately also the affordability of housing into two basic, clearly distinguishable (though hard-to-define) groups:

- the segment of households enjoying the advantages of 'privileged' housing, which includes households paying regulated rent, households who acquired their own or cooperative housing in between 1948 and 1990 (socialism), and households who had the opportunity to buy their own housing during the privatisation of municipal flats after 1990, wherein flats were and still are sold at prices far below market prices;
- and the segment of households living in 'non-privileged' housing, consisting of people who, precisely because of the existence of rent controls on flats in the 'privileged' segment, are paying unnecessarily high market

rents (Lux & Sunega, 2004), and who, owing to fixed-term tenancy contracts enjoy very little legislative protection against the actions of landlords (in contrast to the protections of sitting tenants), and people who have acquired their own or cooperative housing under market conditions and paid the price set by the market.

Unlike other social inequalities this inequality in access to housing did not develop out of market pressures but exclusively through the actions of the state and municipalities and through the central and local housing policy: what is all the more remarkable is that none of the income or social criteria that usually accompany other redistribution policies were taken into account in this case (see also the insider-outsider situation as a common outcome of transitional housing policies described in the first chapter of this book). This substantial economic subsidy (in the form of either low rent in rental housing or a price lower than the market price of the housing purchased) was not means-tested, and was unjustified from the perspective of social justice (Sunega, 2005, below). However, it is not the aim to make an evaluation of the housing policy reforms here; but for the analysis at hand the important finding is that two notably distinct segments of the market have clearly taken shape. Therefore, the analysis of housing affordability was conducted separately for the 'privileged' and for the 'non-privileged' housing sectors, and the results are presented in separate sections.

Given that at the time of writing this book no other guidelines existed, the following three normatively selected affordability limits for the housing expenditures-to-income ratio are used: 20%, 25% and 33%. The most relevant affordability limit in the Czech Republic is (corresponding also to international practices) considered to be a limit of 25%. In each section devoted to the affordability of various types of housing tenure and housing in different market segments, the percentage of households whose housing expenditures-to-income ratio exceeds the affordability limit is monitored.

3.6.5.3 The affordability of rental housing in the 'privileged' housing sector between 1991 and 2003

The affordability of rental housing is monitored for the years 1991, 1993, 1995, 1997, 1999, 2001 and 2003, based on data from the Family Budget Surveys. The housing expenditures-to-income ratios relate to the 'privileged' rental-housing sector, which includes rental flats owned by the municipality, the state or private landlords in which tenants pay regulated rent. The following data adjustments were made owing to the division of the analysis into special market segments, the above-mentioned shortcomings of the FBS, and the general difficulties involved in using the housing expenditures-to-income ratio indicator:

- an adjustment of the declared level of rent, owing to the fact that the analysis in this part refers only to the 'privileged' housing sector, and that a portion of households indicated in their survey logs the higher rent paid per m² of the total floor area than how much the maximum (regulated) monthly rent for this type of flat in a given year was (this was either the result of a mistake, methodological error, or because they did not belong to the 'privileged' housing sector);
- an adjustment that takes into account expenditures on secondary housing (cottages, recreational homes), which in the FBS are not distinguished from those on primary housing;
- an adjustment that takes into account the housing allowance (which unfortunately was not observed separately in the FBS until 2003) based on the assumption that all eligible households applied for the housing allowance and the amount of the allowance consequently reduces housing expenditures;
- an adjustment that takes into account housing over-consumption in conformity with the qualitative rule that the number of household members = the number of habitable rooms (adjustment based on Thalmann, 1999).

The first adjustment of the basic housing expenditures-to-income ratio is an adjustment of the rent level so that it corresponds to the level of rent in the 'privileged' housing sector. It is likely that there are other justifications for this adjustment, as the nature of the FBS (which is almost a panel survey) is such that one can expect that the overwhelming majority of the households included in the survey do indeed live in the 'privileged' housing sector (i.e., in the rental sector paying regulated rent), but in the survey households record other expenditures connected with housing as a rent too. Given the constant and relatively large proportion of households (always around 30% of households) that in each of the years monitored (i.e., even at the start of the economic transformation, when regulated rent applied to almost every household in the rental sector) cited a higher level of rent in the survey than what was the valid maximum regulated rent at the time, it is likely that a certain portion of households, constant over time, does not just record the net rent in their logs but indicates a level of rent that in reality includes expenditures on other services connected with occupying the home/flat.

In order to account for expenditures on secondary housing the difference was determined between the level of basic housing expenditures of households that owned a recreation home and the level of basic housing expenditures of households that did not own a recreational home. Owners of recreational homes tend mostly to be households with a larger number of members, who also usually reside in larger flats and thus also have higher basic expenditures on primary housing; so the differences in the level of basic housing expenditures were calculated while taking into account the size of

the primary housing. The differences were also adjusted by a correction coefficient that accounted for the size of the municipality where the household's primary housing is located. Finally, for all households that indicated they own a recreational home the level of basic housing expenditures was reduced by the average observed difference in housing expenditures.

Another adjustment to the housing expenditures-to-income ratio intended to reflect the effect of the housing allowance (or other benefits exclusively targeting housing), which up until 2003 was not monitored separately in the FBS. Given that the main objective of this section of the book is to more accurately measure housing affordability, I have made a theoretical assumption: every household entitled to the housing allowance actually applied for it. Even though in reality this was not the case, the fact that some households did not apply for housing allowance should not artificially increase the number of households endangered by low housing affordability. The amount of the housing allowance is calculated on the basis of reported household incomes. The housing allowance is then deducted from the basic housing expenditures entered in the calculation of the housing expenditures-to-income ratio.

The problem of housing over-consumption has proven to be highly significant in the Czech housing sector. Housing over-consumption means that a household inhabits a flat that is more than adequate in size, and understandably that can have a fundamental impact on the household's housing expenditures-to-income ratio. The most commonly used standard for determining the degree of housing consumption is the number of habitable rooms in the housing in relation to the number of household members.

As the first step, the amount of the average basic housing expenditures for households in the rental sector is calculated for each flat size (the number of rooms) and for individual municipality size categories (by population size). Then, following the rule that 'number of rooms = number of household members', the degree of housing over-consumption is calculated for each household.²⁵ Based on knowledge of the actual size of the flat occupied and the amount of housing over-consumption, it is possible to determine an adequate level of housing consumption for every household (meaning a flat in which the number of rooms corresponds to the number of household members) and a level of basic housing expenditures that corresponds to flat size in a municipality of the same size category in which the household currently resides. In

25 It can be argued that 'number of rooms' is not the appropriate indicator of over-consumption as the rooms may be of different sizes. However, setting a different normative, such as minimum floor area of habitable rooms, would be very difficult as there is no benchmark that could be used for this purpose. One could always say that the selected normative is too small or too high and the consequences for housing over-consumption would then vary largely. Therefore we decided on a normative that is used relatively often in research, such as the one done by Thalmann (1999).

other words, if a household with two members resides in a three-room rental flat, then following this approach the amount of over-consumption is one room. Therefore, in the next step the household is assigned a level of basic housing expenditures for two-room flats in the same-sized municipality.²⁶

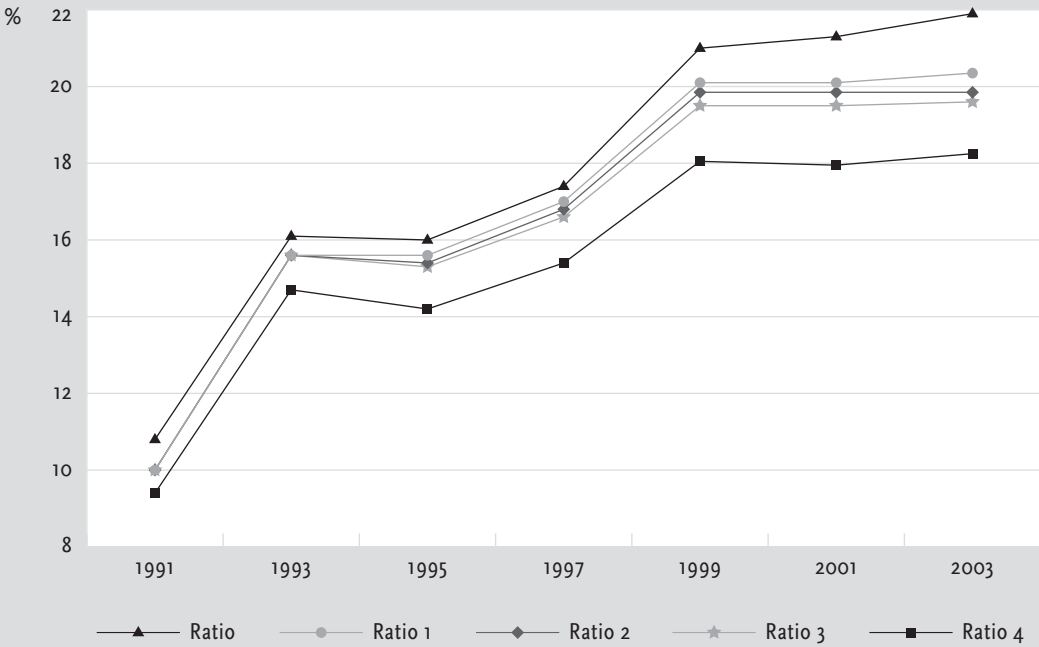
Figure 3.13 illustrates the development of the unadjusted average basic housing expenditures-to-income ratio (marked as 'ratio') for the sum of all households in the 'privileged' rental sector and the effect of the above-described adjustments on its value (marked as 'ratio 4'). The curve marked 'ratio 1' traces the development of basic housing expenditures-to-income ratio in individual years after rent adjustment. The curve marked 'ratio 2' shows the development of the housing expenditures-to-income ratio after rent adjustment and excluding the expenditures on secondary housing. The curve marked 'ratio 3' corresponds to the housing expenditures-to-income ratio after rent adjustment, excluding the expenditures on secondary housing, and reducing housing expenditures by the amount of the housing allowance. The curve marked as 'ratio 4' shows the basic housing expenditures-to-income ratio after rent adjustment, excluding the expenditures on secondary housing, reducing housing expenditures by housing allowance and adjusting housing consumption (excluding over-consumption).

Figure 3.13 illustrates that housing over-consumption had the biggest effect on the difference between the value of the original unadjusted ratio and the resulting ratio in individual years. The average value of the unadjusted housing expenditures-to-income ratio in 1991 is 10.92%, in 1993 it increases to 16.20%, in 1995 it falls slightly to 16.10%, in 1997 it reaches 17.44%, in 1999 21%, in 2001 21.31%, and in 2003 it increases even further to 21.90%. The yearly values of the adjusted housing expenditures-to-income ratio ('ratio 4') are 9.37%, 14.72%, 14.29%, 15.47%, 18.10%, 17.91%, and 18.32%, respectively. In the final year of the analysis (2003) the difference between the unadjusted and the adjusted housing expenditures-to-income ratio is roughly four percentage points, which is a relatively significant difference.

Figure 3.13 also indicates that the biggest increase in the average ba-

26 Housing under-consumption has not been computed although this had been included in Thalmann's study (1999). There are two reasons: first, under-consumption occurs far less frequently than over-consumption (as again demonstrated by Thalmann, 1999) but secondly and especially, it does not distort the indicators on financial affordability of housing in the same way as over-consumption. From the point of view of efficiency of housing subsidies, that is, from the perspective forming the main focus of this book, over-consumption 'artificially' increases the problem of financial affordability of housing. If it is not controlled for, allowances are paid to households who are just over-consuming housing. Under-consumption may 'artificially' decrease the problem of financial affordability but, again from the perspective of housing policy, it is generally not taken into account by particular housing allowance models (traditionally the housing allowance is computed from real or normative costs, whatever is lower, so if real costs are lower than normatives, the real costs are taken into the computation).

Figure 3.13 Average basic housing expenditures-to-income ratios in the Czech Republic, 1991-2003



Note: Data sets from the FBS 1991-1997 are weighted according to the Microcensus 1992, 1996; data sets from the FBS 1999, 2001 and 2003 are weighted with coefficients recommended by the Czech Statistical Office.

Source: FBS 1991-2003, own computation

sic housing expenditures-to-income ratio occurs in the years 1991-1993 and 1997-1999. The differences in the values of the unadjusted and the adjusted ratio increase during the observed period. It is interesting, for example, that the effect of taking into account the housing allowance significantly increases between 1995 and 1999, decreases slightly in 2001, and decreases more notably in 2003. The reason for the increasing effect of the housing allowance between 1995 and 1999 on reducing the housing expenditures-to-income ratio is the growing proportion of households entitled to housing allowance and the effect of supplementary housing benefits in 1997 and 1999. Between 2001 and 2003 the proportion of households entitled to the allowance decreased (from 9.4% to 6.9%), while the average amount of the allowance remained virtually unchanged.

The effect of housing over-consumption over the course of the years between 1995 and 2003 decreases – if in 1995 the over-consumption formed 58% of value of difference between unadjusted and adjusted ratios, in 2003 it was only 39%. However, this is not because there is a decrease in the proportion of households over consuming housing; on the contrary, it increases (in 1995 it was 26%, in 1999 34%, in 2001 35%, and in 2003 33%). The average amount of over-consumption in the period observed increases (from 1.13 rooms in 1995 to 1.29 rooms in 2001, and 1.27 rooms in 2003). However, the structure of over-

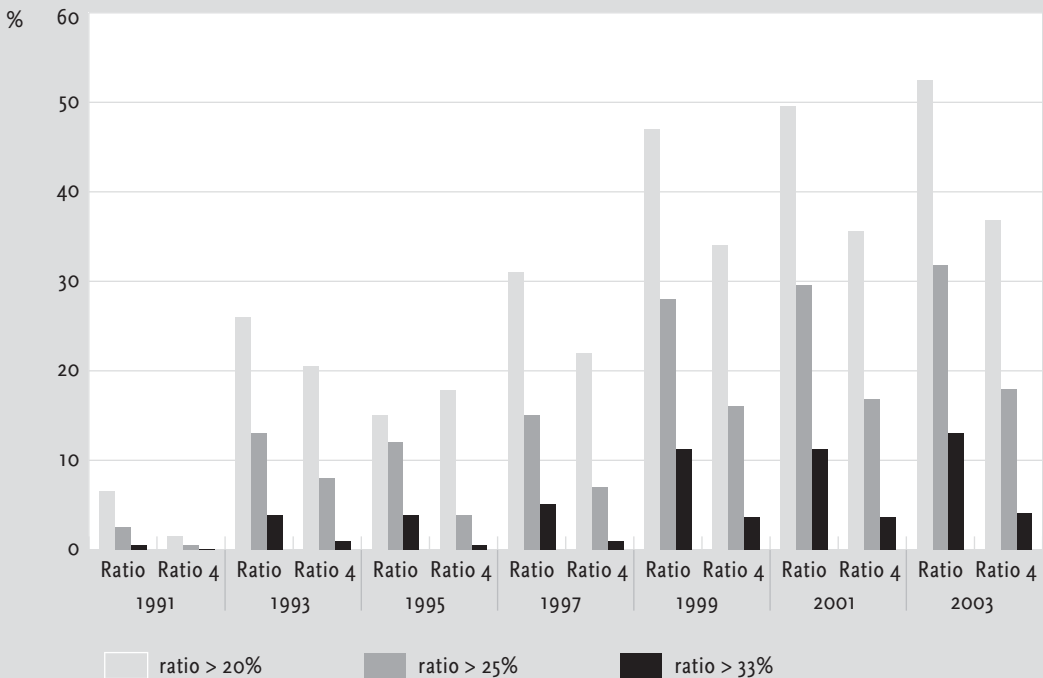
consumption changes: the number of households over-consuming housing in large flats increases, while the proportion of households over-consuming housing in smaller flats decreases. There is an economic rule that variable unit costs decrease at a larger volume; analogically, in larger flats the expenditures on one room are lower than the expenditures on one room in smaller flats. This is the main reason for this finding.

A more detailed analysis of the housing expenditures-to-income ratio for individual groups of households would reveal the worst-off position of senior-citizen households, which in all years have the highest housing expenditures-to-income ratio. However, while in 2003 the value of the average unadjusted basic housing expenditures-to-income ratio of senior citizens was 29%, when factors that 'artificially' increase the housing expenditures-to-income ratio are taken into account this figure decreases to roughly 24%, thus by five percentage points. The main cause of the big difference is the effect of housing over-consumption common in this group of households.

Figure 3.14 shows the percentages of households in which the basic housing expenditures-to-income ratio in individual years exceeds the normatively set affordability limit at 20%, 25%, and 33%. I decided that for an analysis in the Czech Republic the most relevant affordability limit would be a housing expenditures-to-income ratio of 25%. In 2003 32% of households (one-third of households living in the 'privileged' rental housing sector) show an unadjusted housing expenditures-to-income rate above the level of affordability limit of 25%; after adjusting the ratio the percentage decreases to 17%. Compared to the start of the transition period this is a vivid and sharp increase: while in 1991 the percentage of households with a housing expenditures-to-income ratio above the level of the affordability limit is just 2.6% (and after adjustments even less than 1%), in 2001, ten years later, the percentage is ten times higher.

A closer analysis of inequalities between individual age, social, income, and professional categories of households reveals that housing in the 'privileged' rental housing sector in no way means that the given household cannot end up in financial difficulty. On the contrary, the degree of inequality between the highest-income and lowest-income households grows in time and many groups of households (individuals, some senior citizens, single mothers) are exposed to a housing expenditures-to-income ratio above the affordability limit even after the ratio is adjusted. One of the reasons for this might be that the 'privileges' in this market segment are too equally distributed between 'the poor' and 'the wealthy' and overall the equally high hidden economic subsidy derived from regulated rent paradoxically exacerbates social differences instead of reducing them (Lux et al., 2004). Rent regulation is not targeted according to household income, and the housing allowance does not reflect real expenditures but rather only tariff expenditures on housing (see more on this in the next chapter).

Figure 3.14 Percentage of households in the Czech Republic with a basic housing expenditures-to-income ratio higher than 20%, 25% and 33%, 1991-2003



Note: ratio – unadjusted basic housing expenditures-to-income ratio; ratio 4 – adjusted basic housing expenditures-to-income ratio.

The data sets from the FBS 1991-1997 are weighted according to the Microcensus 1992, 1996; the data sets from the FBS 1999, 2001 and 2003 are weighted with coefficients recommended by the Czech Statistical Office.

Source: FBS 1991-2003, own computation

3.6.5.4 The affordability of rental housing in the 'unprivileged' housing sector (2002)

A real quantification of the affordability of 'unprivileged' (market) rental housing in the Czech housing environment cannot be made, as statistics on market rents are only very rarely collected by selected commercial institutions. Such surveys are limited to a small number of large towns and are based only on advertised rents. In the FBS the proportion of households truly paying market rent is marginal; this is the result of the method of data collection and also the fact that only a relatively small portion of Czech households lived in the 'unprivileged' segment of market rental housing.

However, to omit a special analysis of this sector of the market would be a distortion, and therefore I regard it as the 'lesser evil' to attempt an estimate by using a modelling approach. That method involves estimating market rent from the estimated market price of an occupied flat. Not much is known about the social and financial situation of households living in the

unprivileged market rental sector, but the majority of experts incline toward the opinion that all social groups of households are represented in this sector, though they are of lower age. Therefore, for this purpose the data from the FBS 2002 are used with one basic restriction – only households headed by a person under the age of 40 are selected for the analysis.²⁷ It is a fact that young people, after a certain period in their career, often attain on average higher incomes than older people – if we were to include in the analysis households headed by persons over the age of 40, then the resulting housing expenditures-to-income ratio would be higher, and if we were to include in the analysis households of senior citizens, then it would be much higher. However, these results could be regarded as distorted because there is little probability that elderly people will be living in market rental housing.

For rental flats of those households I estimated specific market rents as a product of average yield from residential housing investments in the Czech Republic and estimated market price of their flats. To estimate market rent it was therefore first necessary to estimate the market price of the rental flat occupied by selected household. House prices were estimated by the hedonic price (OLS) regression model (see, e.g., Lux *et al.*, 2004) using data from the Ministry of Finance and the Czech Statistical Office on the transaction prices in 2002. The hedonic price function is determined using the data set on housing prices, which includes the following variables: the date (documented by the financial bureau), type of real estate, transaction price, floor area (m²), depreciation of the property (in %), and size of the municipality and district. A series of semi-log hedonic regression models were tested with the aim of creating a model capable of maximising the percentage of the explained variability of the dependent variable (log house prices). The final model explains 63.97% of the variability of the dependent variable (Adjusted R²) and the following explanatory variables were used: floor area (m²), floor area squared, a dummy variable for the category of housing depreciation (in relation to the age of the building or the period in which it was built), regional dummies, and the size of municipality. Table 3.9 presents the model's specifications.

In order to calculate the annual market rent, the estimated price of the flat was subsequently multiplied by the annual yield of 6.5% corresponding to the net yield on investments into residential real estate in 2002. The yield value is the mean value between the value determined by the Ministry of Finance (appendix no. 34, ordinance no. 279/1997 Coll. of the Ministry of Finance) for 2002

27 Ultimately the results of our analysis do not reveal what the real housing expenditures-to-income ratio is for households living in 'unprivileged' rental housing, but rather what the housing expenditures-to-income ratio would be for younger households (with a household head aged 40 or under) from the 'privileged' sector of housing if they were to find themselves in the 'unprivileged' segment of the market. This indirect indicator makes it possible at least to some degree to compare the affordability of rental housing in both 'unprivileged' and 'privileged' housing segments.

Table 3.9 Hedonic price model (OLS), 2002

Variable	Beta	Variable	Beta
<i>Constant</i>	13.170**	Regional dummy 7	-0.662**
Area of dwelling (in m ²)	0.024**	Regional dummy 8	-0.660**
Date of construction (up to 1946)	-0.645**	Regional dummy 9	-0.720**
Date of construction (1946-1960)	-0.488**	Regional dummy 10	-0.563**
Date of construction (1961-1970)	-0.363**	Regional dummy 11	-0.784**
Date of construction (1971-1980)	-0.274**	Regional dummy 12	-0.623**
Date of construction (1981-1990)	-0.211**	Regional dummy 13	-1.156**
Date of construction (1990-now)	ref.	Regional dummy 14 (Prague)	ref.
Regional dummy 1	-0.580**	Size of residence (up to 1,999 inhabitants)	-0.988**
Regional dummy 2	-0.885**	Size of residence (2,000–9,999 inhabitants)	-0.601**
Regional dummy 3	-0.771**	Size of residence (10,000–49,999 inhabitants)	-0.423**
Regional dummy 4	-0.765**	Size of residence (50,000 and more inhabitants)	ref.
Regional dummy 5	-1.457**	Adjusted R²	0.64
Regional dummy 6	-0.845**	N	4.325

* Significant on 0.05 level of significance; ** Significant on 0.01 level of significance.

Note: Dependent variable: ln (transaction price).

Source: own computation, Czech Statistical Office, Ministry of Finance

and the value indicated by the Institute for Regional Information for 2002 (IRI 2002). The resulting unadjusted average basic housing expenditures-to-income ratio for households living in the 'unprivileged' rental housing sector in 2002 was 27.9%; after taking into account expenditures on secondary housing it was 27.7%; after taking into account expenditures on secondary housing and the reduction of expenditures by the housing allowance it was 27.3%; and after taking into account expenditures on secondary housing, the reduction of expenditures by the housing allowance, and housing over-consumption it was 25.6% (N = 326). If I use the affordability limit of 25% of the housing expenditures-to-income ratio and with knowledge of all the preliminary assumptions (this is an estimated rather than a real situation), 49.6% of households from 'unprivileged' rental housing would have an unadjusted housing expenditures-to-income ratio higher than the affordability limit and 43.7% of the same households would have an adjusted housing expenditures-to-income ratio higher than the affordability limit in 2002.

3.6.5.5 The affordability of owner-occupied housing in the 'privileged' housing sector (1991-2003)

The analysis concentrates on owner-occupied flats as there are no households living in 'privileged' family houses; if I wanted to relevantly compare the situation in the segment of 'privileged' housing with the situation in the segment

of 'unprivileged' housing then I would need to focus on the apartment segments. Results relating to the entire owner-occupied housing sector (i.e., including households occupying family homes) will be, however, also presented at the end of this section.

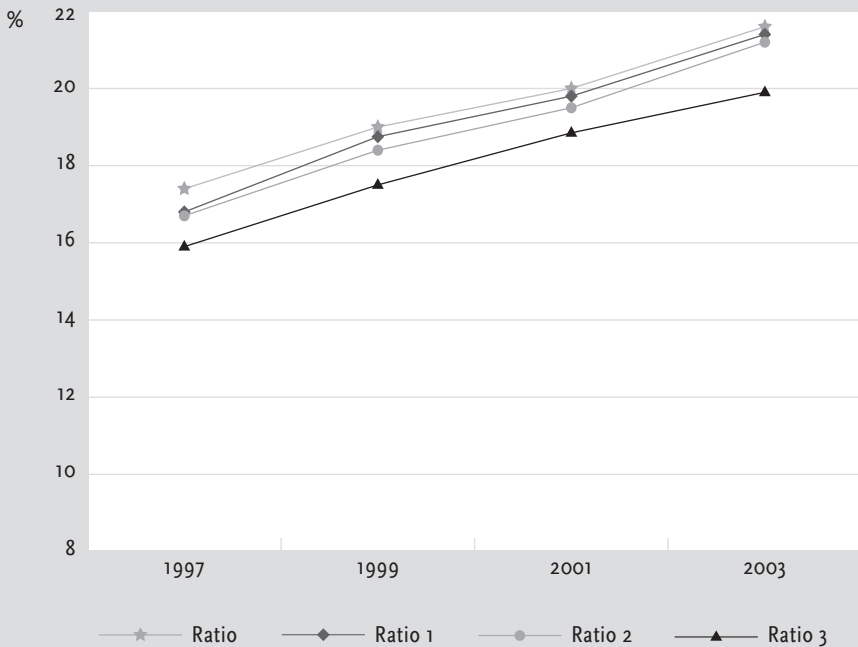
In order to evaluate housing affordability for households that acquired their flats before 1989 or did so in the process of the privatisation of flats after 1989, it is only possible to use the indicator approach (the housing expenditures-to-income ratio) on the FBS data, similar to the way it was used in the analysis of the rental sector. Given the nature of the FBS survey it can be assumed that only a marginal portion of sample households have acquired their housing on the open market at market prices; at least, there will not be enough of them for there to have any significant impact on the average results. In order to calculate the housing expenditures-to-income ratio, aggregate housing expenditures will be used (instead of basic expenditures, as in the case of rental housing).²⁸ The aggregate housing expenditures were purged of the effects of the housing allowance (since 1996 households in owner-occupied housing are also eligible for housing allowance), expenditures on secondary housing, and housing over-consumption.

Figure 3.15 shows the development between 1997 and 2003 of the average aggregate housing expenditures-to-income ratio following each of the individual adjustments; Figure 3.16 shows the percentage of households that exceed the affordability limit for the adjusted and unadjusted housing expenditures-to-income ratio. In 2003 the average unadjusted aggregate housing expenditures-to-income ratio for these households reached almost 22%; the average adjusted ratio in the same year is 20%. According to Figure 3.16, in 2003 30% of these households had an unadjusted housing expenditures-to-income ratio higher than 25%, while 20% of households had an adjusted housing expenditures-to-income ratio higher than 25%.

In 2003 the unadjusted aggregate housing expenditures-to-income ratio would be 18.5% (in 1991 just 10.5%) and the adjusted ratio would be 17.2%. In 2003, according to the unadjusted housing expenditures-to-income ratio, 21% of households living in the 'privileged' segment of owner-occupied housing would exceed the 25% affordability limit; according to the adjusted ratio the figure would be 11.5% of households. Clearly the effect of the adjustments on the levels of the housing expenditures-to-income ratio in the owner-occupied housing sector is less than it is in rental housing; but housing over-consumption remains significant, and its significance increases over time.

28 The FBS 1991 data set has no category for owner-occupied flats. In the years 1993 and 1995 the proportion of households living in this tenure was too low for reliable analysis. Therefore, the housing expenditures-to-income ratio (adjusted and unadjusted) is monitored for this segment of owner-occupied housing only during the period 1997-2003.

Figure 3.15 Average aggregate housing expenditures-to-income ratios in the Czech Republic, 1997-2003



Note: the FBS 1997 data set is weighted according to the Microcensus 1996; the FBS data sets for 1999, 2001 and 2003 are weighted with coefficients recommended by the Czech Statistical Office.

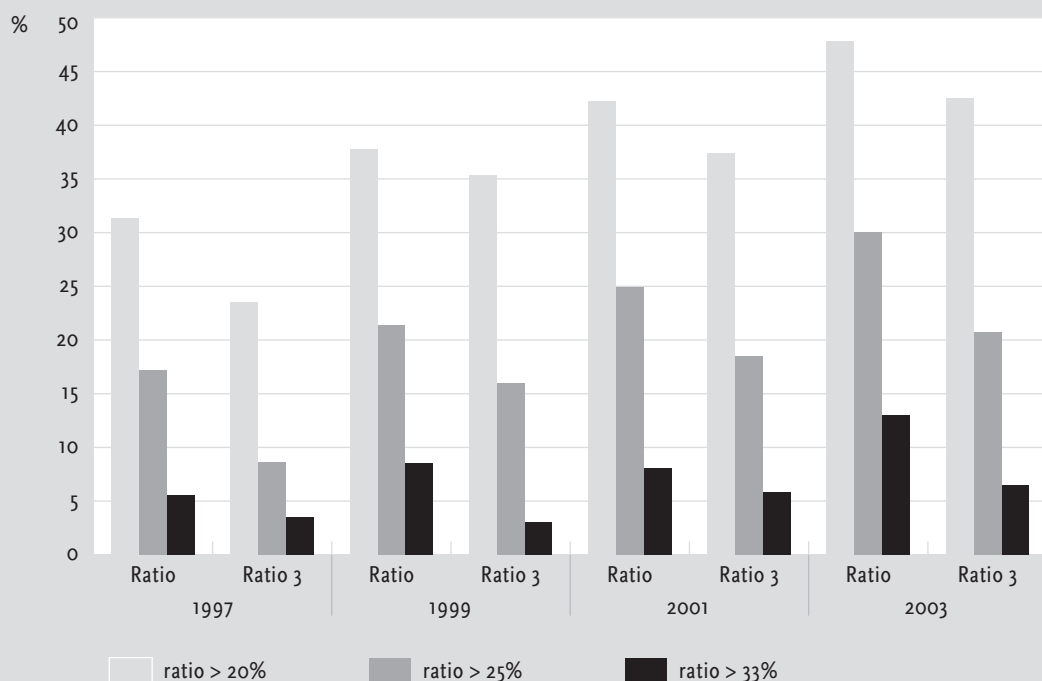
Source: FBS 1997-2003, own computation

3.6.5.6 The affordability of owner-occupied housing in the 'unprivileged' housing sector (2002)

The affordability of owner-occupied housing is often monitored using special indicator comparing the house prices and household incomes, rather than using the housing expenditures-to-income ratio. A standard indicator commonly used is the price-to-income ratio (P/I) – the ratio of the average (median) price of existing housing to the average (median) total annual net income of a household. This indicator shows how many annual net incomes the average (median-income) household would have to spend in order to be able to acquire an average (median-price) flat.

The household incomes reported in FBS surveys were compared to the average transaction prices of flats, as recorded by the Czech Statistical Office (since 1998, the year that the Czech Statistical Office began to systematically monitor house prices). Figure 3.17 shows a relatively sharp increase in P/I indicator between 1998 and 2003 and its subsequent decline in 2004. Thus, with the exception of 2004, during the monitored period flat prices rose faster than household incomes. Given that the primary aim of this paper is to analyse the affordability of housing, the P/I indicator should be weighted by popula-

Figure 3.16 Percentage of households in the Czech Republic with aggregate housing expenditures-to-income ratios above 20%, 25% and 33%, 1997-2003



Note: ratio – unadjusted aggregate housing expenditures-to-income ratio, ratio 3 – adjusted aggregate housing expenditures-to-income ratio (taking into account the effects of secondary housing, the housing allowance, and housing over-consumption).

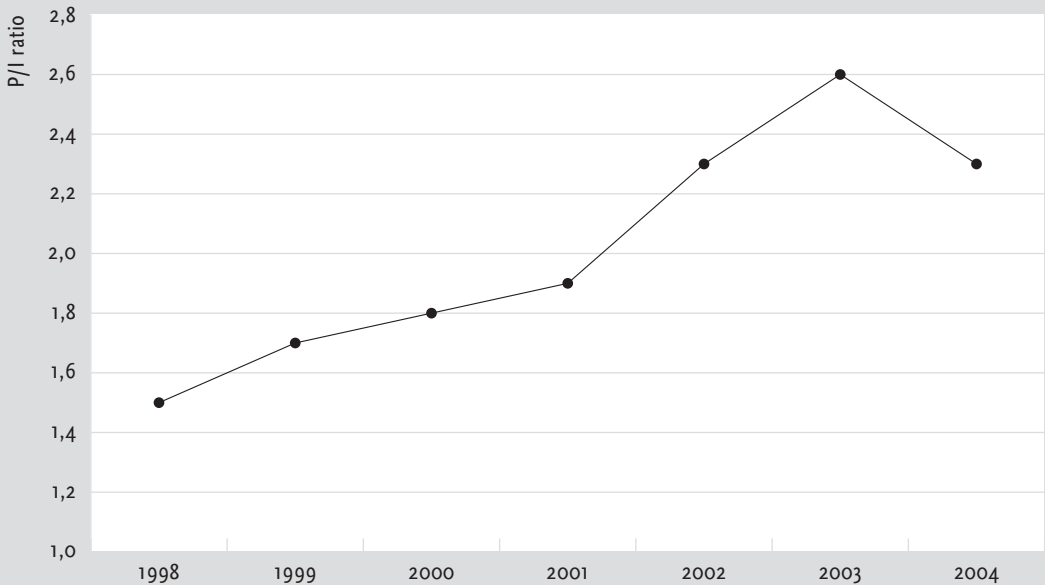
The FBS 1997 data set is weighted according to the Microcensus 1996; the FBS data sets for 1999, 2001 and 2003 are weighted with coefficients recommended by the Czech Statistical Office.

Source: FBS 1997-2003, own computation

tion size, as there is a difference if the indicator value is high in a region with a population of one million and the indicator value is low in another region with a population of only 300,000 inhabitants (number of transactions reflects this differentiation only partially). The values of the indicator were weighted by the population size in individual Czech regions and then within these regions by municipality size. Figure 3.18 shows the development of the weighted P/I for the period between 1998 and 2003. It is evident that the value of the indicator in 2003 is in reality higher after weighting than what has been indicated in Figure 3.17.

Between 1998 and 2003 alone (i.e., within the space of six years) the average value of P/I increased from 1.6 to 2.8 (the weighted indicator), or in other words, it almost doubled! While a slight decline in house prices that ensued (after the Czech Republic became a member of the EU, which resulted in a partial burst of the price bubble) helped to increase the affordability of owner-occupied housing, it was by no means enough to offset the effect of the pre-

Figure 3.17 The development of P/I in the Czech Republic, 1998-2004



Source: Czech Statistical Office, own computation

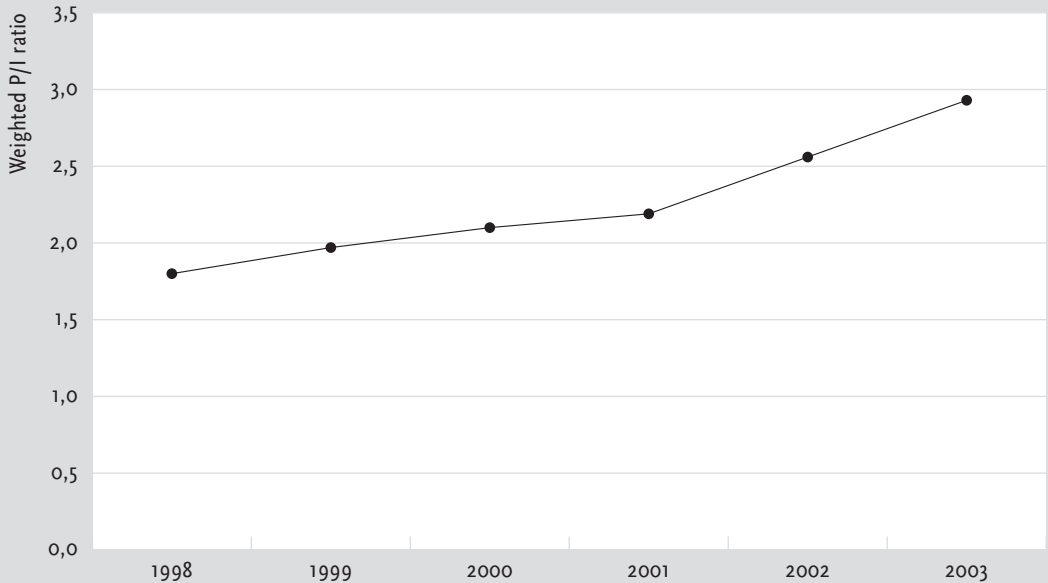
ceding increase. It may be assumed that at the start of the 1990s the value of P/I was significantly lower than in 1998, so the affordability of 'unprivileged' owner-occupied housing worsened over the course of the transformation.

An alternative way in which to monitor the affordability of owner-occupied housing and better compare it with the affordability of housing in the 'privileged' segment of the housing market (and with the affordability of housing in the rental sector) is to use the housing expenditures-to-income ratio; in this case aggregate housing expenditures, including also repayments of mortgage credits used to purchase housing. As in the case of the ratio used in the rental sector, here the housing expenditures-to-income ratio is defined as the average share of the sum of monthly annuity payments on standard mortgage credit obtained for the purchase of existing housing (though at real market prices in 2002) and all other monthly expenditures connected with housing out of the total net monthly income of the household.

Since the necessary statistics do not exist, I used again a simulated model situation, in which all current flat owners under the age of 40 (or in which the head of the household is under the age of 40) listed in FBS 2002 are paying mortgage instalments on the flat they are living in at an amount that corresponds to the price of their flat in 2002. As in the case of 'unprivileged' rental housing we do not know who bought the flat when, so the model situation does not correspond to reality. However, it does show how high the total housing expenditures-to-income ratio would be for young Czech flat-owners if they lived in the 'unprivileged' segment of the market, that is, in flats acquired at market prices in 2002.

The market price of owner-occupied flats surveyed by FBS 2002 has al-

Figure 3.18 The development of weighted P/I in the Czech Republic, 1998-2003



Source: Czech Statistical Office, own computation

ready been estimated using the hedonic price model described above. In 2002 households were able to use housing savings loan and mortgage credit to finance their housing needs, and this was a standard combination of financing in that year. At the same time the maximum LTV for mortgage loans was limited by law to 70%. Therefore, to calculate the housing expenditures-to-income ratio I assumed that households did apply for mortgage credit to cover 70% of the purchasing price of an older, existing flat, with a maturity term of 20 years, and that they obtained the remaining amount (to cover the remaining 30% of the flat's purchase price) from a housing savings scheme. The household saved half of this sum, and it obtained the other half in the form of credit from a housing savings bank at an annual interest rate of 6%. The annual interest rate²⁹ on the mortgage loan was 5.73%.

The calculation of housing expenditures-to-income ratio for 2002 took into account tax relief, namely, a reduction of the income tax base by the amount of interest paid on both types of loan up to a maximum of CZK 300,000 annually. The amount of this tax saving was determined from the difference between disposable income calculated from the tax base minus the sum of interest and disposable income calculated from the tax base without any reductions. Given that the FBS only consistently distinguishes the incomes of the head of the household and the head's spouse, the tax saving was calculated separately for the income of the household head and spouse, and the

²⁹ This interest rate corresponds to the weighted average interest rate on mortgage credit granted to physical persons in January 2003, according to data from Fincentrum Hypoindex.

higher of the two incomes was included in the analysis (in other words, it was logically assumed that the interest deduction would be used by the one whose income would result in a higher tax saving).

The average unadjusted aggregate housing expenditures-to-income ratio in 2002 for households belonging to this housing market segment was 31.1%; after taking into account secondary housing expenditures it was 31.1% (thus, unchanged); it dropped to 30.6% after taking into account the reduction of expenditures by the housing allowance; and after taking into account housing over-consumption it was finally 29.7% (N = 147). In 2002 the unadjusted housing expenditures-to-income ratio of 60.8% of the households in this housing segment exceeded the affordability limit (25%) and the adjusted housing expenditures-to income ratio of 57.2% of households exceeded the affordability limit.

3.6.5.7 Comparison and conclusions

The standard way of measuring housing affordability is with the aid of the indicator approach, that is using the housing expenditures-to-income ratio. This indicator alone is incapable of taking into account housing quality (especially the degree of housing consumption), and therefore it is usually adjusted in the literature. In my opinion, measuring the housing expenditures-to-income ratio in the Czech environment requires additional adjustments to account for deficiencies in data collection and adjustments to account for the fact that this country, like other post-socialist countries, is experiencing a period of transformation. For these reasons I monitored the development of housing affordability separately for the owner-occupied and rental sectors, and also separately for housing in the 'privileged' and the 'unprivileged' segments of the housing market. The results can only be employed while bearing in mind the fact that some cases are based only on modelled situations.

As Table 3.10 shows, the housing expenditures-to-income ratio differs substantially between individual market segments. Although households living in owner-occupied flats in the 'privileged' segment of the market show on average the same housing expenditures-to-income ratio as households living in rental flats in the 'privileged' market segment, the housing expenditures-to-income ratio of households headed by a person under 40 who purchased a flat in 2002 would be roughly 10 percentage points higher than that of housing owners in the 'privileged' market segment, and if instead of buying a flat these households were to opt for market rental housing their average housing expenditures-to-income ratio would be roughly 8 percentage points higher than that of households in the 'privileged' segment of the rental market. According to the adjusted housing expenditures-to-income ratio, 44% of tenant households in the 'unprivileged' segment of the market (as opposed to 17% of tenant households in the 'privileged' segment of the market), and 57% of

Table 3.10 Average housing expenditures-to-income ratio and percentage of households in the Czech Republic above the affordability limit in the individual segments of the market (2002, 2003)

Type and segment of housing	Average housing expenditures-to-income ratio			Percentage of households above the 25% affordability limit		
	unadjusted	adjusted	difference	unadjusted	adjusted	difference
Privileged rental (2003)	21.9	18.3	3.6	32	17	15
Unprivileged rental (2002)	27.9	25.6	2.3	50	44	6
Privileged owned (2003)	21.6	20.0	1.6	30	21	9
Unprivileged owned (2002)	31.1	29.7	1.4	61	57	4

households in owner-occupied flats in the ‘unprivileged’ segment of the market (as opposed to 20% in the ‘privileged’ segment of the market) would have a housing expenditures-to-income ratio that exceeds the affordability limit established in this analysis – that is, higher than 25%.

Table 3.10 shows how significant the effects of the adjustments to the housing expenditures-to-income ratio might be – among households in the ‘privileged’ rental segment of the market, the adjustments described above lead to a reduction of the average ratio by 3.6 percentage points and a reduction of the percentage of households whose housing expenditures-to-income ratio exceeds the affordability limit by 15 percentage points. The adjustments to the ratio are less significant in owner-occupied housing sector and are far less significant in both ‘unprivileged’ segments of the housing market (for housing expenditure-to-income ratio 1.6 and 1.4 percentage points, respectively).

4 Effectiveness and efficiency of housing policy in the Czech Republic

The purpose of this chapter is to assess selected state interventions in the field of housing consumption (housing subsidies) in the Czech Republic from the perspective of their effectiveness and subordinated efficiency. For that I use the theory and methodological device of *welfare economics* described in Chapter 1. This chapter should especially answer the second research question, which is as follows:

2. *How effective and efficient were state interventions in the field of housing consumption during the transition in the Czech Republic if the theoretical framework and methodological device of welfare economics is used for such assessment? How effective were such interventions from the point of view of both vertical and horizontal effectiveness? How efficient were such interventions if we narrow the wide concept of efficiency to the cost-benefit analysis of state interventions in the field of housing consumption (i.e., subordinate efficiency to effectiveness)? How efficient and effective were these interventions when assessed against the assumptions on efficiency and effectiveness of subsidies?*

Table 4.1 shows the structure of housing subsidies (state housing expenditures) between 1999 and 2005. The temporary items (e.g., subsidies to cover damages caused by floods in 1999 and 2002 or subsidies directed to one project) are not listed but are included in the total amounts. I distinguished subsidies directed at promoting the supply of rental housing (light grey), demand for rental housing (medium grey) and subsidies to promote homeownership (dark grey). The items of expenditure are also divided separately according to the executive authority responsible for their allocation – Ministry for Regional Development (MRD), State Fund for Housing Development (SFHD), Ministry of Finance (MF) and Ministry for Labour and Social Affairs (MLSA). The fiscal subsidies in the form of tax relief on mortgage interests and tax exemption on interests on housing savings are also estimated (no official figures are provided by either MF or MRD). The estimate of public costs of tax relief is calculated as a multiple of outstanding mortgage balance (loans for households and for residential purposes), average interest rate on mortgage loans and average income tax rate for each particular year. The estimate of tax loss following from exemption of interests on housing savings is calculated as a multiple of the total savings on savings accounts held by all housing savings banks, average interest on savings and capital income tax rate for each particular year.

As mentioned in the previous chapter, the responsibility for housing policy formation and implementation is divided among three Ministries in the Czech Republic (with SFHD being just the executive body to fulfil programmes prepared mainly by MRD). Housing allowances remain within the responsibility of MLSA as a part of general social policy and the most important programmes supporting owner-occupied housing (state premium to housing sav-

Table 4.1 State housing expenditures in the Czech Republic, 1999-2005 (in thousands CZK)

	1999	2000	2001
Repairs of pre-fab buildings	420,000	533,000	218,500
Pre-fab housing estate refurbishment	0	0	150,000
Support for municipal 'rental' housing construction	3,381,000	2,884,000	2,011,000
Support for social-care municipal housing construction	471,000	578,000	575,700
Support for 'supported' municipal housing	0	0	0
Interest subsidy on mortgage loans	201,000	307,000	432,500
MRD total	6,450,000	4,958,000	3,388,000
Pre-fab housing reconstruction - PANEL	0	0	0
Loans to municipalities for housing reconstruction works	0	0	0
Support for municipal 'rental' housing construction	0	0	1,039,900
Support for social-care municipal housing construction	0	0	377,700
Support for targeted municipal rental housing construction	0	0	0
Support for municipal rental housing construction as part of investment incentives	0	0	0
Qualified mortgage loans for first-time buyers	0	0	0
SFHD total	0	0	1,556,000
Housing savings scheme premiums	6,393,000	7,719,000	9,313,000
Subsidies to banks to cover losses from 'old' loans (pre-1989)	1,411,000	1,414,000	1,630,000
Tax relief (estimate)	335,000	465,000	742,000
Tax exemption on interests from housing savings (estimate)	351,000	414,000	500,000
MF total	8,490,000	10,012,000	12,185,000
Housing allowance	2,084,000	2,518,000	2,698,000
Temporary allowance on energy	236,000	106,000	0
Temporary allowance on rent	127,000	73,000	6,000
MLSA total	2,447,000	2,697,000	2,704,000
TOTAL ALL	17,387,000	17,667,000	19,833,000
GDP at current prices	2,080,797,000	2,189,169,000	2,352,214,000
Share in GDP (in %)	0.84	0.81	0.84
State expenditures	596,909,000	632,268,251	693,920,300
Share in state expenditures (in %)	2.91	2.79	2.86

Sources: Ministry for Regional Development (MRD), Ministry of Finance (MF), Ministry for Labour and Social Affairs (MLSA), Family Budget Surveys and own computations

2002	2003	2004	2005
283,485	286,599	230,185	303,217
79,795	0	110,956	164,527
542,198	795,181	816,804	496,718
584,173	46,000	0	0
0	0	198,067	476,687
517,765	539,291	542,263	414,210
3,540,000	3,276,000	1,898,000	2,059,000
13,500	57,500	103,600	127,380
90,300	323,000	232,900	126,940
1,870,400	2,001,600	1,648,100	356,340
1,280,100	1,448,500	811,800	158,030
0	17,600	540,800	938,060
0	0	57,700	152,020
63,600	145,800	42,500	1,781,480
3,321,000	4,178,000	3,761,000	3,791,000
11,059,000	13,261,000	15,337,000	16,086,000
1,143,000	737,000	630,000	610,000
2,011,000	2,253,000	2,836,000	3,114,000
675,000	710,000	861,000	987,000
14,888,000	16,961,000	19,664,000	20,797,000
3,028,000	2,835,000	2,572,000	2,500,000
0	0	0	0
0	0	0	0
3,028,000	2,835,000	2,572,000	2,500,000
24,777,000	27,250,000	27,895,000	29,147,000
2,464,432,000	2,577,110,000	2,781,060,000	2,970,261,000
1.01	1.06	1.00	0.98
750,682,697	808,718,393	862,718,393	922,798,018
3.30	3.37	3.23	3.16

ings, tax relief) remain within the responsibility of MF. Though, officially, MRD is responsible for state housing policy (preparation of long-term strategies), its competence is substantially fragmented by the interests of representatives of other two Ministries. Table 4.1 also makes clear that the exclusive responsibility for housing policy taken by MRD is not accompanied by the appropriate power in the allocation of financial resources – 71% of total state housing expenditures were allocated by MF and only 20% of total expenditures were allocated by MRD or SFHD in 2005. This inconsistency between formal responsibilities and factual powers of individual ministries is a very important factor explaining the formation of housing policy in the Czech Republic.

As is also made clear in Table 4.1, public expenditure in support of owner-occupied housing dominates recent Czech housing policy. In 2005, the supply-side subsidies for construction of new municipal, supported or social-care housing amounted to CZK 2.5 bn and the demand-side subsidies for housing allowances amounted also to CZK 2.5 bn. However, support for acquisition or reconstruction of own (coop) housing in the form of qualified loans for first-time buyers, interest subsidies, state premiums to housing savings, tax relief and tax interest exemption, amounted at the same time to a total of CZK 23 bn; that is, it was almost five times more than public expenditures supporting rental housing. Moreover, part of the finished municipal rental housing was constructed on terms allowing easy transformation into cooperative form (thus some subsidies served, *de facto*, as support for homeownership) and part of the housing allowance was allocated among homeowners. The scale of total public support for homeownership strongly contrasts with the fact that the Czech Republic was one of the few transition countries (as we saw in the previous chapter) that did not follow the path of mass public housing privatisation and preserved substantial rental housing stock.

It is necessary to point out that Table 4.1 does not include important, yet difficult to measure, economic subsidies. I mentioned in Chapter 2 that one similarity in housing policy reforms among the selected transition countries was that a substantial part of the allocated subsidies was hidden in the form of economic subsidies. Basically, there were two main economic subsidies: one for tenants who enjoyed low regulated rents and the other for homeowners who purchased their housing for prices well under their market levels. These subsidies are not included in the table, simply because they, albeit large, are not fully comparable with other types of listed subsidies and their size is very difficult to estimate.

However, negligence of the economic subsidy for tenants leads, for example, to a biased value of housing allowance subsidy which is low now (due to rent regulation) but which would be far greater if rents were increased to market levels; another example may be the impact on the public cost of public housing maintenance (not done properly nowadays) and/or public costs deriving from failed international arbitrage due to the fact that rent regula-

tion may breach the basic human rights of private landlords. Therefore, an attempt has been made to estimate the amount of this subsidy, employing the relatively complex simulation model fully described in Lux, Sunega (2004) and partially in the next section of this book as well. The model simulates tenure choice among households living in rent-regulated housing (using Family Budget Survey data) when controlled rents are gradually increased. It also simulates the situation on the housing market when the supply of vacant market rental housing rises as a consequence of the migration of better-off households to homeownership, thereby estimating equilibrium market rents (which were substantially lower than existing market rents distorted by regulation itself). The economic subsidy is computed as the difference between equilibrium market rents and current regulated rents. The subsidy totalled about CZK 10 bn in 2002 and due to a decreasing share of rent-regulated housing in total housing stock decreased to about CZK 7-8 bn in 2005.

Estimating the size of the second economic subsidy derived from public housing privatisation is more difficult. As mentioned above, more than half of the total public housing stock was sold between 1990 and 2004; mostly for low 'residual' prices to tenants. Due to the highly variable conditions applied to municipal housing privatisation between different points of time as well as at each point of time among different municipalities, it is simply impossible to calculate this economic subsidy exactly. There are no central statistics that could be used for the purpose. Based on partial information on privatisation prices collected for Prague and some other cities by the Institute for Urban Development, the annual level of it would be close to or more than the annual economic subsidy stemming from rent regulation (i.e., equal or higher than CZK 10 bn).

In sum, hidden economic subsidies would be the most important annual housing subsidies; it is also worth of mentioning that economic subsidy from rent-regulation is not fully paid by the public authorities – part of it is covered by private landlords, and this is now subject to judicial proceedings.

4.1 Effectiveness

In the following sections I will try to evaluate the effectiveness of selected housing subsidies in the Czech Republic. The effectiveness will be measured by comparing household income distribution with the distribution (real or estimated) of selected housing subsidies (state interventions in the field of housing consumption), mostly in the year of 2002. In so doing I will test the assumptions of vertical and horizontal effectiveness elaborated upon in the first chapter of this book:

Main assumption 1: Effective subsidies assist lower-income (needy) households more than higher-income (less needy) households. (Vertical effectiveness)

Main assumption 2: Effective subsidies do not exclude any lower-income (needy) households. (Horizontal effectiveness)

Sub assumption 1: The absolute amount of subsidy should be significantly higher in the group of lower-income (needy) households than in the group of higher-income households (less needy).

Sub assumption 2: The subsidy should contribute to a reduction in the level of inequality in the society.

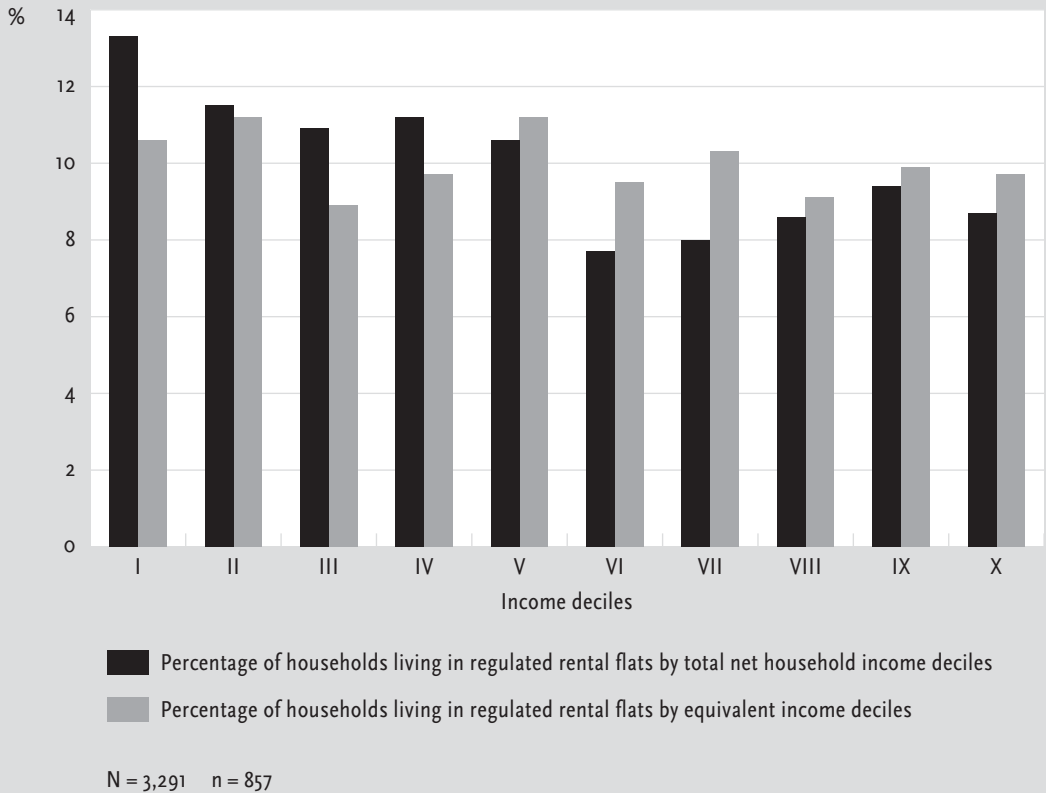
To test the above assumptions I will use statistical data from the Family Budget Survey of 2002. This survey includes necessary information on household incomes and household housing expenditures and the year of the survey was chosen precisely because for that year (using the same data set) I also made an econometric estimate of equilibrium market rents allowing for assessment of economic subsidy stemming from rent regulation. If the data permits, I will compute all the necessary indicators of income inequality and subsidy distribution, as stated in the first chapter (standard deviation, variance of the log-income and others).

In one case the assessment of subsidy distribution draws on a different data set (information from the Ministry of Finance) and in one case it also draws on data from the national *Housing Attitude Survey 2001* conducted by the Institute of Sociology in 2001 on a sample of 3,357 respondents. This is because for many housing subsidies there is no registered information about eligible households whatsoever; nor could I find the distribution of these subsidies in the *Family Budget Survey* data. Partial information about distribution is however contained in MF statistics or this sociological survey.

In two cases (supply-side subsidies in the field of rental housing and economic subsidy stemming from privatisation of public housing) I could not use the attitude survey and so these results are estimated using other information sources. This 'flexibility' in methodology on subsidy effectiveness measurement is a prerequisite for presenting any kind of generalised conclusions here since data on the monitoring of allocation of housing subsidies is unavailable (not provided by any audit, ministerial or other central organisations) and additional statistical sources are also rare.

The sections below present the conclusions of the assessment of effectiveness of the following subsidies: economic subsidies (one stemming from rent regulation and the second from public housing privatisation), housing allowance, supply-side subsidies in the field of rental housing, tax subsidy and state premium to housing savings scheme.

Figure 4.1 The percentage of households in the Czech Republic 'profiting' from regulated rent, 2002



Source: FBS 2002

4.1.1 Economic subsidy from rent regulation

From the perspective of effectiveness, rent regulation could be justified, as with other housing policy instruments, by the redistribution of resources in favour of lower-income households. If that were the case then primarily lower-income households should be living in rent-regulated flats and this group of households ought to be the recipients of most of the resources contained in this economic subsidy. Figure 4.1 shows the percentage of households living in the regulated rent housing sector in the total number of households in individual categories according to total household income or equivalent household income.

As Figure 4.1 makes clear, rent regulation was almost equally applied to both 'rich' and 'poor' households. As many as 10% of the wealthiest Czech households (according to equivalent income ranking in the 10th decile of the income distribution) lived in a flat with regulated rent and this percentage was not significantly lower than among the poorest households (according to the equivalent income in the 1st decile of the income distribution: 10.6%). The hypothesis was tested as to whether households living in flats with regulated rent are roughly equally represented across individual income deciles. This hypothesis cannot be rejected as the results of the chi-square test indicate a

95% level of significance.

Another possible method of evaluating the equity effect of rent regulation is by drawing the distribution of the economic subsidy stemming from rent regulation. The level of economic subsidy should be calculated as the difference between the equilibrium market rent that would probably emerge after rent deregulation and the actual regulated rent. Equilibrium market rents in the Czech environment can be estimated, for example, using methods that were proposed by Lux *et al.* (2004) and Lux & Sunega (2004). They are briefly described below.

In terms of pure economic theory, as long as certain conditions are met (perfectly competitive market, perfect dissemination of information among market actors, zero transaction costs, etc.), the price of real estate should be determined as the sum of expected discounted revenue from investment into a property, that is, the sum of expected discounted revenue from rent (plus potential capital gains from the sale of the property at the time of sale):

$$P_A = \frac{R_1}{(1+i)} + \frac{R_2}{(1+i)^2} + \frac{R_3}{(1+i)^3} + \frac{R_4}{(1+i)^4} + \dots + \frac{R_n}{(1+i)^n} + \frac{P_p - P_k}{(1+i)^n}, \text{ where:}$$

P_A - the current equilibrium price of the property;

$R_1 \dots R_n$ - rent in year 1 to rent in year n ;

i - interest rate (the interest rate from alternative assets, or mortgage credit);

P_p - selling price of the real estate in year n ;

P_k - purchasing price of the real estate;

n - the duration of possession of the real estate.

Given that real estate investments are generally long term in character, the price of a property should be determined as a quotient of the rent and the discount rate (usually at the level of rates on mortgage credit, or alternative assets). In other words, for a sufficiently large n (e.g., $n = 30$) and roughly equal R , if we abstract from the capital gains at the time of sale, then:

$$P_A = \frac{R}{i} \text{ and therefore: } R = P_A * i$$

If we know the current market price of a property, and that price is the equilibrium price, then the level of rent could be calculated as the product of the market price of the property and the discount rate. However, when applied to housing, this principle for calculating the equilibrium level of rent, based on the principle of dividend discount models (models used to determine the 'correct' market value of shares; that value is compared to the current market value, which makes it possible to determine whether a given market share is undervalued or overvalued), has numerous weaknesses, for which it is criticised. One reason is that as an economic good, housing has a number of

specific features that distinguish it from other assets. Therefore this method of determining equilibrium rent may be somewhat misleading, especially in Czech circumstances, where housing prices were distorted to some extent owing to the continued existence of the first-generation rent regulation and other aspects of economic transition.

In order to determine the equilibrium market rent level, a relatively complex simulation model of 'shock' rent deregulation was developed instead using data from the *Family Budget Survey 2002* (FBS, 2002). The model was designed to determine at what level of rent a sufficient number of rental flats are vacated so as to satisfy the demand of needy households (households living in overcrowding conditions or households living in temporal tenures).

The rational part of the theory of tenure choice is based on the decision whether it is more of an advantage to rent or buy housing. For this purpose the household compares the net cost of rent (i.e., rent after deducting any housing allowance the household may be receiving) and the user costs of owner-occupied housing. The standard way of calculating user costs (UC), adjusted here for the specific terms of mortgage financing in the Czech Republic with a maximum loan-to-value of 70% in that time, is as follows:

$$UC_0 = [(1-t) * i + \delta + \alpha - g] * 0,7P^e + [i_0 + \delta + \alpha - g] * 0,3P^e,$$

where t is the marginal tax rate for the household member with the highest income, i is the nominal interest rate on mortgage credit, δ is the rate of depreciation, α is the real estate tax rate, g is the expected nominal price appreciation rate of the given real estate in the future, and i_0 the opportunity costs from the use of personal savings to cover 30% of the cost of the real estate. In other words, annual user costs include the sum of annual interests paid on mortgage credit (and lost revenue from the potential use of personal savings in other investments, e.g., the purchase of government bonds), but reduced by the option of deducting interest paid on mortgage credit from income tax base. Alongside the adjusted sum of paid interests, user costs also include depreciation and real estate tax. The expected price appreciation of the property is then deducted from this sum, as unlike rental housing the purchase of owner-occupied housing is also an investment, often the biggest investment in the life of a household.

For the purpose of simulations, we set i at the level of average interest rate on mortgage credits granted on housing purchase in 2002 (6.7%), i_0 at the level of the average yield on long-term government bonds in 2002 (4.5%), δ at the level of 1%, t according to particular income tax rates valid in 2002, and α was excluded from the equation owing to its marginal significance. The expected price appreciation of real estate g was estimated separately for eight individual geographic zones. The average annual expected appreciation for a 20-year outlook (determined in an effort to eliminate the effects of short-term price

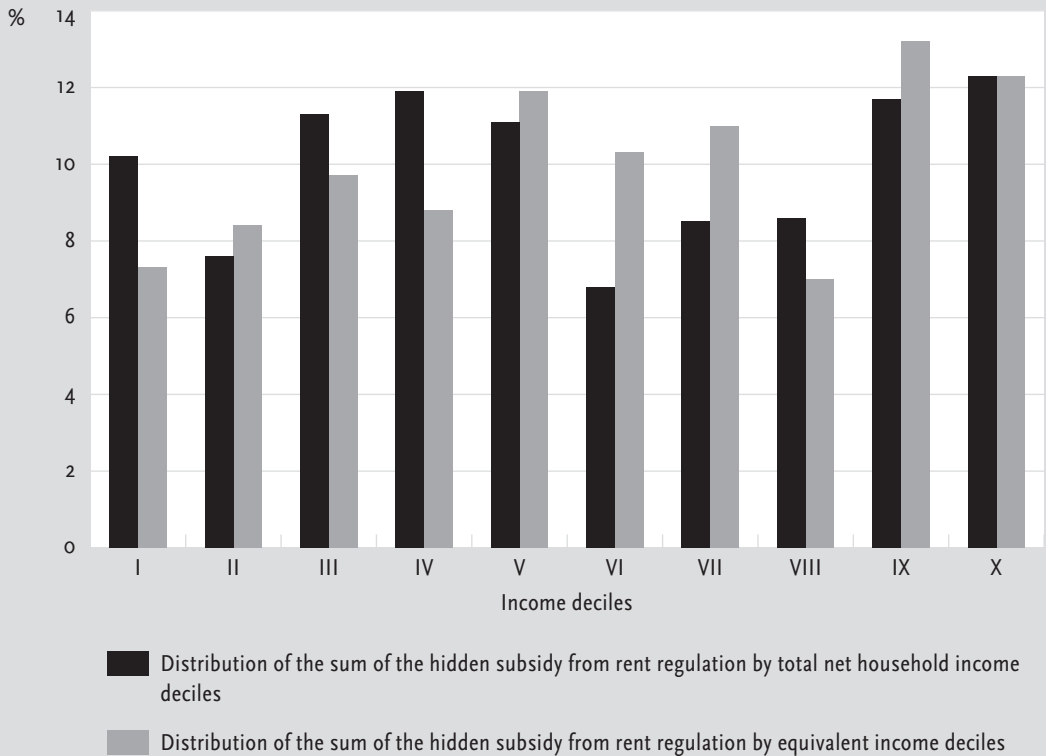
fluctuations) were then around 1.5% in Prague and zero in the eights zone.

The price of housing P^e in 2002 was estimated by means of testing hedonic price models (OLS) using data from MF and the Czech Statistical Office (CSO) on the transaction prices of housing in 2002 (the same model as applied for housing affordability analysis in the previous chapter). For every household surveyed in FBS 2002 living in the rent-regulated housing sector, the house price and subsequent user costs were determined for the case were they to acquire owner-occupied housing corresponding in size and location to the rental flat they occupy at present. We assumed that if a household satisfies certain age and income criteria while the potential user costs of owner-occupied housing are lower than the new (simulated) level of regulated rent, then that household will exit the rental sector and enter the owner-occupied housing sector. We also assumed that as soon as the number of vacated flats in the rent-regulated housing sector equal the total number of 'needy' households, then the rent deregulation process will stop and a demand-determined equilibrium rent will emerge. The number of needy households in individual regions of the Czech Republic was estimated using data from the survey *Social Conditions of Households 2001* (SSD, 2001) carried out by the Czech Statistical Office in 2001.

From the perspective of the whole rental housing market, another important question is how landlord behaviour might reflect the level of demand-determined equilibrium rent, established by means of the method described above; in other words, would demand-determined equilibrium rent provide investors with at least the minimal amount of returns on invested capital required for them to be willing to lease their flats? We studied income and capital returns on residential real estate investments in advanced countries (using, e.g., the Investment Property Databank) and their relations to the rate of return on government bonds; after that we established the minimum net income return on real estate investments in the Czech Republic in 2002 at a level of 3.75% of flat market price. If the real return rate is lower, it can be assumed that private landlords would probably begin increasingly to sell their properties. Therefore the whole market equilibrium rent was set at a level of demand-determined equilibrium rent in places where this was higher than minimum income return on investments in residential real estates, while it was set at a level of minimum income return on investments in residential real estates in places where the demand-determined equilibrium rent was lower than such a minimum income return.

Figure 4.2 shows how in 2002 the total economic subsidy derived from rent regulation (defined as the difference between equilibrium rent and actual regulated rent) was distributed by total net household income and equivalent income, using data from the FBS 2002. Clearly in 2002, higher-income households and middle-income households were the main recipients of economic subsidy in the form of regulated rent, while the lowest-income households benefited from this subsidy relatively the least. The main reason is that high-

Figure 4.2 Distribution of the sum of economic subsidy among tenants in the Czech Republic living in regulated rental housing, 2002



Source: FBS 2002; own computation

er-income households lived in larger flats than lower income households where the difference between market and regulated rents was also higher.

With regard to distribution of the economic subsidy from rent regulation, whether the average subsidy amount differs significantly between individual income deciles of households was tested by statistical tests. The LSD test shows that the average level of subsidy for households in the last two equivalent income deciles was statistically significantly higher than the average level of subsidy to the lowest-income households in the first two equivalent income deciles. The criterion selected to indicate an instrument's high effectiveness was the kind of redistribution where 90% of the total sum of the subsidy goes to 50% of the households with the lowest incomes and at the same time 75% of the total sum of the subsidy goes to 30% of the households with the lowest incomes. The economic subsidy following from rent regulation failed to satisfy this criterion. Only around 46% of the total amount of the subsidy was received by 50% of the households with the lowest equivalent incomes, and 30% of the households with the lowest equivalent incomes received only 25% of the economic subsidy.

Table 4.2 summarises the values of different indicators of income inequality; the values were calculated using equivalent income, firstly without the

Table 4.2 Indicators of the level of inequality of income distribution in the Czech Republic, before and after the economic subsidy from rent regulation

Indicator	Without subsidy	With subsidy
Standard deviation (V)	4,786.4	5,102.5
Variation coefficient (C)	0.482	0.456
Variance of log-income (H)	-0.054	-0.055
Mean income ratio (W)	4.18	4.19

Source: own computation, FBS 2002

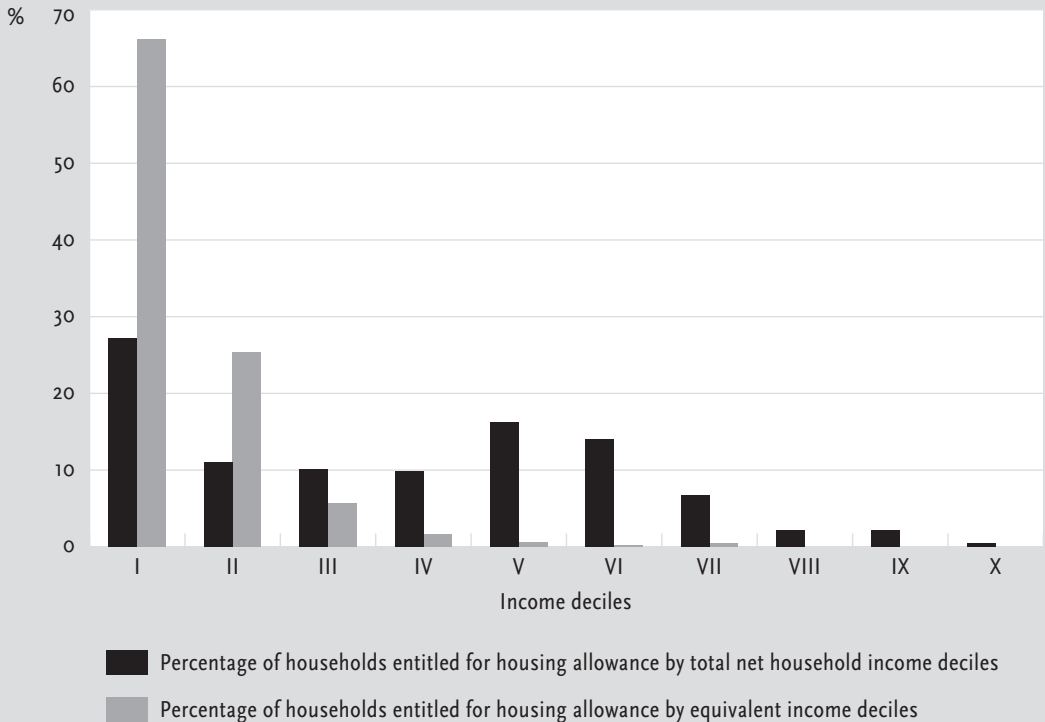
subsidy and then with the economic subsidy (i.e., the household income was increased by the amount of the subsidy).

The data in the table show that while standard deviation, variance of the log-income and mean income ratio of 5% of the highest-income and 5% of the lowest-income households indicate that income inequality increased in society when the economic subsidy to households paying regulated rent is taken into account, only the variation coefficient indicates the opposite trend. The reason why the variation coefficient shows the opposite trend in comparison to other indicators is probably the fact that to a large extent middle-income households profited from the subsidy; because the variation coefficient is not sensitive to the level at which redistribution takes place, the value of the coefficient indicates lower inequality in income distribution after the subsidy. However, the most informative indicator is probably the variance of the log-income, which gives greater weight to the lower-income groups.

In all systems of rent regulation (social housing) some low-income households may actually be excluded from the right to get rent regulated housing (immigrants, non-residents etc.). However, the system applied in the Czech Republic was, from the point of view of horizontal effectiveness, even more discriminating. Rent regulation and strong tenant protection had the character of a safety net for existing tenants while new households had, due to the low tenant turnover and end of the mass state rental housing construction, few chances to get involved. Though it is hardly measurable explicitly, a substantial part of needy new households (young couples and families, singles after divorce) were, in fact, completely excluded from the eligibility for this type of subsidy.

4.1.2 Economic subsidy from public housing privatisation

Due to the fact that price conditions on public housing privatisation vary both in time and space it is difficult to estimate (or simulate) distribution of the amount of economic subsidy stemming from public housing privatisation. Although we know what rent tenants paid, we do not know what price homeowners paid for their owner-occupied housing. Therefore we cannot measure the effectiveness of this subsidy in the same way as the previous economic subsidy.

Figure 4.3 Percentage of households in the Czech Republic entitled to housing allowance, 2002

N = 3,292

Source: FBS 2002

As the social structure of tenants living in rent-regulated housing (measured by household income distribution) changes slightly towards lower income households in time this is a very weak sign that distribution of economic subsidy from public housing privatisation is skewed more towards higher income households than rent regulation. Some really poor households or households of pensioners with relatively low income decided not to take part in the privatisation and stayed on as protected tenants. The target population is generally similar to the target population of the first economic subsidy though, naturally, tenants in restituted (though rent-controlled) housing are excluded. Both factors taken together may lead to the somewhat vague conclusion that the effectiveness of economic subsidies following from public housing privatisation might be even lower than the effectiveness of rent regulation demonstrated above. There is however no other way than this reasoning to confirm this supposition.

4.1.3 Housing allowance

Based on simulations using data from FBS 2002 Figure 4.3 shows how the sum of potentially paid housing allowances (in the form valid till the end of 2006) would be distributed among households according to their total net income

Table 4.3 Indicators of the level of inequality of income distribution in the Czech Republic, before and after the housing allowance

Indicator	Without the housing allowance	With the housing allowance
Standard deviation (V)	4,465.5	4,439.9
Variation coefficient (C)	0.448	0.445
Dispersion of the income logarithm (H)	-0.054	-0.052
Mean income ratio (W)	4.02	3.82

Source: own computation, FBS 2002

and equivalent income, if all eligible households had asked for the allowance. Figure 4.3 shows that the housing allowance was genuinely designed to help lower-income households in particular.

Table 4.3 presents the values of the indicators of inequality of income distribution before and after the housing allowance is taken into account; the values of the indicators refer to equivalent income. The data in the table show that the housing allowance contributed unequivocally to reducing income inequality in society, and from this perspective it can be regarded as effective. The housing allowance satisfied the normative criterion of effectiveness: 50% of the lowest-income households (by equivalent income) would be the recipients of 99% of the total sum that would be paid in housing allowances (under the conditions indicated above), and 30% of the lowest-income households would receive approximately 97% of the total sum paid in the form of housing allowances.

However, the allowance's major flaw was the fact that the equation did not take into account real housing expenditure but only the tariff component of the subsistence minimum, which reflected the assumed (notional) housing costs of a household living in rent-regulated housing. In this way it breached the imperative of horizontal effectiveness. Households living in market rental housing, paying several times higher market rents, were thus excluded from any truly effective help from the state. They often had an income higher than the ceiling because they would not have been able to live there otherwise - the potential housing allowance computed from tariffs applied in the 'privileged' rental sector would have been, even in the case of low income, insignificant and would not have allowed them to stay in the flat. This serious shortcoming leads to the conclusion that even housing allowance, a means-tested targeted benefit, failed to fully meet the effectiveness criteria.

4.1.4 'Social' housing subsidies

Social rented housing is not defined in the Czech Republic on the central level and is only occasionally defined on the local level (municipalities). There is no legislative framework for non-profit housing associations. Though rent control has been applied (and is still applied) to all running tenancies, it is not designed as a part of social policy (targeting those in housing need). Only a few municipal flats became vacant annually (tenant protection allows the

transfer of a flat with regulated rent to other households and this creates the grounds for massive black market practices). Such vacant municipal flats are partially rented out again at market rents (highest bid) and partially as regulated rents to those in housing need. Only the last segment (allocation of vacant municipal flats with regulated rents to those in need) may seriously be considered social rented housing. It is, however, impossible to estimate the number of such flats.

The central administration refuses to label any part of housing stock as social rented housing but, in some cases, the term refers only to the following housing stock:

- *Supported housing* – new municipal rental housing constructed under the programme introduced in 2003 by the Ministry for Regional Development. The grants are provided to municipalities for the purpose of construction (exceptionally reconstruction) of municipal rental flats. These flats may be allocated only among people who face housing accessibility problems due to their special needs (resulting from their health, age, unpleasant life circumstances) and who are endangered by social exclusion. This housing includes: *protected housing* (for the handicapped and old people needing special flat design and social care), *half-way housing* (for people living in risky social environments who are unable to solve their social situation by themselves, such as young adults leaving children homes, people returning from prison, single parents, victims of domestic violence) and *start-up housing* (for people for whom housing is inaccessible, even after all existing means of housing and social policy are used). Altogether there were 2,568 supported flats till July 2006 (i.e., constructed between January 2003 and July 2006): 2,458 protected flats, 69 half-way flats and 41 start-up flats.
- *New municipal rental housing* – constructed under the programme introduced in 1995 by the Ministry for Regional Development. The scale of housing output was about 62,000 housing starts till the end of 2002. Due to the fact that there were no abiding cost or income ceilings (targeting) for dwelling allocation and mainly the fact that the programme was transformed in a way that allowed speculation and abuse (lost character of municipal rental housing), it was highly criticised and, finally, largely amended in 2003. In 2003 the cooperative form was forbidden, cost and income ceilings were introduced and the subsidy increased. Since 2003 the allocation of flats has become income targeted and, more importantly, flats cannot be transferred to the cooperative form and remain as municipal rental housing. They may be allocated only to singles with a monthly income lower than a 0.8 multiple of the average monthly wage in the Czech Republic and among households with more members and a monthly income lower than a 1.5 multiple of the average monthly wage. About 7,000 flats were built under this reformed programme between 2003 and July 2006.
- *Housing with social care* – new municipal housing constructed under the

programme introduced in 1995 and finished in 2002 by the Ministry for Regional Development for seniors and other people needing 24-hour social care. The small new apartments serve the elderly and handicapped people and social care support is provided there. About 7,500 flats with social care were built in the period 1995-2002. Since 2003 housing with social care is formally part of the protected housing programme (total size of protected housing constructed since 2003 is estimated above).

- 'Holobyt' (*shelter*) – municipal housing of a very basic standard (one room, common bath and kitchen facilities) in abandoned buildings (former industrial buildings, barracks, empty lodging houses) or in new, very basic building at the edges of cities, occupied exclusively by people and households evicted for long-term rent arrears. Many occupants are Roma households. About one third of all municipalities dispose of some 'holobyt'; however an estimate of the total number of flats is impossible to make.

Altogether, taking a very broad definition of social housing that includes all existing rent-regulated municipal housing (constructed before 1989) and all new municipal housing constructed during the transition (even some 'quasi-rental' flats), the total would have reached 610,000 municipal dwellings in 2001 (17% of housing stock). However, taking a more serious definition of social housing as rental housing with rents below market rates and allocated administratively according to the income and social situation of the applicant, then it would include only existing municipal housing that was vacated and rented out again during the transition for regulated rents to those in need (by a very rough estimate about 6,000 flats), only the new municipal housing that was constructed since 2003 when the programme of the Ministry for Regional Development stopped being abused (about 7,000 flats), supported housing (2,568 flats) and housing with social care (7,500 flats). In this case the total would be only about 23,100 dwellings, that is, about 0.6% of housing stock. This shows how ineffective the Czech national housing policy remained in the field of real supply-side subsidies to target those in need.

Vacant municipal flats are allocated according to very different specific criteria set by the municipalities. A part of the vacant flats is often allocated among people offering the highest rent (the envelope method where applicants send in bids on rent and the highest bid wins), but the majority of vacant flats are allocated to people who need low regulated rents – the definition of need (social criteria) is left, however, to the municipalities. Many municipalities (mostly the bigger ones) have a point-giving system for fulfilling some criteria (measuring the need for housing) but the most of smaller municipalities decide on an *ad hoc* basis. Even when a point system exists, the criteria are often not very 'social' ones – points are given mainly for having a permanent address in a particular town for some period of time (non-residents are disadvantaged), number of years on waiting list, size of household

(overcrowding) and source of permanent income (sometimes health conditions, family rupture). In Brno or Prague, the two largest Czech cities, the municipal boroughs who manage the municipal housing stock apply no income criteria. In fact, households with higher incomes may have a preferred status compared to those with lower incomes because of some criteria that are related to the source of permanent income. For example in the Brno-Zabovresky municipality (information is for 2002), an applicant with income from employment or business obtained 20 points, an applicant with income from a disability pension obtained ten points and an applicant living on social support (getting subsistence minimum) obtained zero points. The more points, the better the position on the waiting list. Municipalities tried to avoid future rent arrears in this way.

4.1.5 Tax relief

As with rent regulation and housing allowance, it is also possible to analyse the effectiveness of another form of public support – tax relief – using data (estimates) from the Ministry of Finance for people who submit individual income tax declarations.³⁰ Tax subsidy generally (the possibility to deduct, from the tax base or the calculated tax payable, the full or partial amount of interest or the portion of the principal from mortgage credits, or relief from the tax on imputed rent or on capital gains) is the common form of subsidising owner-occupied housing.

However, making a relevant calculation of the amount and distribution of this public subsidy is no simple matter. In order to calculate it we must first determine how we intend to look at owner-occupied housing. Is owner-occupied housing a consumer good, investment good or financial asset? As O'Sullivan (1985) pointed out, this decision "is by no means trivial. If someone is of the opinion that owner-occupied housing should be viewed as a consumer good, then the main subject of debate is the option of deduction of interest from taxes. No other consumer good receives a subsidy of this kind However, if we regard owner-occupied housing as an investment good, then the perspective from which the tax deduction is viewed changes entirely, as at that moment it becomes analogous to the practice of deducting as costs interest on credit that has been obtained for the purpose of purchasing equipment necessary for production in a standard firm" (O'Sullivan, 1985, p. 6).

On the other hand, in the latter case it is necessary to regard the owner of a dwelling exactly as if he were a typical investor, and thus, specifically in the

³⁰ Income tax declaration for an employee may be submitted by his or her employer if an employee had only one income from one employer; the Ministry of Finance does not, however, have the documentation of tax declarations submitted by employers.

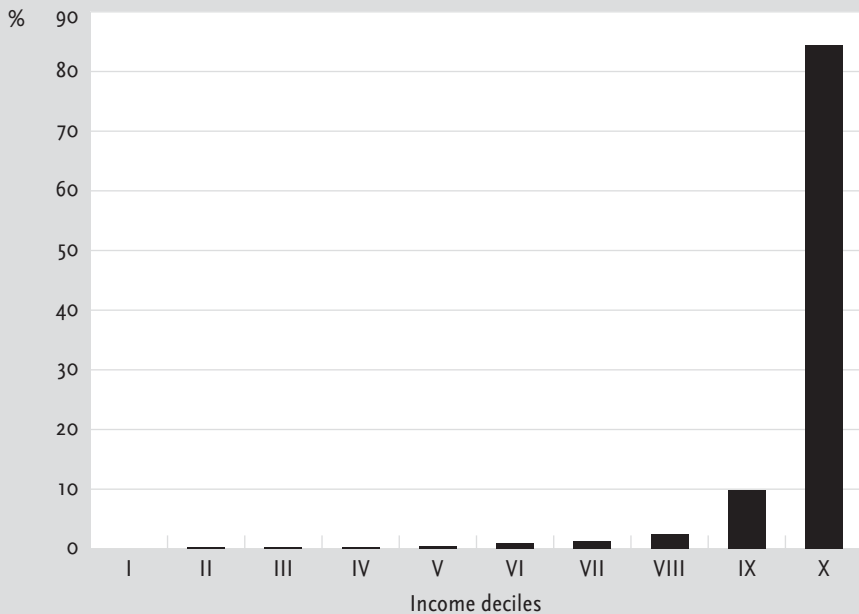
case of the housing market, as a private landlord; all the more complicated about this perspective is that the owner is not just the landlord but also the tenant of the dwelling that he has purchased and occupies. A typical landlord must, after deducting his costs, pay tax on the rent he collects from his tenants – and so too should the owner-(self)landlord, although the rent, which he is essentially collecting from himself, is implicit rather than real. Part of his taxable income is moreover not just income from rent but also income from capital appreciation, that is, the gain from the increase in the value of the residential real estate over time. The homeowner has to pay not just the tax on imputed rent but also the tax on capital appreciation (capital gains tax).

To sum up the discussion so far, if, for the purpose of calculating the tax subsidy, I regard owner-occupied housing as a consumer good, then the main tax subsidy is the option to deduct interest on mortgage credit from the tax base, because this kind of support is not accorded to any other kind of consumption good. However, if I look at owner-occupied housing as an investment good, then the deduction of interest from the tax base is perfectly acceptable (in fact, it would be wrong to set any kind of maximum limit on this kind of deduction as that could be seen as a form of tax penalty) and the main public tax subsidy comes in the form of relief from paying tax on imputed rent and the capital gains tax.

In the Czech Republic the possibility to deduct an almost unrestricted amount of interest from housing loans (both mortgage and housing savings loans) used for the purchase of permanent housing from income tax base is not compensated for by imputed rent taxation (the concept of imputed rent is generally not well known) or effectively by capital gains taxation (people are exempt from this tax two years on from the purchase or even sooner, if the capital gain is used for another permanent housing purchase). Therefore we can look at the tax subsidy from the perspective of both the consumer and the investor. For the purpose of effectiveness (as well as subordinated efficiency) assessment in this book I will regard housing as a consumption good and will therefore measure how the tax relief on interest from housing loans is distributed according to household income. The main reason to opt for this perspective is the simplicity of the measurement and also the focus of this book on housing consumption.

Figure 4.4 shows that the distribution of the fiscal advantages derived from the possibility to deduct interests from housing savings loans and mortgage loans from income tax base was in the Czech Republic strongly skewed in favour of the highest-income taxpayers. If the analysis were also to include those taxpayers whose tax declarations are submitted by their employers, the distribution of benefits would probably not be as clearly distorted in favour of people with the highest incomes but the picture would not change substantially. This housing subsidy was therefore likely the most regressive housing subsidy in the Czech Republic. This is also the case in other advanced

Figure 4.4 Distribution of the total fiscal loss to the state budget of the Czech Republic due to tax relief, according to the personal income from economic activity (population of individuals submitting their individual tax statement), 2001



Source: Ministry of Finance

countries, as it is always middle to high-income households that acquire owner-occupied housing, which is why in some countries this tax relief has been completely abolished (UK) or seriously restricted (France, Scandinavian countries). The figure shows that 50% of the lowest-income taxpayers divide up only just under 1.3% of the total subsidy from tax relief, and 30% of the lowest-income taxpayers receive only 0.43% of the total sum of this subsidy.

It was not possible to compute values of other indicators of the level of income inequality before and after the subsidy because only the cumulative percentage distribution of the subsidy among specific income groups (deciles) was available. From the perspective of horizontal effectiveness, all lower income taxpayers were actually excluded from this subsidy as they would not have met the solvency criteria of the banks in 2002.

4.1.6 State premium to housing savings scheme

Although the state premium to housing saving schemes is the highest explicit state housing expenditure, we know nothing about its recipients. Allocation of state premium is not subject to means-testing (unlike e.g., in Germany) and savings are generally made by those households that have income sufficiently high to set part of it aside. It is often said that the main profit from housing savings scheme subsidisation goes to the middle class. The only evidence comes from sociological surveys (on national sample of population) asking people if and how they use the housing savings scheme.

One such survey, *Housing Attitudes 2001* conducted by the Institute of Sociology on a national sample of 3,357 respondents, which I managed in 2001, proved that 48% of those who ranked their household as low-income, did not and did not intend to have a housing savings account. The same applied to only 26% of those who ranked their household as middle-income and 21% of those who ranked their household as high-income (altogether 7% of respondents perceived their household as high-income, 45% as middle income, and 48% as low-income). As indicated by adjusted residuals, those who ranked their household in the middle-income group used or intended to use the scheme significantly more for general savings (i.e., not for housing) and those who ranked their household in the high-income group used or intended to use the scheme (both savings and loans) significantly more for housing purposes. The differences among respondents according to perceived income situation of their households are statistically highly significant (Pearson chi-square had a value of 223 with 8 degrees of freedom). This shows that effectiveness of state premium on housing savings was, probably, also very low.

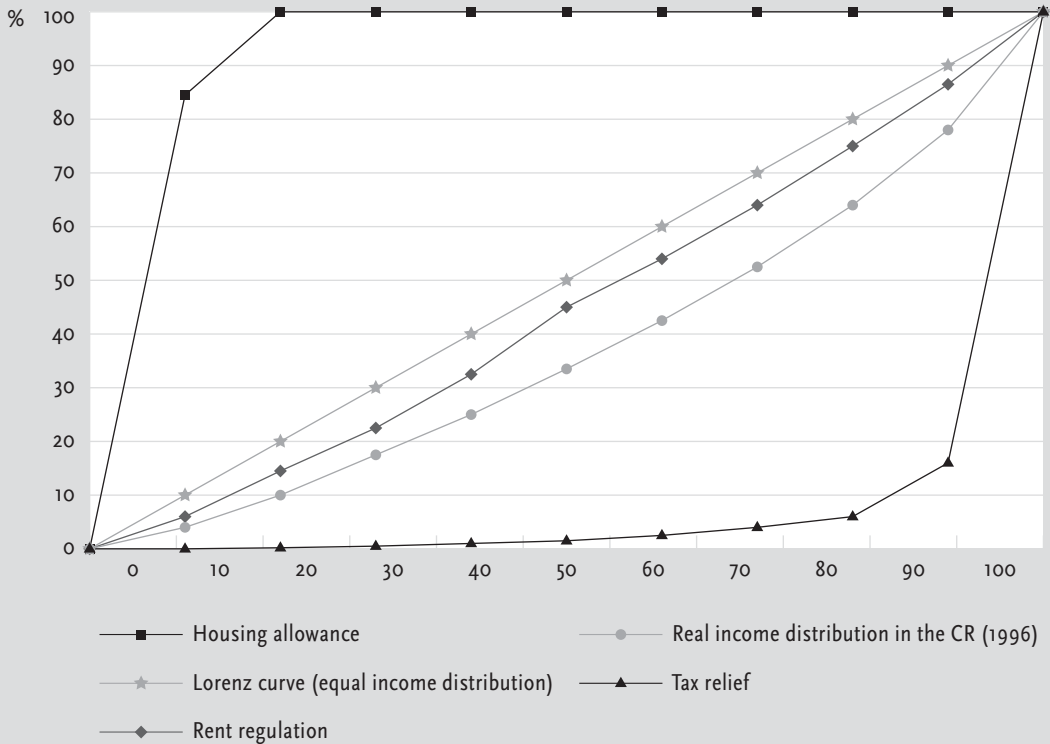
4.1.7 Conclusion

Figure 4.5 is an attempt to capture the distribution of selected housing subsidies in a Lorenz curve. In view of the fact that many subsidies are not income-tested and thus the income of applicants cannot be ascertained even from alternative sources, we can draw only the distribution of the housing allowance (according to the total equivalent income and FBS 2002 simulations), the distribution of an indirect subsidy following from tax relief (according to the total gross income of a taxpayer, applies only to people submitting their own tax assessment basis and according to the MF) and distribution of the economic subsidy following from rent regulation (according to total equivalent income and according to FBS 2002 simulations).

Among the analysed housing policy instruments, housing allowance was most targeted at the households with the lowest income; practically the entire volume of state funds paid out in the form of the housing allowance was divided among 20% of households with the lowest income. The curve capturing the distribution of economic subsidy in the form of rent regulation most approximates the curve of equal income distribution and therefore it is clear that low-income households and high-income households benefited from rent regulation almost equally. Tax relief, on the contrary, benefited particular households with the highest income; 90% of households divided among themselves less than 20% of the total volume of this indirect support, the remaining 80% of the support went to 10% of households with the highest income.

The effectiveness of three selected housing subsidies was especially evaluated: economic subsidy stemming from rent regulation, tax relief and housing allowance. Given that both in the Rawlsian and the Utilitarian concepts

Figure 4.5 Distribution curve of selected housing subsidies in the Czech Republic



Sources: FBS 2002, Microcensus 1996, Ministry of Finance, own computation

of the welfare state effectiveness is linked to equality, the analysis of effectiveness was based on two criteria. The first criterion was whether the three instruments contribute to a reduction of the level of inequality in society. To this end several indicators of income inequality were used. The second criterion was based on a comparison of the real distribution of the subsidy among various income groups with a normative criterion of effective distribution. Effective distribution of a subsidy was regarded as distribution of the subsidy where 90% of the sum of resources was distributed among 50% of the lowest-income households, and 75% of the sum of the subsidy was distributed among 30% of the lowest-income households. A test was also made of the hypothesis of whether the percentage of households with an entitlement to the subsidy is significantly higher among the lowest-income deciles in comparison with the percentage of households entitled to the subsidy in the highest-income deciles.

The results of the tests showed that households most likely paying regulated rent were relatively evenly distributed across the individual income deciles. It also confirmed that the economic subsidy following from regulated rent was significantly higher among highest-income households in comparison with the lowest-income households. Rent regulation did not fulfil the normative criterion of effectiveness either, as 50% of the lowest-income households received approximately 46% of the sum of the subsidy (to satisfy

the criterion of effectiveness the figure should be 90%), and 30% of the lowest-income households received approximately 25% of the sum of the subsidy (to satisfy the criterion of effectiveness it should be 75%).

The main group of recipients of tax subsidy was formed primarily by high-income households, and therefore the effectiveness of this form of subsidy was very low. The percentage of households that took advantage of this form of support was clearly significantly higher among the highest-income households. The Lorenz curve showed that of the instruments evaluated here this form of subsidy unequivocally favoured the highest-income households.

Unlike the other instruments evaluated here, housing allowance is a means-tested benefit, and therefore it is natural that the percentage of households entitled to housing allowance was obviously highest among the lowest-income households. The distribution of this subsidy was also clearly directed in favour of the lowest-income households, which were the largest recipients of the sum that would hypothetically be paid out in housing allowances. The indicators of income inequality revealed that the housing allowances did contribute to a reduction in the level of income inequality in society. This is confirmed again in the depiction of the distribution of the subsidy using the Lorenz curve. The housing allowance also satisfied the selected normative criterion of effectiveness, given that 50% of the lowest-income households would be the recipients of 99% of the sum of the subsidy, and 30% of the lowest-income households would be the recipients of 97% of the sum of resources paid out as housing allowances. However, housing allowance did not meet the criterion of horizontal effectiveness as some needy households were excluded from eligibility (those paying market rents).

Although the available data sources do not allow full empirical verification, it may be assumed that the other housing policy instruments aimed at supporting homeownership tenure – economic subsidy stemming from privatisation of public housing and state premiums to housing savings – also, very probably, displayed relatively low effectiveness. The same applies to supply-side subsidies in the field of rental housing – low effectiveness was demonstrated by showing the gap in the share of housing stock that could be labelled social housing, if I use a wide or narrow definition of social housing.

4.2 Efficiency

Here I intend to assess the efficiency (subordinated to the concept of effectiveness) of selected housing subsidies in the Czech Republic; the goal is to assess particular subsidies against the following assumption:

Main assumption: Subsidies are efficient when it is not possible to meet redistributive goals in the field of housing consumption in a less costly way, that is, under an alter-

native setting of the subsidy or an alternative setting of the whole set of subsidies.

I have previously mentioned and justified why the concept of efficiency is, in my book, subordinated to the concept of effectiveness and how difficult is to measure the efficiency of subsidies if wider interactions between markets were also taken into account. The wider economic impact of subsidy alterations, asking for the use of econometrics and additional data sources, is therefore measured and evaluated only for one type of subsidy – economic subsidy stemming from rent regulation. For all other types of subsidies I will only look at whether any short-term public savings could be achieved if current subsidy rules are changed (with no taking into account of the interactions with other housing subsidies and with only weak attention paid to wider economic and social consequences). This ‘restricted’ methodological approach is the result of the limitations of econometrics and is also well reflected by the subordinated position of efficiency in my policy evaluations.

In the following sections I will evaluate the efficiency of economic subsidy from rent regulation, housing allowance, tax subsidy and state premium to housing savings scheme.

4.2.1 Economic subsidy from rent regulation

The total amount of economic subsidy allocated to households living in rent-regulated housing is difficult to calculate but it was estimated at a level of CZK 10 bn in 2002 and CZK 7-8 bn in 2005. If estimated correctly, it could be one of the largest housing subsidies in the Czech Republic (next to state premium to housing savings scheme). From an economic perspective, rent regulation in its current design has caused incalculable damage. The negative economic effects include in particular:

- ineffective allocation of flats – many households occupy flats that are disproportionately large in relation to household size, while many other households occupy flats that are too small or are completely excluded from the sector of rent-regulated housing; all households are thus trapped in the ‘golden cages’ they were allotted many years ago, when they were in quite different circumstances (well documented by surveys *Housing Attitudes 2001*, *Social Conditions of Households 2002* and others);
- the creation of a perpetual and artificial shortage of flats (long municipal waiting lists documented by the survey *Local Government and Housing in 2001* and regular surveys by the Institute of Urban Development among selected municipalities);
- the market rent applied in vacated or newly built rental flats is skewed and exceeds the equilibrium rent, which is the rent level that would be established if rent regulation did not exist (see Maclennan, 1982; Fallis, 1985; Lux et al., 2004; Lux & Sunega, 2004);

- the large black market primarily in municipal rental housing;
- the growing number of uninhabited (vacant) flats in the rental housing sector (documented by census data between 1991 and 2001);
- the lack of sufficient resources to modernise and repair the housing stock, prolonging the poor quality of housing and increasing the hidden deficit of repairs and modernisation inherited from the ineffective management of flats under the previous regime.³¹

As described theoretically by Maclennan (1982) and Fallis (1985) in their housing economics monographs, rent regulation in one housing market segment may have a substantial impact on rent prices in another market segment where rents are negotiated freely (rent regulation is often applied on 'old' running tenancies whereas it is withdrawn for new tenancies). This theoretical argument has been partially verified in the Czech environment by econometric simulations made by Petr Sunega and myself (see Chapter 4, or for more detail, Lux & Sunega, 2004). The simulation of the housing market and consequences of rent growth in rent-controlled housing was based on the assumption that people would choose their tenure rationally and therefore they would decide to leave rental housing to homeownership if the rent paid to the landlord (net of housing allowance) rose higher than the user costs of homeownership. When demand for rent-controlled housing is saturated (demand gradually decreases due to the rent growth in the rent-controlled housing segment and gets saturated by the growing number of vacant rental flats) and, at the same time, landlords earn appropriate returns from renting their properties (returns comparable to yields from alternative investments taking into account the specific risk premium), market rents are assumed to be in equilibrium. In Prague, the equilibrium market rents would be, according to the results of the simulations, about one third lower than the skewed 'market' rents in 2002 if rent control had been immediately abolished.

Rent regulation is also an important factor behind the black market practices which were common and widespread in the country until very recently (unlike in most developed or transition countries). Generally, many tenants who did not need their rental flats rented them on the open market for market rents without the consent of the landlord (mostly municipality). The other form was 'to sell' the right for regulated rent and protected tenancy on the open market; 'the price' for such title was in 2002 between half and two-thirds of the price of the comparable owner-occupied dwelling. It has been

31 In this regard it should also be noted that the level of regulated rent usually serves as a reference point for determining the amount of the contributions homeowners pay into funds for repairs and house modernisation. If it were raised then the willingness of homeowners to contribute appropriately to the modernisation and reconstruction of the buildings would increase.

partially proved (Lux *et al.*, 2006) that rent regulation also leads to a decrease in household mobility aspirations and may thus increase the unemployment rate in the Czech Republic.

A special new econometric methodology has been applied here to measure 'adequate' ('efficient', 'optimal') rents in the rent-controlled sector to attain efficient rent policy (using Lux, 2007). This methodology was introduced as a 'quasi-normative approach to housing affordability' and it was originally related to the housing affordability issue.

It is often cited that the main goal of housing policy reforms for demand-side subsidies was to decrease public spending and increase policy efficiency (Maclennan & More, 1997; Harloe, 1994; Priemus, 1997; Ghekiere, 1992; Borgegard & Davidson, 2000). Let me thus define the percentage value of an increase or decrease in total public housing expenditures $PC_{t,t+1}$ incurred by the rent increase in the rent-controlled housing stock as relative public costs (RPC_{t+1}):

$$RPC_{t+1} = \frac{PC_{t+1}}{PC_t}$$

The level of rent in rent-controlled housing that leads to the lowest relative public cost might be perceived as an economic quasi-norm on 'optimal' rents (from the point of view of efficiency). Under such rents the total public cost will be lowest. During simulations of relative public costs I would assume that basic housing affordability norms (targeting criteria, affordability limit) are well incorporated into the existing housing allowance formula. It means that for the recent level of regulated rents the housing allowance equation well reflects the social norms connected with housing affordability (e.g., what effort ratio for particular type of household is perceived as too high and therefore requires state help in the form of an allowance). However, both notional housing costs (tariffs) and part of the subsistence minimum (designated for housing expenditures) incorporated in the specific Czech housing allowance (see above) should be uprated proportionally to the simulated rent increase at each stage of the simulation. In this manner those who already receive the allowance will not be affected by a rent increase and will still pay a similar proportion of their income on housing. The uprating will also increase the maximum income in the equation, and this will allow other needy households (including middle income households at the low end) to apply for a benefit. In this manner the simulation of 'optimal' or 'efficient' rents in rent-controlled housing would not breach the effectiveness imperative of subsidies – effectiveness of subsidies to tenants is assumed to be assured by distributional parameters incorporated in the housing allowance formula.

In my simulations, I employ real public costs and benefits of rent change under the real economic, social and institutional conditions of particular so-

ciety. This may be defined as a 'context-based' approach in contrast to the 'universally-applied' approach based on pure housing economic theory. The econometric public cost-benefit analysis will thus take into account not only the most relevant public cost and benefit items, but also the side effects of a particular housing allowance and housing policy changes generally.³² In this way the proposed economic quasi-norms reflect a real situation more satisfactorily than economic quasi-norms derived from economic theory.

To begin with, it is necessary to identify the main public cost items used in simulations. As the aim is to measure the relative public costs ($RPC_{t,t+1}$), only those public costs that change with rent level are selected: the revenue subsidy to municipal landlords (RS_t), public housing construction costs (HC_t), public housing allowance costs (HAC_t), Consumer Price Index costs (CPI_t) and costs arising from voids in municipal dwellings (CVV_t).³³ The following equation shows the expected correlation between the variable and rent price.

$$PC_t = RS_t^- + HC_t^- + HAC_t^+ + CPI_t^+ + CVV_t^+$$

Consumer Price Index costs are the public costs of up-rating pensions and social benefits when rent increases are reflected in the consumer price index. Costs via voids in municipal housing are included in an attempt to estimate the costs of residualisation of municipal housing, which are often overlooked. The higher the rents, the higher the proportion of occupants in rental dwellings coming from the lower income strata of society due to the outflow of better-off households to homeownership. This in turn has empirically verified effects on costs via voids in the residualised municipal housing stock. A higher vacancy rate in social housing is a well-known side effect of the policy that gives preference to demand-side subsidies over supply-side subsidies, and this fact should not be ignored. Residualisation of rental housing also gives rise to the potential costs from rent arrears, but these are not included in the simulation because it has already been demonstrated elsewhere that rent arrears are not dependent on rent levels if the amount of the benefit fully compensates for the increase in rent for benefit recipients (More et al., 2003, p. 88; *Housing Corporation* 1997, p. 12).

Many research studies in the UK have also analysed the impact of a rent increase on labour market incentives (Bradshaw & Millar, 1991; Wilcox, 1993a; Wilcox, 1993b; Wilcox, 1994; Ford & Wilcox, 1994; Ford et al., 1995; Kearns et al.,

32 Change in policy towards housing allowances decreases the direct costs from social (rent-controlled) housing but increases the costs from the housing allowance and its administration and may have an impact on labour market incentives and social exclusion. Wherever possible all this should be included in the calculation to determine the quasi-norm.

33 Costs via voids reflect the loss of rental income in the case when rental housing becomes too residualised.

1996; Kempson *et al.*, 1997; Wilcox & Sutherland, 1997; Bingley & Walker, 1998; Ford *et al.*, 1998; Pryce, 1999, etc.). While it is not the aim of this book to summarise the findings of these studies, it is worth noting here that they all give consideration to the question of whether or not the UK housing benefit with a relatively sharp taper leads to the poverty and unemployment trap. Though there are rational economic reasons why it may do so, analyses of empirical data have shown that this hypothesis does not necessarily apply to certain types of households, and even when it does the effect may be negligible. The taper of the Czech housing allowance was relatively slight (0.1) and this, together with the findings from British housing research, means that labour market implications can be excluded from the analysis.

In the simulated model the quasi-norms on 'optimal' rents are estimated on the basis of a single year, and therefore it is possible to assume that all other income and demographic variables during the simulated rent-increase stages remain constant. The simulation estimates the relative public costs of higher rents in the rent-controlled housing sector in 2002.

4.2.1.1 Data and methodology

The simulations presented in this analysis draw on several data sets. The main data source was again FBS 2002. With the use of data from the *Housing Attitudes 2001* survey it was possible to test a Logit model designed to calculate the probability of a household moving out of the rent-controlled housing sector. *The Social Condition Survey 2001*, conducted by the Czech Statistical Office on a representative sample of 10,599 Czech households, and the KISEB database of market rents, run by the Institute for Regional Information, were used as sources to estimate the demand for rent-controlled housing. Data on transaction house prices in 2002 from the Czech Statistical Office were again used to estimate house prices.

Any increase in rents would be connected with an outflow of better-off households from the rent-regulated sector. The reason for this is that the increasing housing costs of these households are not compensated by a benefit. A rational household compares its net rent (rent after deducting a potential housing allowance) and the user costs of comparable owner-occupied housing, and finally chooses the cheaper option. For the computation of user costs I used here the same equation, same variables and same values of these variables as for the estimate of economic subsidy from rent regulation made in the previous chapter. The expected price appreciation g was, however, excluded in the first step, as it is not entirely clear whether Czech households take price appreciation into account when they make decisions about moving. However, price appreciation can be a very important aspect of tenure choice, and therefore it was included in the sensitivity analysis of the model.

The price of the dwelling was estimated using a hedonic price regression

model, again similar to the one used both for the housing affordability analysis and estimate of economic subsidy following from rent regulation (see above, adjusted R^2 was almost 64%). However, the tenure choice analysis is refined here. The fact that the move to owner-occupied housing is rational from the economic point of view is not enough to lead people to move in reality. First, the purchase price of the new dwelling must be affordable, or, more precisely, mortgage loans must be accessible and the household must be able to meet the solvency criteria of the particular bank in order to receive a loan (credit constraints). Second, people must be inclined to move – for example, older people are much less willing to move than the young, even if moving would save them money. Many people would prefer to adjust their consumption patterns than to move to their own housing. Three conditions were therefore set in order to determine the probability that a household would be willing to move out of rent-controlled rental housing to owner-occupied housing:

- movement to homeownership is beneficial (user costs < net rent);
- the household meets the solvency criteria for receiving a mortgage credit; and
- estimated probability of movement (computed by move-stay Logit model) equals 1.

The criteria applied by the leading mortgage lender in the Czech Republic were used in order to define precise credit criteria. The Logit regression used to determine move-stay probability was run on a sub-sample taken from the *Housing Attitudes 2001* data. The final model is presented in Table 4.4. The sub-sample contained only respondents living in rent-controlled housing. In the analysis the Nagelkerke R^2 equalled 0.235 and almost 70% of predictions were correct. As expected the probability of moving was influenced mainly by the size of residence (the bigger the residence, the higher the probability of moving), the age of the respondent (the higher the age, the lower the probability of moving), the age of the dwelling (the older the dwelling the higher the probability of moving out) and the size of the dwelling in relation to the size of household (overcrowding increases the probability of moving).

After behavioural reactions to rent increases were simulated the total public costs were computed. The first cost item monitored in the simulation was *public expenditure on housing allowances*, calculated as the percentage of households eligible for the housing allowance at a given simulated rent level,³⁴ multiplied by the total number of households living in rental dwellings and the

34 The take-up of housing allowance was assumed to be 100%. Though current take-up is lower, it would increase if rents played a substantial part in household budgets. Moreover, for the purpose of analysis it is better to overestimate public costs than to underestimate them.

Table 4.4 Move-stay decision (Logit Model)

Variable	Beta
<i>Constant</i>	1.437*
Size of residence (up to 5,000 inhabitants)	-0.570*
Size of residence (5,000 – 100,000 inhabitants)	-0.172
Size of residence (more than 100,000 inhabitants)	0.087
Size of residence (Prague)	ref.
Date of construction (up to 1945)	1.020*
Date of construction (1946–1960)	0.629
Date of construction (1961–1980)	0.402
Date of construction (1981–1990)	0.773
Date of construction (1990–)	ref.
Age of respondent	-0.049**
Number of persons per room	0.368*
Nagelkerke R²	0.235
Predictions correct	69.5% (cut-off 0.5)
N	742

* Significant on 0.05 level of significance.

** Significant on 0.01 level of significance.

Note: Dependent variable is a dummy variable with values 1 (move) and 0 (stay).

Source: own computation, Housing Attitudes 2001

average simulated housing allowance for a given rent level.

Second, the simulation took into account the *revenue subsidy to municipalities*, which generally amounts to the difference between the costs of management and maintenance of municipal housing and municipal rental income. In reality, there is no such a subsidy in the Czech Republic and therefore the question may be posed: why should it be included in the public costs? The absence of revenue subsidy contributes to the deterioration of the housing stock and the poor efficiency of housing management because rental income does not cover necessary management and maintenance costs. At some point somebody has to pay the accumulated debt on housing maintenance. However, the level of such a debt is very difficult to measure. The revenue subsidy (computed as the difference between ‘cost’ and regulated rent) thus represents here the current value of necessary future public investments. According to the findings from Ministry for Regional Development, the annual cost rent in second-hand flats is determined as 2.8% of the dwelling price. This rent includes only maintenance and management costs; capital costs are excluded because the municipalities received the housing stock through a no-charge transfer from state at the beginning of the transition period. The revenue subsidy is therefore counted as the difference between real rental income under the simulated rent level and rental income from above defined cost rent. It is important to note that the revenue subsidy for municipalities may

also be negative – if rental income exceeds the M&M costs then municipalities achieve additional public benefit (i.e., negative public subsidy).

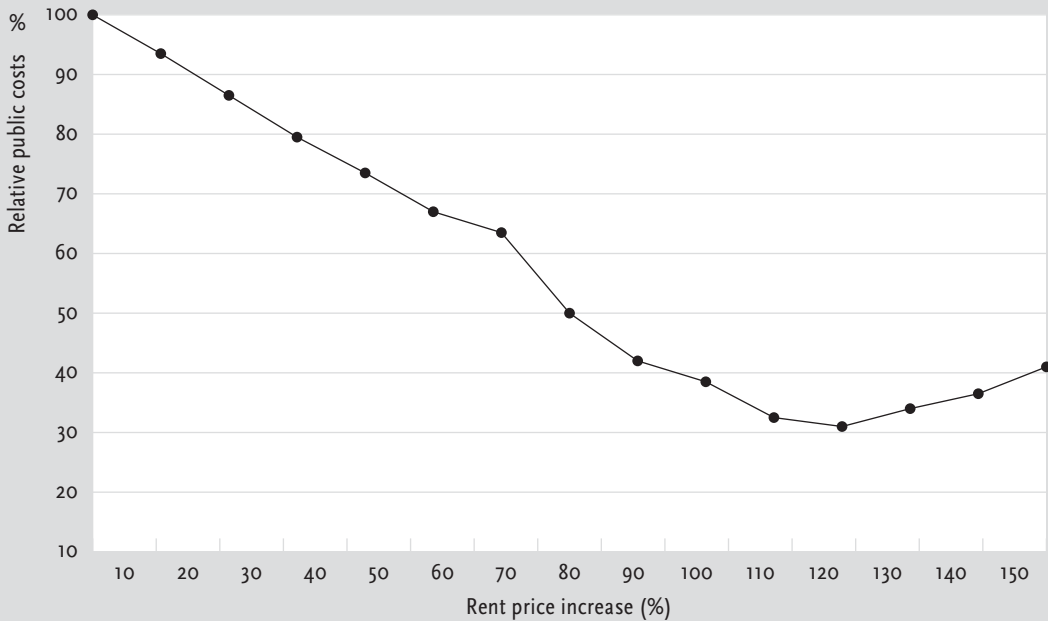
Third, the simulation also includes *the costs arising from the pension and social benefit up-rating (CPI costs)*. The adjusted weight of the rent in the consumer basket used for the purpose of up-rating pensions and benefits was 2.344% in 2002. Therefore, a 10% rent increase in rent-regulated flats would result in a 0.2344% increase in the consumer price index (CPI). According to information from Ministry of Labour and Social Affairs (and its research institute), a 10% rent increase could result in additional annual public costs arising from the pension and social benefit uprating that would amount to CZK 463 million.

Fourth, as no reliable model for estimating the *costs via voids of municipal landlords* could be found from the municipal performance data (there are almost no voids recorded in 2001), the simulations used the following assumption: today there are no voids, and empty flats will appear only when the number of vacated municipal flats at a particular stage of simulation exceeds the estimated additional (unsatisfied, hidden) demand for rent-controlled housing in a given region.

Finally, the simulation calculated the *subsidies for the construction of new public rental dwellings*. In order to calculate the cost of these subsidies, it was necessary to presume a certain norm of need for new public housing construction. The norm was defined as the number of dwellings capable of satisfying 10% of the estimated additional demand for rent-controlled housing in a given region. The higher the rents in the rent-controlled sector, the higher the tenant turnover and the lower the unsatisfied demand for this type of housing would be – this would consequently lead to lower public housing construction costs. Though there is no specific reason to set the norm at a level of 10% of additional demand, the impact that changing the norm to 20% or even 50% of additional demand has on quasi-norms on rents is negligible (see the sensitivity analysis below).

The 'cost' rent of new dwellings is defined as the total of all capital costs (mortgage repayments) and other management and maintenance costs (calculated as 2% of the property value).³⁵ The difference between collected rent, which equals the regulated rent at a given stage in the simulation, and 'cost' rent would be covered by public subsidies for construction of new public rental dwellings – either in the form of a capital grant or a qualified loan. The costs to the public budgets arising from grants and qualified loans were expressed in the simulation in their net current values in order to clearly distinguish the costs of the grant from those of the qualified credit. A financial

35 If the construction of new municipal flats occurred only on a commercial basis, then according to our calculations the average 'cost' rent in new municipal flats would reach approximately 9% of the property price.

Figure 4.6 Relative public costs and rents

Source: FBS 2002, own computation

optimisation programme was developed which sought an optimal combination of a grant, qualified and commercial credit to cover capital costs of new public housing construction at a given rent level while ensuring the lowest possible total public costs (see Appendix C). In this manner I estimated the public housing construction costs.

4.2.1.2 Conclusions and sensitivity analysis

Figure 4.6 shows the final shape of the relative public-cost curve. Clearly there was a relatively large scope for rent increases in Czech rent-controlled housing to meet the assumption of efficiency of this economic subsidy. Within this framework the rents should be, however, raised only to 220% of current levels, because it is evident that any rent increase above this would not result in public savings. Though, on average, such an increase in rents would not be sufficient to raise the rent to market levels, according to the simulated public cost-benefit analysis, when particular income, demographic and other conditions valid in 2002 were taken into account, a higher rent increase appears not to be a rational policy goal from the point of view of efficiency.

Figure 4.7 shows the change in each public cost item incurred by 10% regulated rent increase. CPI costs and revenue subsidies to municipal landlords change linearly with rents while housing allowance costs, public housing construction costs and costs via voids are far more dependent on the behavioural aspects of the simulations – moving from rental to owner-occupied housing. The figure also shows the significance of CPI costs that grow faster

than housing allowance costs in the specific Czech environment.

The model was based on several assumptions, which, if they were to change, could change the results of the simulations too. Firstly, we should find out which cost items have the greatest impact on simulation results. The following is a partial elasticity of total public costs according to each cost item. The elasticity (E) shows a percentage change in total public costs incurred by a 1% change in a particular cost item.

$$E^{RS} = \frac{\Delta PC}{\Delta RS} = 0.1038\%$$

$$E^{HC} = \frac{\Delta PC}{\Delta HC} = 0.8379\%$$

$$E^{HAC} = \frac{\Delta PC}{\Delta HAC} = 0.0489\%$$

$$E^{CVV} = \frac{\Delta PC}{\Delta CVV} = 0.0093\%$$

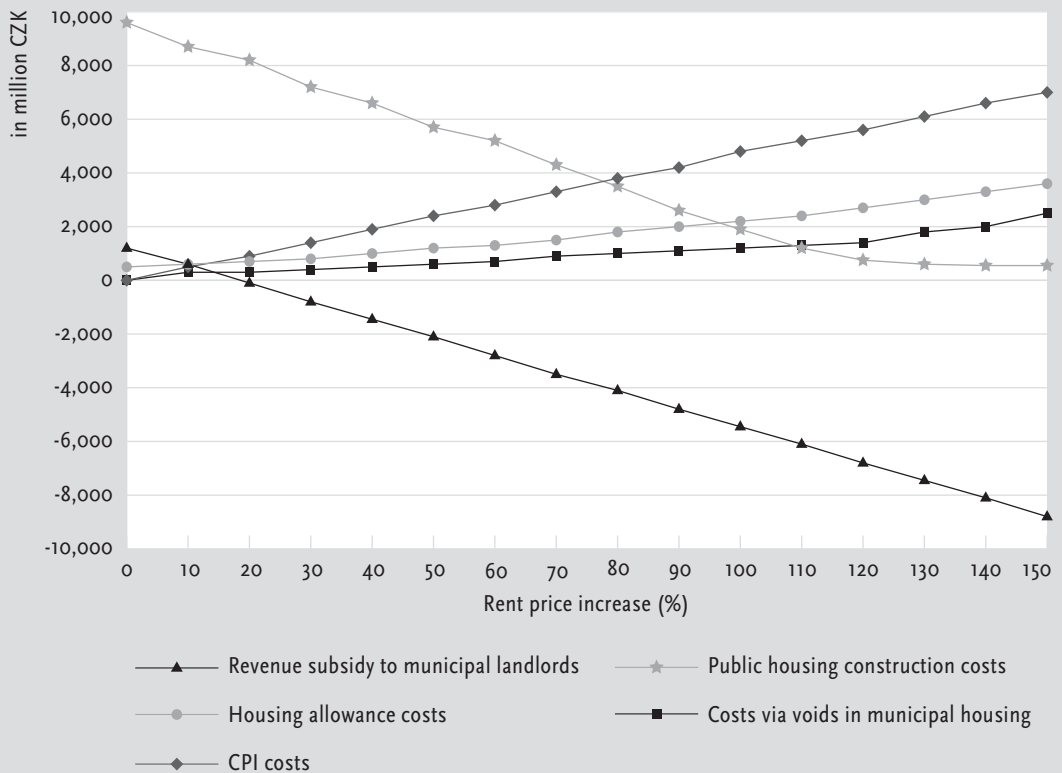
$$E^{CPI} = \frac{\Delta PC}{\Delta CPI} = 0.4049\%$$

Evidently housing construction costs and CPI costs form the most important items in the total public costs summary. However, the real impact of particular cost items is far more important. As the public-costs relationship with rent level is not always fully linear, I analysed the changes caused by a 10% rent increase ($t = 1.1$). The percentage changes in particular cost items and their weighted impact (elasticity is used as a weight) on relative public costs are:

$\Delta RS_{t=1.1} = -56.14\%$	$\Delta RS_{t=1.1} * E^{RS} = -5.83\%$
$\Delta HC_{t=1.1} = -8.35\%$	$\Delta HC_{t=1.1} * E^{HC} = -7.00\%$
$\Delta HAC_{t=1.1} = 17.19\%$	$\Delta HAC_{t=1.1} * E^{HAC} = 0.84\%$
$\Delta CVV_{t=1.1} = 114.64\%$	$\Delta CVV_{t=1.1} * E^{CVV} = 1.07\%$
CPI	$= 4.05\%$
Total	= -6.87%

The CPI weighted impact is calculated as a residual impact. The sum of weighted impacts is equal to almost 7% total public cost decrease (i.e., public savings incurred by a 10% rent price increase). As we see, public housing construction costs not only have the highest elasticity but also the highest dynamic (-7%). Obviously revenue subsidies to municipal landlords (-5.8%) and CPI costs (4%) also have a high dynamic. Conversely, housing allowance costs have relatively low elasticity and the lowest dynamic. This is partly a result of

Figure 4.7 Separate public cost items and rents



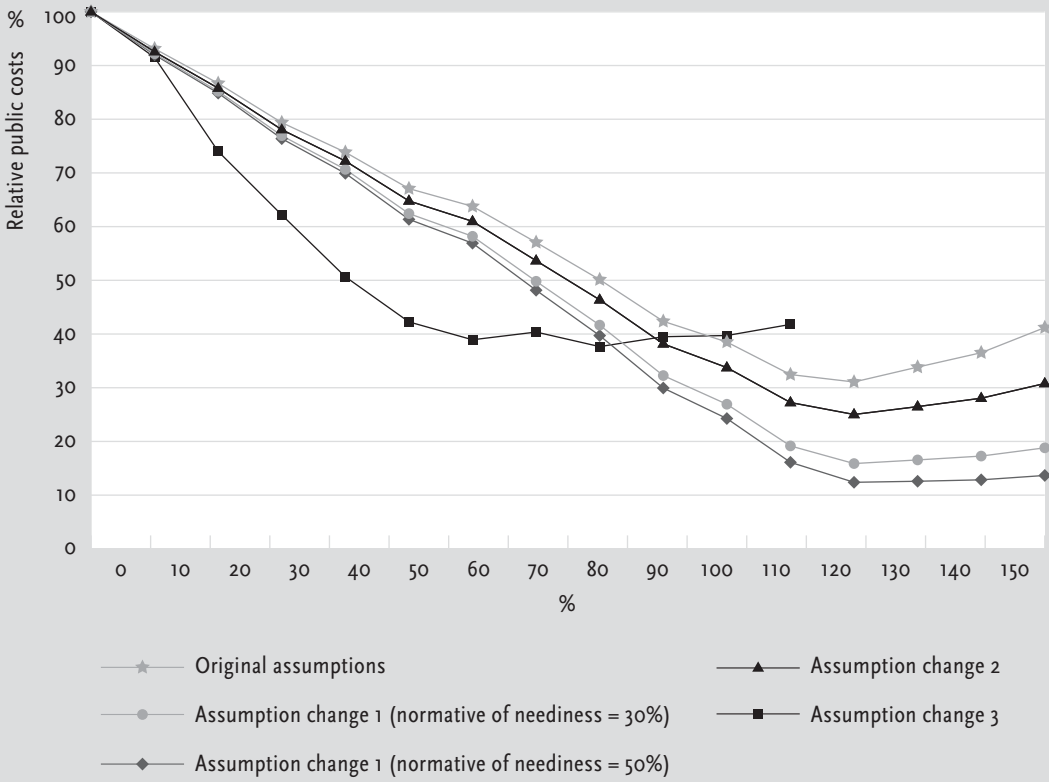
Source: FBS 2002, own computation

the household structure in rent-controlled housing (a significant proportion of households had high incomes).

As public housing construction costs show the highest elasticity and the highest total dynamic, this particular cost item should be focused on in sensitivity analysis. There may be a problem connected with the expected scale of needy housing construction. Simultaneously, municipalities may be able to solve part of the problem with empty flats by their demolition or sale. The movement from rental housing to owner-occupied housing may also be different, if tenants' decisions take into account future price appreciation. The following assumption changes were therefore tested:

1. A change in the annual 'need' norm, that is, the demand for public housing construction from 10% of the additional demand for rent-controlled housing to 30% and 50% of the additional demand for rent-controlled housing.
2. A decrease in the costs via voids in municipal housing to 50%.
3. The inclusion of the expected price appreciation into tenure choice. The expected price appreciation (g in the equation on user costs calculation) was estimated separately for eight zones according to past price increases. All Czech counties were divided into eight zones based on average annual price change in 1998-2002. Under the assumed price cycles the expected annual appreciation oscillated around 1.5% in the capital of Prague

Figure 4.8 Relative public costs and rents, after changes in model assumptions



Source: FBS 2002, own computation

(Zone 1) and was close to zero in Zone 8, composed of counties with the lowest past price increases.

As Figure 4.8 makes clear, only the inclusion of the expected price appreciation into tenure choice simulations moved the ‘quasi-norm’ on ‘optimal’ (‘efficient’) rents from a level equal to 220% of current rents to a level equal to 180% of current rents. It is possible to assume that some people rely on price appreciation and also perceive housing as an investment, while many others consider housing purely as a consumption good and do not see any benefit from future capital gains. Taking into account the fact that other important costs arising from the residualisation of public housing could not be included, it is still possible to conclude that the government reference point on rents (the quasi-norm on regulated rents from the point of view of efficiency) should have been ‘somewhere’ between 180% and 220% of controlled rents in 2002.

Further elaboration of these conclusions (re-computation for specific market segments, regions, cities and, especially, social groups of households) would be needed if they should really be used for practical implementation. The purpose of presenting these simulations here is just a rough estimate of how big the difference might be between efficient state rent policy (‘optimal’

rents) and the actual situation in 2002. The results show that the efficiency of economic subsidies in this field was very low because the difference between 'optimal' and real rents in the rent-controlled housing sector was very high.

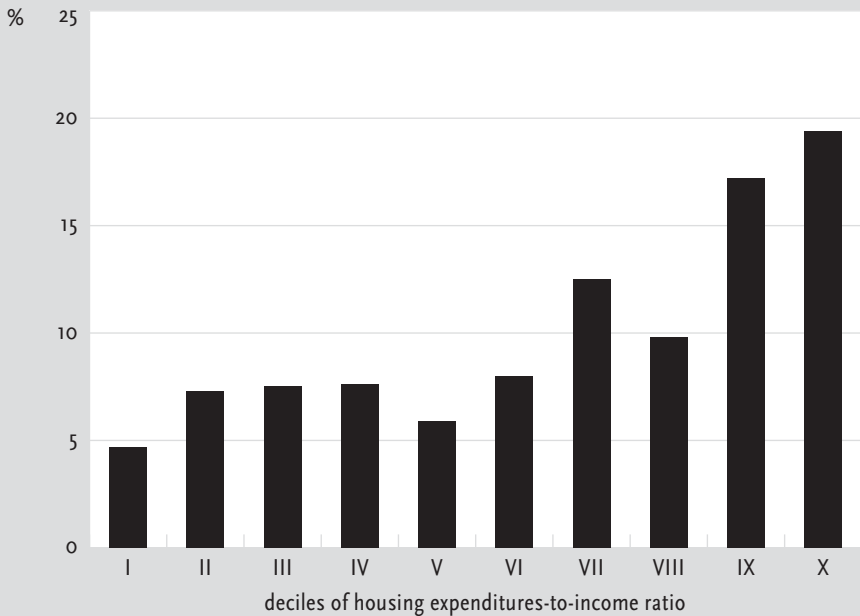
4.2.2 Housing allowances

One serious problem with housing allowance in the form valid until 2006, pointed out in a study by Mareš (2001), was its low take-up, that is, the number of actual applicants was lower than the number of eligible households. "Reference generally is made to the 'non-take up of social security benefits', that is, benefits are not drawn by the people they are designed for, and to an indicator of one form of crisis in the effectiveness of the welfare state – wherein it fails to accomplish its objectives" (Mareš, 2001, p. 3). According to Mareš, less than 40% of households eligible for housing allowance in 1996 applied for it, and similarly in 1999, only around 60% of eligible households applied for it. Among the reasons Mareš cites are the relatively general problems associated with all social benefits: values that prevent a person from letting themselves be dependent on support, rational calculations of its real benefit considering the costs involved in applying for it, a lack of information, the effort to avoid being stigmatised, a lack of capability (Mareš, 2001, p. 12).

However, in the case of the housing allowance there was, in my opinion, an important specific reason for its low take-up. As noted in my evaluation of effectiveness of housing allowance, the allowance is tenure-neutral, does not take into account real housing costs and tariffs used in formula simply ignore the existence of market rents. The main fault of the allowance lies therefore in the fact that it is allocated not according to the level of housing expenditures (being e.g., much lower for outright owners) but only according to the household income situation. Consequently, many eligible homeowners with relatively low housing expenditures do not apply for the allowance; in this way the state offers help as well to those who do not need it (while excluding those who need it). This can be demonstrated by drawing the distribution of housing allowances not according to household income (as was done in the evaluation of its effectiveness) but according to housing expenditure-to-income ratio assuming again a 100% take-up of an allowance.

Figure 4.9 presents the distribution of the sum of potentially paid housing allowances among households with varying levels of total housing expenditure-to-income ratio, if I assume expenditures being before allowance (the 1st decile corresponds to a low level of housing expenditure-to-income ratio, the 10th decile to a high level of housing expenditure-to-income ratio) under the situation of 100% take-up in 2002 (again, using data from FBS, 2002). It appears that the allowance did not adequately target households with higher expenditure-to-income ratio, as, for example, 5% of the sum of potentially paid allowances would be distributed among households with the lowest level

Figure 4.9 The distribution of total sum of housing allowances in the Czech Republic, according to the housing expenditures-to-income ratio (assumed 100% take up), 2002



N = 3,292

Source: FBS 2002

of this ratio (1st decile). It is necessary to note that targeting households with high housing expenditure-to-income ratio should be the main objective of housing allowances; targeting households according to the household income is just a by-product of the main goal of the allowance.

The efficiency of housing allowance was due to low take-up and inappropriate targeting according to real expenditures-to-income ratio (caused by its 'tenure-neutral' setting) definitely lower than optimal. There could be substantial state savings if the allowance was better targeted to those for whom housing really was unaffordable, that is, whose housing expenditure-to-income ratio was high. Outright homeowners needed less state aid than households living in the rental sector. On the other hand, there was no sign that the allocation of housing allowances would lead to rent inflation – as the allowance could hardly be used by tenants paying market rents and as it was related to rents regulated administratively, its role was thus more connected with social policy tasks than with the specific goals of national housing policy.

4.2.3 Tax subsidy

It is generally very difficult to find a tool for assessing the efficiency of tax subsidy; it is definitely more difficult than assessing its effectiveness. One possible approach would be to estimate the influence of tax subsidy on housing demand and house prices but I lack the appropriate data to do so. Clearly, in many cases the tax subsidies increase the level of housing consumption

only among high-income groups of society and have a marginal effect on housing consumption (affordability) among those in need of state assistance. The withdrawal of tax subsidies might thus have an effect only on prices and consumption in high-level housing market segment but we cannot demonstrate it with the data available here. The only thing I can do is to evaluate the scale of tax subsidies in the Czech Republic in comparison with some other developed countries; for this purpose I will use the findings of a recent paper (Lux, 2005a).

The biggest public tax subsidy (and the biggest violation of both tax neutrality and tenure neutrality) can be found in countries that allow almost unlimited deduction of interest (principal) on mortgage credits from the income tax base using the marginal income tax rate (which is usually progressive, and the highest tax rate is usually higher than the standard tax rate on capital income) and where neither imputed rent nor capital gains are taxed. In many countries capital gains tax is not collected regularly, only in the case of the sale of real estate, when it becomes possible to make the best calculation of the amount of capital appreciation – the base then equals the difference between the purchasing price and the selling price. Given that this arrangement benefits owners who never move or at least move rarely, this form of taxation does not fully represent a consistent capital gains taxation. In addition, payment of this type of tax is often ‘deferred’ for several years, and if the income from the sale of the real estate is used within the time frame of deferral to purchase another piece of real estate for residential use, then it may be completely relieved or at least deferred again until the newly purchased real estate is sold.

The following international comparison of tax subsidies in 19 selected countries refers to both possible forms of public tax subsidy: (1) the deduction from the tax base or directly from taxes payable of interest or a part of the principal from mortgage credit used to purchase owner-occupied housing (a public subsidy of owner-occupied housing as a consumer good), and (2) relief from payment of tax on imputed rent and on capital appreciation (a public subsidy of owner-occupied housing as an investment good). Figure 4.10 shows how selected countries are divided according to the significance of the public tax subsidy; this scheme of course provides only an orientation, as in order to rank countries by their total public tax subsidies I would require exact figures on the current values of these subsidies per capita in each country.

A consistent form of taxation of owner-occupied housing is where people on the one hand are unable to use the tax deduction of interest on mortgage credit obtained for purchasing owner-occupied housing, but on the other hand where they do not have to pay tax on imputed rent and tax on capital appreciation (i.e., owner-occupied housing is regarded as a consumer good). Also consistent is the kind of taxation of owner-occupied housing where the owners can take advantage of the tax deduction of interest on credit obtained

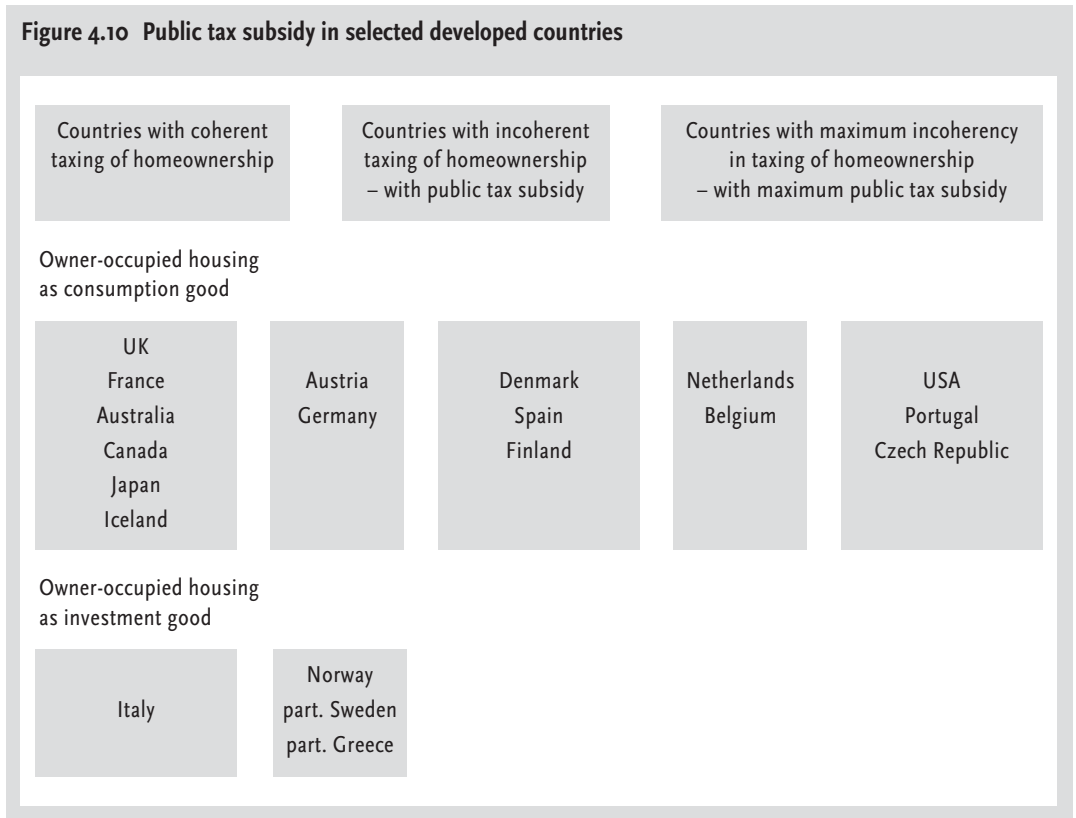
to purchase their housing but still pay tax on imputed rent and capital appreciation (i.e., owner-occupied housing is regarded as an investment good).

Some countries are situated somewhere between the two. For example, in Norway, owner-occupied housing is regarded as an investment good (tax deduction of interest is allowed and imputed rent is taxed), but capital gains are not taxed. Conversely, in Greece capital gains are taxed, but, except for unusually large houses, imputed rent is not taxed. In Austria, owner-occupied housing is regarded more as a consumer good, but the option of tax deduction of the interest exists in a quite limited form. In Germany it is not possible to write off interests from the tax base, but in the past for homeowners (regardless of whether they used credit or not to purchase their dwelling) there was a limited opportunity in the first eight years after buying a dwelling to deduct a certain portion of the purchase price from the tax base as depreciation – this form of tax advantage was replaced in 1996 with a new grant system, so by 2004-2005 it related to only a small proportion of homeowners.

In the countries listed in Figure 4.10 with inconsistent taxation of owner-occupied housing and with a public tax subsidy of owner-occupied housing, what usually happens is that the option to deduct the interests from income tax base is not accompanied by an obligation to pay tax on imputed rent and capital gains (in Denmark, Finland, and Sweden, however, it is necessary to keep in mind that imputed rent is actually taxed in the form of a higher property tax, and thus their relative position is in reality closer to that of Norway and Greece). For the purpose of tax deduction of the interest on mortgage credit, the taxation rate used in these countries is lower than the highest marginal income tax rate applied in those countries, which to a certain extent reduces the level of public subsidy.

Finally, in countries with the most inconsistent taxation of owner-occupied housing, listed in the right-hand column of Figure 4.10, owner-occupied housing receives the maximum possible public tax subsidy because the deduction of interest on mortgage credit is usually applied through higher marginal income tax rates, and owners either explicitly or *de facto* do not pay the tax on either imputed rent or capital gains. Although the Netherlands ranks among the countries that allow taxpayers to deduct the interest on mortgage credit under the marginal income tax rate, the level of public subsidy in this country is reduced by a small tax on imputed rent. Similarly, in Belgium there exists, albeit very limited, a tax on imputed rent, and the deduction of interest on credit under the marginal income tax rate is temporally limited and progressively reduces after five years of credit repayment. For this reason, these two countries are also presented in Figure 4.10 as located somewhere in the middle.

In the majority of the advanced countries monitored here, the taxation of owner-occupied housing was relatively consistent and mainly held the viewpoint of owner-occupied housing as a consumer good. The largest degree of inconsistency was found in the US, Portugal, and in the Czech Repub-

Figure 4.10 Public tax subsidy in selected developed countries

lic as well; the Czech Republic was thus one of a relatively small segment of countries that applied the 'extreme' maximum tax subsidy. It can therefore be concluded that public budgets in the Czech Republic paid a relatively very high price for this regressive support of acquisition of owner-occupied housing and, taking into account the effectiveness of this subsidy, there are definitely many opportunities (reform approaches) to save public expenditures in this field without endangering the affordability of owner-occupied housing for low-income (needy) households at the same time. Efficiency of the tax subsidy in the Czech Republic is therefore low.

4.2.4 State premium to housing savings scheme

The original purpose of housing savings schemes was mainly to offer low-interest and easily available credits for housing purchase and modernisation, that is, the system was originally introduced to help people overcome the 'tilt' problem and increase affordability of housing loans. The efficiency of public support of the system of housing savings may therefore be demonstrated by the value of the coefficient of the outstanding loan-to-savings balance (the share of the balance of loan accounts to the balance of savings accounts). We can see in Figure 4.11 that even many years after the introduction of the scheme the balance reached only 30.8% by 30 June 2005 and the system was still characterised by excessive savings and low demand for loans. Although from 2002 onwards (after stagnation and a slight decline in 1999-2002) the

Figure 4.11 Loan activity of building savings banks in the Czech Republic, 1997-2005



Note: The line shows the share of the outstanding loans granted in a given year to savings (deposits) on the savings accounts of housing savings banks in a given year, in % (i.e., the coefficient of the outstanding loan-to-savings balance).

Source: Ministry of Finance, own computation

value of loan-to-savings balance shows a tendency to increase, it was still below the level of developed countries with a similar system of housing savings (Austria, Germany) in the middle of 2005, where it ranged between 70% and 80%. It is worthy of repetition that if savers do not take out a loan from the scheme they can use their savings (including state premiums) for any purpose.

The reason for the low value of the loan-to-savings balance in the Czech Republic may be the too 'generous' state support, which attracted an excessively large number of clients ('good brothers') into the system. The state premium on housing savings is definitely higher than in Germany or Austria and its generosity, which remained even after the partial reform of the system in 2004, has been admitted even by representatives of two housing savings banks participating in the survey evaluating the efficiency of market-based housing finance system in the Czech Republic (see more in Lux *et al.*, 2005; Sunega & Lux, 2007). Due to the generous state premium no other savings product (at the same level of risk and for particular limit of savings) on the financial market could compete with the housing saving scheme. The optimal amount of annual savings maximising interest return is equal to CZK 18,000, yielding interest of about 27% on annual savings amount for pre-reform contracts (contracts concluded before 2004). Effective interest rate on the total of

savings is lower but is still a double-digit number annually for the five-year savings period while the interest rate on a five-year banking deposit was at the same time only close to 4% a year. Moreover, people can hold onto 'old' contracts (pre-reform contracts) for decades (they can continue to save even after five years under the original set of interest and premium conditions) and many savers do so.

The high public costs and not very transparent outcomes of the whole system are often defended by the argument that housing savings schemes were introduced not to support housing consumption but more to support household saving behaviour. However, even this argument has been proven false by Plischke (2007). She clearly demonstrated that total net savings as a percentage of a country's GDP is definitely not higher in the Czech Republic (with its system of state-supported housing savings) than in Poland (without such a system) and according to time series data there is no sign that the introduction of the housing savings scheme led to growth in the propensity to save. She found a clear inconsistency between the development of value of balance on housing savings accounts and development of net savings as percentage of GDP between 2001 and 2004 – while the first sharply grew, the second sharply declined throughout this period. Moreover, she showed how partial reform of the housing savings scheme at the begin of 2004 had an impact on household savings behaviour – many savers switched their time deposits to a housing savings account in 2003 to be eligible for pre-reform high state premium while the overall level of time deposit savings (including savings held both by commercial banks and housing savings banks) remained stable.

The value of the spread (defined as the difference between cost of funds and average interest rate on loans extended from housing savings schemes) for housing savings banks has been estimated as being probably significantly higher than for mortgage lenders. The reasons for this could be the lower volume of granted loans, the fixed interest rate for the whole period of loan repayment and the possibility to prepay the loan any time free of penalty. Such loan conditions increase operating costs. Housing savings banks also offer low-value loans and administration of such loans could be more expensive (when we consider marginal costs) than in the case of mortgage loans. However, the higher level of spread may also be a sign of hidden 'product' monopolisation and inefficiency because in their loan activities they do not, in fact, compete with mortgage lenders. All housing savings banks are members of larger financial groups; generally, the parent bank (universal bank) owns one housing savings bank and sometimes one specialised mortgage bank as well. In other words, though housing savings banks could offer loans with lower interests than universal or mortgage banks (thanks to cheaper deposits assured by state subsidisation) they are not doing so as in this case they would compete directly with their partners in the same financial group.

The housing savings system played a very important role at the beginning

of transition when mortgages were either not yet introduced or unaffordable for most of the population. However, the comparative advantages gradually disappeared. The system is in acute need of reform but due to the bad legislative framework this would be very difficult. The system (including the level of state premium) may be changed only by a law passed by parliament (and not by a decision of the government); lobbying of powerful banking groups is however much more effective in parliament than among government members. The state premium is set by law in its absolute value (not relating to general economic conditions) and the government cannot adjust the premium level to react to changing inflation and interest rate conditions in financial markets. This makes the whole system very rigid and unresponsive to the changing economic environment.

4.2.5 Conclusions

In the efficiency part of housing policy (subsidy) evaluation I dealt with economic subsidy stemming from rent regulation, housing allowance, state premium to housing savings scheme and tax relief. The efficiency of all mentioned subsidies is probably sub-optimal though I cannot make any judgment on tax relief; especially low efficiency was detected in the case of the economic subsidy stemming from rent regulation and state premiums to housing savings. The sub-optimal result for housing allowance is one of the outcomes of housing allowance being perceived more as a general social benefit than a housing policy tool in the Czech Republic. As the responsibility for housing allowance lies within MLSA, it might be related to other social benefits as well but it shows substantial efficiency failures when the goals and perspectives of national housing policy are taken into account.

I have shown the deep gap between 'efficient' and real rent prices in rent-controlled housing sector and demonstrated low efficiency of state premiums to housing savings both by performance of housing savings bank (low loan-to-savings balance, competition constraints) as well as by savers' behaviour (switching savings from other deposits by holding overall savings rate constant). In the case of tax relief I was able only to show that the Czech Republic belongs among countries with the highest inconsistency in housing taxation, that is among countries with maximal fiscal subsidies to promote homeownership. The actual efficiency has not been evaluated here as data were not available for that time.

5 Efficiency and effectiveness of new supply and demand-side subsidies in transition countries

The previous chapter assessed selected state interventions in the field of housing consumption (housing subsidies) in the Czech Republic. In Chapter 2, however, I noted that inappropriate targeting of huge economic subsidies allocated during the 1990s has also been described in other transition countries. Therefore the question is whether low effectiveness and efficiency of housing subsidies (including new ones) is either specific to the Czech Republic or a common feature of housing policy reform in all (or most) transition countries? If this is not a shared phenomenon then the question arises: what factors visible through international comparison can explain the low effectiveness and efficiency of Czech public subsidies?

In the Introduction I stated that the main goal of this book is not comparative. However, in some cases only international comparison can help understanding of the particular situation in one country. Therefore I have included a partial comparison of housing policy changes in six transitional countries, using the outcome of a *Local Government and Housing* project conducted in 2000 and 2001. This project gathered details of policy programmes directly from country experts and through intense discussion with the research team – and not only from secondary sources alone – and thus met the imperatives on international comparative research discussed above. The selected countries were the Czech Republic, Slovakia, Estonia, Bulgaria, Romania and Poland.

This fifth chapter expands on the second chapter by presenting an evaluation of the efficiency and effectiveness of housing policy interventions in the field of housing consumption in the selected transition countries. Again, the concept of welfare economics has been used for the evaluation; due to a lack of data this could only be done partially and only for those countries that took part in the project. In summary, the purpose of this chapter is to answer the third research question, which is, as follows:

3. *How efficient and effective were state interventions in other transition countries (if the imperative on individual openness of researchers during the international comparison of housing policies is met)? What explanations for particular levels of effectiveness and related (subordinated) efficiency of state interventions in the field of housing consumption in the Czech Republic can be found in a partial international comparison? Can such a partial international comparison help me to understand the specific situation in the Czech Republic?*

Table 5.1 shows the main socio-economic indicators for the selected transition countries in the time of the comparative research, that is between 1999 and 2001. With the exception of Slovakia, the total population was shrink-

Table 5.1 Socio-economic indicators in selected transition countries, around 2000

	Population (in thousands)	Population growth rate (%)	Share of urban population (%)	Area (in km ²)	GDP (PPP) per capita (USD)		Unemployment (%)
	mid-2001 ¹⁾	2001 ¹⁾	mid-2001 ¹⁾	¹⁾	2000 ²⁾	2000 ³⁾	²⁾
Bulgaria	7,867	-1.14	67.4	110,910	6,200	–	17.7 (2000)
Czech Republic	10,260	-0.07	74.5	78,866	12,900	14,285	8.7 (2000)
Estonia	1,377	-0.55	69.4	45,226	10,000	–	11.7 (1999)
Poland	38,577	-0.03	62.5	312,685	8,500	9,588	12.0 (1999)
Romania	22,388	-0.21	55.2	237,500	5,900	–	11.5 (1999)
Slovakia	5,403	0.13	57.6	48,845	10,200	11,643	17.0 (2000)

Sources:

1) United Nations: 'World Urbanisation Prospects, 2001 Revision'

2) CIA: 'World Fact Book 2001'

3) OECD Statistics (www.oecd.org)

ing, particularly in those countries with the lowest GDP per capita (Bulgaria, Romania) and Estonia. The Czech Republic had the highest percentage of its population living in urban areas, while Romania and Slovakia were among the countries with the lowest level of urbanisation. Bulgaria and Romania had the lowest GDP per capita and Bulgaria and Slovakia were struggling with high unemployment.

Tables 5.2 and 5.3 provide summaries of general housing conditions and tenure structure in that time. The most significant changes in tenure structure appeared in Estonia, Slovakia and Romania; these are consequences of large-scale public housing privatisation. In the Czech Republic and Poland, due to the slower tempo of privatisation, municipalities remained the largest landlords of rental housing in 2001. Unfortunately, the figure indicating the share of private rental housing of the total housing stock was not available, though this housing sector was present in all analysed countries. The highest share was probably in Estonia and the Czech Republic, where restitution of property to former owners applied to a relatively large amount of expropriated residential housing. The number of dwellings per 1,000 inhabitants was relatively high in Estonia, Bulgaria and the Czech Republic. From this point of view, it would seem that these countries were characterised by housing sufficiency.³⁶ Poland had the lowest number of dwellings per 1,000 inhabitants and as the only country in our comparison probably suffered from a real shortage of housing units.

³⁶ However, in practice many other factors enter the equation: rent regulation, high costs of acquiring new housing, low quality of prefab housing and relatively low dwelling area per person.

Table 5.2 Tenure structure and its change in selected transition countries, 1991-2001 (% of total housing stock)

	Bulgaria		CR		Estonia		Poland		Romania		Slovakia	
	1992 ¹⁾	2000 ¹⁾	1991	2001 ²⁾	1992 ³⁾	2000 ³⁾	1991 ⁴⁾	2000 ⁴⁾	1990 ⁵⁾	1998 ⁵⁾	1991	2001 ⁶⁾
State rental housing	1.8	1.8	39.0	-	25.8	0.7			21.4	4.0		1.1
Municipal rental housing	2.0	2.2	-	24.0	34.7	3.3	17.9 ⁷⁾	11.5 ⁷⁾	-	-	21.2 ⁷⁾	5.4
Enterprise rental housing ⁹⁾	2.9	3.2	-	-	-	-	13.7	4.6	-	-	6.5	-
Cooperative housing	0.2	0.3	20.4	20.0	5.0	3.9	25.4	28.6	1.5	-	22.1	15.6
Private rental housing	0.5	0.8	-	7.0	n.a.	n.a. ⁸⁾	n.a.	n.a.	1.0	3.0	-	4.1
Rental stock of housing associations	-	-	-	-	-	-	-	0.01	-	-	-	-
Homeownership	91.0	92.5	40.5	49.0	34.5	85.9	43.0	55.3	76.1	93.0	50.2	73.8

Notes and sources:

1) Statistical Office of Bulgaria

2) Housing Policy Strategy, Ministry for Regional Development of the Czech Republic

3) Statistical Office of Estonia; in 2000: 1.1% of housing stock is owned by other owners and the owner of 5.1% is unknown

4) Statistical Office of Poland

5) UN/ECE – CHF Practical Workshop on Housing Privatisation, Krakow 1999

6) Preliminary results of Census 2001; Slovakian Statistical Office

7) Including state rental housing

8) The share is estimated at a level of 10% of total housing stock (Kahrik 2003)

9) Enterprise housing consists of the stock of rental housing owned by former state enterprises allocated among employees.

The majority of housing was privatised or transferred into the ownership of municipalities at the beginning of transition

5.1 Analysis and criteria used for comparison of housing policies

The selected countries were grouped into three types according to the public housing privatisation strategy: (1) Fast privatisers (Romania, Estonia, and Slovakia); (2) Slow privatisers (Czech Republic, Poland); and (3) Bulgaria. Only a weak association between a country's per capita GDP and its privatisation approach can be detected but certainly such a relationship cannot be supported. Figure 5.1 draws a comparison of approaches to public housing privatisation (homeownership versus rental model) with the level of decentralisation in the field of rental housing sector. The y axis represents the application/non-application of right-to-buy policy. Higher decentralisation in the segment of rental housing, measured on the x axis, is assumed to be connected with:

- higher freedom in rent setting and dwelling allocation for both private and public landlords (abolition or substantial limitation of central rent control and/or central public dwelling allocation criteria);

Table 5.3 Housing condition indicators in selected transition countries, 1991-2001

	Bulgaria ¹⁾		Czech Republic ²⁾		Estonia ³⁾		Poland ⁴⁾		Romania ⁵⁾		Slovakia ⁶⁾	
	1992	2000	1991	2001	1992	2001	1991	2000	1992	1999	1991	2001
Number of dwellings per 1,000 inhabitants	400	424	396	427	407	434	289	306	336	352	336	350
Average floor area of dwelling (in m ²)	63.5	63.9	n.a.	49.3 ⁷⁾	53.5	54.0	59.6	61.5	33.7 ⁷⁾	34.4 ⁷⁾	48.3 ⁷⁾	56.1 ⁷⁾
Average floor area per person (in m ²)	25.4	27.1	25.4	18.6 ⁷⁾	21.8	23.4	17.5	19.2	11.3 ⁷⁾	12.1 ⁷⁾	14.6 ⁷⁾	17.5 ⁷⁾
Average number of rooms per dwelling	2.92	2.89	2.66	2.71	2.9 ⁸⁾	2.6 ⁸⁾	3.41	3.48	2.46	2.50	2.86	3.21
Average number of rooms per person	0.86	0.82	n.a.	n.a.	1.2 ⁸⁾	1.1 ⁸⁾	1.00	1.09	0.80	0.88	0.88	1.00

Note: Dwelling is defined as a room or set of rooms and facilities that serve or are assigned to permanent housing and create one structural/technical unit. (In Bulgaria: has one or more exits to commonly accessible area. In Romania: with separate entrance from the staircase hall, yard or street which has been built, transformed or arranged with a view to be used, in principle, by a single household). The indicator is calculated from the total number of dwellings (including both inhabited and vacant dwellings) if not stated otherwise. Room means habitable room that has the possibility of daylight, ventilation and heating, including kitchen if it is only a one-room flat and with minimum area of 8 m². (In Bulgaria: minimum area of 7.5 m². In Poland: minimum area of 4 m². In Romania: minimum area of 4 m² and at least 2 metres high at its tallest point, excluding kitchen. In Estonia: kitchen and other supplementary spaces are excluded). Floor area is defined as total floor area of the dwellings if not stated otherwise.

Notes and sources:

1) Statistical Office of Bulgaria

2) Czech Statistical Office

3) Statistical Office of Estonia

4) Housing Economy in 2000, Central Statistical Office

5) National Commission for Statistics (2001)

6) With the exception of the first figure (number of dwellings per 1,000 inhabitants) all other figures are only for inhabited housing stock. Source: Slovakian Statistical Office.

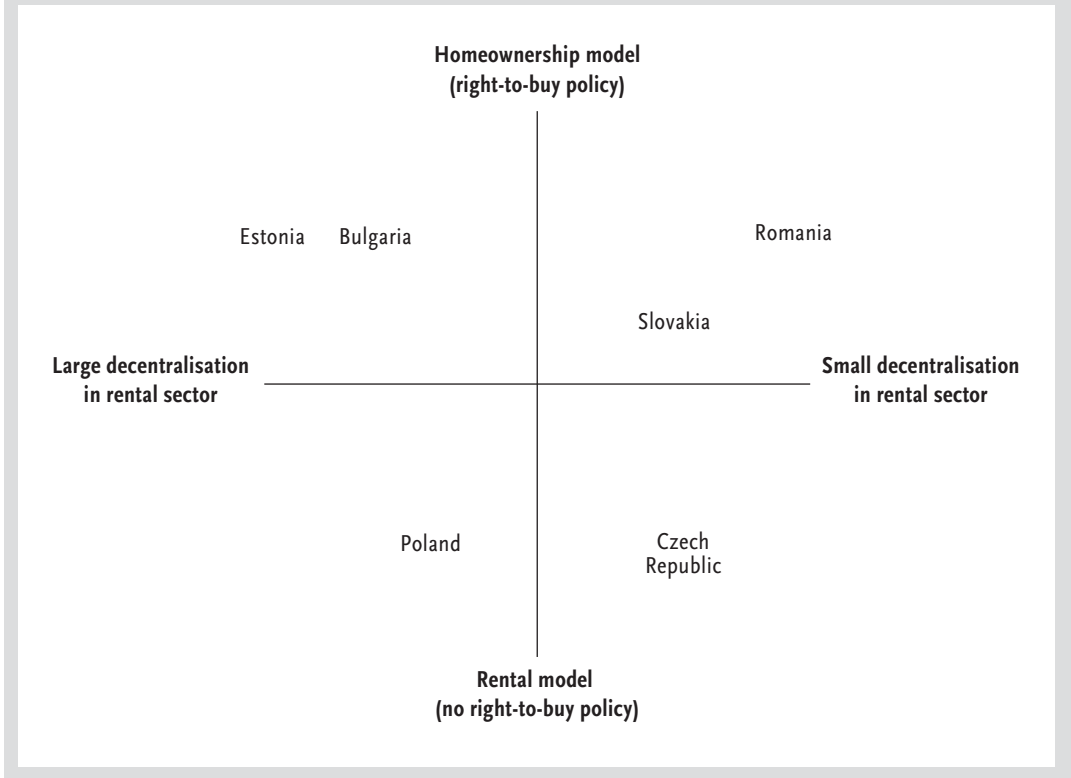
7) Average living floor area of dwelling (floor of habitable rooms and part of kitchen area, over 12 m² for Czech Republic, Slovakia; floor of habitable rooms for Romania).

8) The figures are calculated from inhabited housing stock only.

- lower state (legal) tenant protection in both private and public rental housing; and
- larger competence of local governments in allocation of housing allowances to tenants.

Here follow the main facts that influenced the positioning of countries in Figure 5.1. In Romania the rents were regulated by the state and allocation of vacant public dwellings was also limited by central criteria. In Slovakia and the Czech Republic rent regulation and tenant protection had been maintained although municipalities were free to allocate vacant or new dwellings. At the

Figure 5.1 Comparison of state housing policies



opposite end of the spectrum, in Estonia rent regulation was abolished at a state level and only half of the municipalities applied some kind of rent regulation on their territories. Estonian municipalities could also substantially shape housing allowances by setting expenditure ceilings. Though rents were controlled in Poland, the ceiling set in the Act was relatively high to allow municipalities higher rent deregulation, with rents reflecting a dwelling property value. The Polish municipalities were responsible for housing allowance payments. Slovakia applied only a partial right-to-buy policy.

There is one clear logical implication. The policy orientated towards the homeownership model, accompanied by low privatisation prices or even 'no-cost' sales (Estonia, Bulgaria, Romania), leads to rapid residualisation of public housing. This is connected to social segregation (only the lowest income households or pensioners do not use their right to purchase a dwelling) and a strengthening of tensions between tenants in public and private (restituted) housing sectors. The problem with tenants in restituted houses appeared in all countries belonging to the fast privatisers that offered very advantageous right-to-buy options to public housing tenants. This problem was gradually solved in Romania and Bulgaria by giving tenants priority in municipal housing allocations or in Estonia by allocating privatisation vouchers among them (see country profile details in Lux *et al.*, 2003). In the converse situation, tenants in restituted houses in Poland and the Czech Republic obtained neither preferential state subsidies nor any preference in vacant municipal housing allocation.

Theoretically, no privatisation approach can be evaluated as purely bad from the point of view of economic efficiency. Large-scale public housing privatisation (homeownership model) is the speediest way of dealing with the burden of socialist heritage, cutting public subsidies substantially and supporting the housing market (though it leads to tensions between different groups of society due to its very low effectiveness). On the other hand, policy orientated towards the rental model helps maintain a significant rental sector (possibly allowing higher labour mobility in the future), guards against social segregation and spatial residualisation and allows more substantial rent price deregulation. Existing public rental housing can be used to assist socially needy households with lower incomes in the future and this may produce substantial public savings (no need to subsidise needy households in other ways, e.g., support for new social housing construction or down-payment subsidies for housing purchase).

If I want to compare the countries according to the efficiency and effectiveness of their supply and demand-side housing subsidies in the field of housing consumption, I would need to specify the assumptions for such evaluation, as I did during the same evaluation made for the specifically Czech case. However, these assumptions need to take into account the limited possibility of getting any reliable statistical data in those countries for that time.

Let me thus assume *demand-side subsidies* as effective if:

- the housing allowance model does not use *notional* housing costs (tariffs) and instead includes actual costs and expenditure ceilings in the equation (capped by ceilings);
- the housing allowance model applies 'optimal' taper which has only a modest poverty/unemployment trap effect.

The effect of using notional instead of actual costs in housing allowance computation has already been discussed in the second chapter. Notional costs are generally set at a low level (level of rents in 'privileged' rental sector) and those households living in free market ('unprivileged') rental housing paying rents several times higher are thus excluded from any effective help. Moreover, the reliance of such models on income as the only criterion and not taking into account actual housing costs may lead to the situation when a substantial share of households with low actual housing expenditure-to-income ratio may also be eligible for a benefit (see the situation in the Czech Republic above). In other words, under such conditions the allowance helps those who do not need help and, in contrast, refuses effective help to those who need it. My assumption is not by far universal: if there were not two levels of rents for the same dwellings (market and regulated; market rents being several times higher than regulated) and if notional costs relating to one rent price level are set separately for each municipality (to catch regional deviations from average house and rent prices) the housing allowance with notional costs may al-

so be effective. High taper incorporated into housing allowance model is also not very effective as it may lead to a poverty/unemployment trap if beneficiaries prefer unemployment and benefit dependency as a better option than looking for a new job.

Let me assume *supply-side subsidies* as effective if:

- there is a clear definition of social housing in a particular country;
- subsidies are directly or indirectly targeted to households in social need;
- subsidies are more designed for rental housing than for homeownership;
- central 'old' non-targeted rent regulation rules are abolished or, at least, rent control power is transferred into the competence of municipalities.

Precise definition of policy goals (provision of social housing) certainly helps to enhance the effectiveness of potential subsidies (or, at least, to better its evaluation). Targeting new supply-side subsidies as well as allocating existing public flats with controlled rents among needy households (application of means testing) is a basic condition of any truly effective help. Moreover, only regular income inspections of beneficiaries can prevent the situation where higher income households profit from 'social' rents. If household income exceeds the ceiling set by the Act or the subsidy programme then landlords should have the right to make appropriate rent adjustments.

The preference of rental housing programmes to subsidisation of homeownership (via down payment subsidies) is justified because, from the point of view of effectiveness in the latter case, targeting is less strict (see the evaluation of subsidies to promote homeownership in the Czech Republic). This is a natural consequence of high house prices and a sharp decrease in financial affordability of owner-occupied housing in the region. It can be assumed that the majority of needy households in the selected transition countries would need to cover the substantial costs of house purchase through such a subsidy because they are not eligible for mortgage loans to cover the residual costs. Moreover, the down payment subsidies can be abused (speculative sales by future homeowners) even if forbidden by law; political representatives can be expected to abolish possible restrictions on house sales just because it is popular and/or such restrictions may be found as unconstitutional (breaching the right for free disposal connected with private ownership).

If allocation of new 'social' rented dwellings were really based on means testing and if regular income inspections were applied, then households noticing an increase in their incomes will be forced to move out of the sector and vacated flats will serve another needy household. This is, however, not possible in the case of down payment subsidies for house purchase or construction. On the other hand, in some environments subsidies directed to non-profit social housing may lead to stigmatisation and social segregation while promoting homeownership may contribute better to wider welfare goals (health, education) and prevent, at least partially, deepening social seg-

regation. As this discussion is closely concerned with the evaluation of the comparative benefits of demand and supply-side subsidies, on the general level it is far from over (despite current policy shifts to demand-side subsidies and possibly only temporary homeownership promotion). My assumption is related more to the particular situation in transition societies where housing affordability for needy households is perceived as a far more important issue than social segregation, a preference clearly proven by the survey of local government representatives conducted for the above-mentioned comparative project in selected transitional countries. Housing affordability is mentioned as the main target of local housing policies in all the selected transition countries. In contrast, social inclusion (social segregation prevention) is regarded as the least important or almost the least important local housing policy target in the same countries (see Lux *et al.*, 2003).

The criteria based on abolition or substantial change to the 'old' central rent regulation rules applied to existing rental housing (often both public and restituted private rental stock) is also crucial because such regulation benefits a substantial share of higher income households (Lux, 2001). The untargeted 'first generation' rent control not only distorts the housing market but it is also connected with considerable social injustice.

Let me assume *demand-side subsidies* as efficient if:

- the housing allowance model takes account of regional and area price differences when setting housing expenditure ceilings (notional costs, maximum notional costs);
- the housing allowance model applies a normative rate of burden that rises with housing costs and the income of an applicant;
- both municipal and state budgets co-finance housing allowance payments.

Regional differentiation in notional costs or notional maximum costs that are included in the allowance calculation may lead to public expenditure savings as there may be (and in reality are) huge house price differences between regions and cities in one country. If prices (or rents) are lower in some region, the ceiling may also be lower, and *vice versa*. The form of the normative rate of burden was discussed in Chapter 2. This criterion means, in other words, that households moving to a more expensive dwelling (better equipped and/or in a better location) are expected to meet a higher proportion of housing costs. Public spending can be lower than in a case when such a condition is not applied.

Co-financing of allowance payments decreases state expenditures by making municipal rent policies more careful and efficient. Municipalities partially responsible for paying the allowance due will increase the rents in their housing stock only if it does not lead to substantial increase in allowance payments. I assume that total public expenditures on housing allowances (inflation effect) may thus be lower than if municipalities are free to set the rents

and the state budget alone will cover the costs of rising rents.

Let me assume *supply-side subsidies* as efficient if:

- subsidies for rental housing construction are allocated more among private non-profit housing associations than among municipalities;
- subsidy programmes presuppose the participation of private capital; and
- subsidies are 'sustainable' in the long term (the state budget will have enough resources to cover the demand of applicants in the future).

Although municipalities may also be efficient developers of new social housing the general trend based mainly on the past experience both in EU countries as well as transition societies is to strengthen the role of private non-profit entities (housing associations, cooperatives) (Maclennan & More, 1997). Though unconfirmed by empirical research, one assumes that housing associations are more efficient in planning and housing management than public authorities, purely because they are responsible for their losses. This form of new social housing development allows for higher participation of private capital and further cuts in potential housing subsidies.

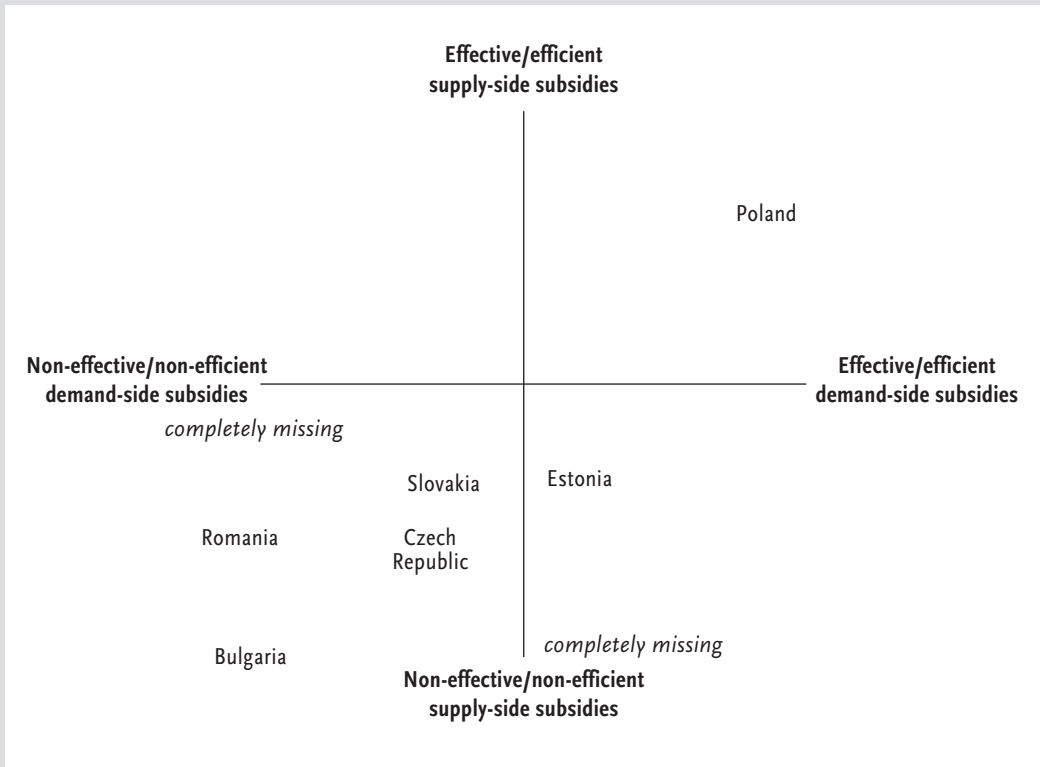
Though some programmes (mostly subsidies for young people) are targeted at people in housing need, they are often prepared in such a way that does not allow long-term sustainability (limited resources, too many applicants, long waiting period). These poorly designed programmes are more expressions of political populism rather than efficient housing policy instruments.

5.2 Evaluation and conclusions

To make the conclusions from this partial international comparison straightforward and really helpful to understand the particular situation in the Czech Republic I will evaluate the efficiency and effectiveness of subsidies together (i.e., assuming that both policy targets are closely connected). There are several possible trade-offs between the requirements of subsidy efficiency and subsidy effectiveness. One example can be private capital participation which is always assumed in the case of subsidies promoting the homeownership, but they are less present in subsidies for new social rental housing construction. In the instances of such trade-offs, in my evaluation the decisive influence would have been assigned to subsidy effectiveness, which is consistent with the subordination of efficiency to effectiveness in this book. The targeting of public support is the main purpose of public intervention; economic efficiency should only ensure that the costs of the intervention are as lowest as possible.

Figure 5.2 summarises the comparison of state housing policies in the field of housing consumption in the selected transition countries around the years 2000 and 2001. Based on the criteria outlined above, Poland was the only

Figure 5.2 Assessment of housing subsidies



country with a relatively high level of efficiency/effectiveness in both demand and supply-side subsidies. It had a legal definition of social housing, housing association legislation and subsidies were allocated mainly for new social rental housing construction among non-profit housing associations. A subsidy took the form of a qualified loan and covered only part of total construction costs (the remainder had to be covered from private resources). The allocation of social flats was subject to means-testing and associations made regular income inspections of beneficiaries (every two years). 'Old' rent regulation was slighter and the housing allowance model was counted with actual housing costs limited by indirectly set ceilings (reflecting the regional differentiation in rent prices), applied normative rate of burden increasing with income level and a gentle taper did not lead to the poverty trap. The total payment due was co-financed from both state and municipal budgets.

Similarly, the Estonian housing allowance (subsistence benefit) model did not use flat notional costs and maximum notional cost were set at a local level (reflected regional differentiation in housing costs), therefore it provided more effective help to those in need than the Czech or Slovakian models. However, the high taper and exclusive state financing disadvantaged the model in comparison with the Polish housing allowance model. On the one hand, Estonia had already abolished a central system of 'old' rent regulation and introduced a legal definition of social housing. On the other hand the Estonian government supported only purchase or construction of owner-occu-

ped housing regardless of the applicant's income and did not introduce any non-profit housing associations.

Romania and Slovakia introduced programmes for new 'social' rental housing construction (means testing is applied during the allocation of dwellings) but in that time neither country introduced non-profit housing associations nor abolished 'old' first-generation rent controls. The Slovakian model of housing allowance did not reflect regional price differentiation and programmes supporting purchase or construction of owner-occupied housing were not always sustainable in the long term (many applicants and long waiting period). At the time Romania had no significant demand-side subsidies and Bulgaria was the only country to not have implemented decisive supply or demand-side subsidies (with the exception of temporal energy allowance).

Surprising was the relative position of the Czech Republic. The Czech housing allowance model used only flat notional housing costs, taking no account of regional differentiation in prices/rents nor reflecting the higher level of market rents. Allowances were paid solely from the state budget. There was no legal definition of social housing, no legislation on housing associations and the 'old' system of untargeted central rent control had been maintained in both the public and private rental sector. Though the programme for new 'municipal' rental housing construction allowed for private capital participation, it often led to some kind of 'quasi-rental' tenure. As it did not include means testing the effectiveness of this subsidy was low. No other municipal social housing development programmes following the rules of Slovakian case were introduced at the time.

If we compare Figure 5.1 with Figure 5.2, we can draw relatively important conclusions. The most effective/efficient subsidies were implemented in the country where general policy orientated towards the rental model was accompanied by decentralisation in the rental housing sector (Poland). If we exclude Bulgaria and Romania from the comparison (as they miss some types of subsidy), the least effective/efficient subsidies appeared in the country where policy orientated towards the rental model was accompanied by a low level of decentralisation in the rental housing sector (the Czech Republic).

This is not just because higher decentralisation itself leads to higher efficiency/effectiveness of subsidies measured according to our criteria (co-financing of allowances, abolition of 'old' central state rent regulation). This may also be due to the fact that when the old inefficient practices are simply decentralised to the local level or indirectly abolished (e.g., through housing privatisation) the central administration has, very probably, stopped being attacked by various interest groups wanting to keep those practices alive. This might allow the central government to prepare new more efficient/effective subsidies with no need to look for any kind of hybrid solution between the relics of the past and new initiatives. Decentralisation may thus help central governments to clear the table and make a new start.

The comparison of housing conditions in particular countries uncovers another empirical implication. The relative housing sufficiency (Czech Republic, Slovakia, and Estonia) leads to lower effectiveness/efficiency of housing subsidies while relative housing insufficiency (Poland) leads to the opposite. The factor of housing need (housing shortage) may have some influence on the actual efficiency and effectiveness of state subsidies because a country in acute need of new housing cannot afford to experiment with hybrids of new and old practices. However, further empirical work on a bigger sample of transitional countries is needed to confirm such a conclusion. The general macro-economic situation is influential only if any policy instrument is introduced at all. Bulgaria and Romania, the poorest countries in our comparison, had only limited public and private sources to provide effective and efficient help to those needing support.

6 Efficiency and effectiveness of housing subsidies in the Czech Republic

Conclusions from housing system analysis

The final chapter of the book should especially answer the following research questions:

4. *What general conclusions can be drawn about the application of the role of 'understanding paternalist' by the Czech state between 1990 and 2005? What reasons for particular levels of effectiveness and related (subordinated) efficiency of state interventions in the field of housing consumption can be found from housing system evolution analysis? What influence did ideologies (norms), traditional problem solution patterns and institutional as well as political structures have on the development of specific state interventions in the field of housing consumption, and what effects did they have on the efficiency and effectiveness of these state interventions?*
5. *Do the main findings of the research conducted for this book show whether it is possible to increase efficiency and effectiveness of state intervention in the field of housing consumption in the Czech Republic? If so, what would be the policy recommendations?*

6.1 Context analysis

Several potential causes for the relatively low efficiency and effectiveness of housing subsidies in the field of housing consumption during the transition in the Czech Republic emerge from detailed descriptions of Czech housing system development:

- government instability (since 1996, mainly due to the proportional election system);
- the frequent presence of coalition governments with small politically weak and always centre-orientated Christian democrats (KDU-ČSL) often taking the post of the Minister for Regional Development (responsible for housing policy);
- the hard-line communists (KSČM) taking second place for a long time in parliamentary elections (till 1998);
- very high level of decentralisation of power and the increasing influence of mayors of smaller cities on central policies – mayoral lobbying could therefore direct central policies to satisfy their own 'immodest' interests;
- fragmentation of the responsibility for central housing policy among three ministries – Ministry for Regional Development, Ministry of Finance and Ministry of Labour and Social Affairs – and lack of any or, at least, efficient cooperation between them;
- 'populism' ('banking socialism', 'state capitalism') of the leading right-wing

party (ODS) in the first phase of transition preferring short-term achievements (safety nets, *ad hoc* reactions), over-employment and excessive wealth redistribution to long-term economic growth and modern social and housing policies (causing, probably, the economic recession in the second part of 1990s or the acceleration of high public budget deficits especially when the stream of privatised income dried up);

- general fear of political representation in the first phase of transition that to alter behaviour patterns common during the communism in this field might cause social disorder, breach social peace and endanger the transitional project;
- lengthy period (1998-2006) of government led by 'market-weak' social democrats (ČSSD) trying to establish (preserve) a strong welfare state and in the field of housing policy representing the interests of sitting tenants;
- the inherited institutional culture of clientelism and corruption that created excellent conditions for social networking and the increasing power of lobby groups (all clearly evident during enterprise privatisation), that is the factors opposing to higher transparency in government spending (no questioning of the efficiency and effectiveness of policies, nor measurement, analysis, or monitoring);
- traditional social norms of Czech society (egalitarianism, 'think left, vote right') coming from traditional animosities to the nobility and Catholic Church;
- the inherited normative expectations of Czechs to receive free 'gifts' from the 'omnipotent' state, especially when it concerned the housing;
- the inherited focus of public policymakers and politicians on extensive housing indicators (e.g., how much new housing has been built with no attention paid to where and to whom it was allocated) and only very slow recognition of the need to define new types of policy assessment means;
- traditionally much attention paid to the 'social question', social policy, solidarity (again a clearly apparent social norm since 1918);
- due to the large shadow economy, means testing became highly unreliable – any kind of targeting of subsidies (increasing the potential effectiveness of subsidies) would miss its goal;
- relatively good housing conditions supported by a low number of foreign immigrants;
- the objective effort of politicians to support the highly taxed middle class that received only little from the otherwise generous social support system;
- the objective effort of politicians to liberalize energy prices first (gas, oil, electricity) and increased utility costs then remained only few room for further increase in housing expenditures (e.g., through growth in rents).

Another twofold reason might be found first in the intransigent unwilling-

ness of political representatives to alter views and behaviour patterns in this sphere (despite similar action taken in other areas) that had been carried over from the era of the previous regime, and secondly in the effort to maintain a false image of housing as such a unique and 'non-marketable' good that reform in this area could lead to political instability and the disruption of the entire transformation process. Housing might be intended, and not only in the Czech Republic, to absorb the shock coming from other reforms and compensate for the loss resulting from liberalisation in other sectors of the economy. The security of having 'a roof over one's head' was meant to bridge the discomfort from the loss of other social securities.

The main question is: despite the negative social effects of prevailing rent regulation leading to the creation of artificial social inequalities and social tension, why was (and still is) system reform confronted with so much political obstruction? One answer is the high level of other household expenses, a problem I mentioned above. This problem could be solved by means of an housing allowance to needy households, which estimates (Lux *et al.*, 2003) indicate would be eight times less costly to the state budget than public support for a housing savings scheme and after calculating the increased rental income to municipalities from higher rents it would ultimately have a positive effect on total public budgets. However, the main reason is likely to be outside of purely rational financial analysis.

To generally determine which factors may lie behind the limited efficiency and effectiveness of subsidies in housing policy, I conducted interviews with two former ministers who had been responsible for housing policy and one interview with high-ranking public official, all of the same ministry (Ministry for Regional Development). An enormous amount of empirical data would be required to perform a real structural analysis of the significance of individual factors (moreover for multiple countries, in order to allow for a comparison of the effect of structural factors), but such data are not available (or would be very difficult to obtain), and therefore there is no other option but to partially determine the significance of these factors indirectly instead, that is, from the opinions of those people who prepared and implemented housing policy during the economic transition. Selected statements of the respondents are presented below in italics.

The respondents most often referred to factors concerned with the political system's immaturity, lack of qualified political representatives, the unwillingness of political representatives to elaborate on long-term concepts, their mistrust of research and of recommendations from ministry officials, and the strong influence of the personal opinions of the country's former premier for many years, Mr. Vaclav Klaus.

"..the life of society was dominated by politicking and not politics. If the life of society had been dominated by politics, then politics would have had to communicate with

science...that isn't done, because it's politicking that's going on, and it is uneducated people who are engaging in that politicking, fools who just happened to get into politics, where no educated person wants to be..."

"The political situation was such that the left ended up without any qualified people. The qualified people were subject to intimidation, the qualified people were excluded from society by anti-communism."

"They were politicking, the right and the left. The left didn't understand enough, it had no concept..."

"I'll tell you that even in housing Klaus was an enemy of concepts. And any concept, surely, should be preceded by some kind of analysis. So perhaps that could be a reason. The housing policy concept was passed by the government, in a curtailed form, only because Klaus wasn't present in the government at the time."

"Klaus just cast a shadow on rent deregulation. In the government he really did say that if they were going to talk about deregulation then only without him, he really used his mother as an argument...And the landlords didn't make too much noise, until 1998 ... when the initiated process was halted when it was only halfway done."

"Why didn't they look to Austria?... The left didn't pick up on the Austrian experience because the political conditions didn't exist for. .. there was no political force here to reach an agreement."

In response to the question of whether some kind of test of the targeting and financial costs was carried out before the introduction of the housing savings scheme: "I don't know, I wasn't in top politics at that time, it's but not very likely. I think maybe that it was actually an MP bill. Even though it was obviously prepared by the Ministry of Finance, but I don't know. I wasn't that interested in it, so I can't tell you. I know more about the time when I was in or around the government, then it was simply a battle. ... But about anything else, about testing, say, there was no discussion."

It is necessary to add that the research sphere in this area was also weak and largely influenced by ideological clichés inherited from the previous regime. Respondents relatively often referred to the fact that the transformation process was under way during a time when everything was done by trial and error. Naturally, this case is no different in other transition countries and therefore this factor can hardly explain the specific position of the Czech Republic within the cluster of transition countries.

"I wanted to say that many things were done chaotically, there's no question about

that. Someone would just come along with this fantastic idea and it was put into play without the requisite analyses.”

“As for efficiency, everyone was learning about all that as they went along... It couldn't be solved in a year or two. That was the price of transformation ... So, everything basically proceeded along by trial and error. What was worse were those populist proclamations, like, we will give loans to young people ... and then also the inexperience of those politicians.... I'll just think this up, and there were x number of those. Also, the distrust of public servants and of people who write about these things.”

Paradoxically, the extensive decentralisation of power also played a role to an extent unparalleled in any other transition country. Because more than 6,000 municipalities with elected political representation were established in the Czech Republic (for a population of ten million), a substantial portion of top political representatives began to be recruited from or at least influenced by people from the ranks of municipal mayors, who in top politics were mistrustful of independent analyses in the field of research and who also tended to assert the interests of the municipalities rather than the general principles of how a social system should operate.

“It is usually political factors, but in the entire spectrum of politics because the municipalities got rental flats from the state, then they built new ones. Housing policy was always executed at the local level....this created the strong influence of the mayors.”

In response to the question of why the respondent, supposedly operating at the level of the municipality, supported the untargeted privatisation of flats sold to tenants at less than half their market value while doing nothing for those without housing who had to pay high market rents: “Well, the question is whether the municipality was able to make that distinction... I understand what you're getting at, of course, why should the well-off receive further support like this, but it's probably not realistic, because that's decided by the municipal council. The majority decides, and that includes poor, rich, middle ranks, the poor are maybe there, but maybe they don't get involved.... At that time a state administration periodical, or one of the local authorities published a recommendation saying that the number of flats remaining in the ownership of the municipality should be around 10-15% of the total number of flats in that municipality's territory. But then ODS came along and that was that. Everything was swept out, even ideas like that, because a council isn't required to adhere to what their predecessors set up. That is not thought through, it will come back to haunt the municipality. Well, I still believe that, it's the reality of politics at the local level. So I don't know how to answer that for you.”

Also cited were factors relating to the political structure, especially in the case of governments formed by the left:

*"I think that the main reason on the side of the Social Democrats is that **** (influential Social Democrat deputy) convinced them that they won the elections thanks to voters in regulated flats...he managed to do that, so they were afraid to change anything."*

The absence of any qualified policy was compensated for by well-prepared lobbying that was very effective in transition countries:

*"How housing savings was set up, for example, well, there were consultations with Germans and Austrians, where building savings operates perfectly, but today that's obviously also the past, but it was something at a certain stage. *** picked that up, and really insisted on it, who he got it from I don't know, I'd have remembered a name...so they always picked on these fragments without any theoretical foundation."*

"At the time we had a survey available, I don't even know who did it, it was just a survey, which revealed that only 5% of the people who complete their housing savings use the funds for a purpose other than housing. Perhaps not as strictly as defined by law, that it goes on furnishing one's flat, but definitely not on buying cars." (The results of this survey, which can no longer be traced, contrast with the results of the Housing Attitudes 2001 survey carried out on a national sample of respondents by the Institute of Sociology AS CR; however, it is not known who conducted the survey).

"Corruption in the creation of those programmes, legislation, I don't think so.... Housing saving banks, in my view, know how to lobby well... so even an initially relatively bold proposal for a system amendment was considerably toned down in Parliament, because the savings banks simply know how to approach politicians.... I think that the lobbying was strong but still fair."

*"These MPs are strongly manipulated by local politicians... so they convinced them, that's the way to go (untargeted programme for the construction of quasi-ownership 'municipal' housing operating between 1995 and 2002). The mayors didn't want to deal with the poor...****, mayors and building companies, and **** always wanted to oblige the mayors, so the mayors loved it, the building firms loved it too, everyone wanted it...."*

In response to whether lobbying had a direct effect: *"Of course it does. But that has to do with the fact that the neoliberal concept lacks any social context, lacks any analysis of the social consequences. I mean, it's terrible who they give state support funds to..."*

“Certainly there were far more tenants with regulated rent, the pressure in that direction was much stronger, and it was the transition period, which means, I remember, say, when we increased rents, my drivers at the ministry cursed me, even as a minister.”

An interesting question is why rent deregulation was such a thorn in the side of many politicians on both right and left, while relatively substantial increases in the costs of energy, increases often introduced by enterprises in which the state had a substantial ownership share, were usually approved without difficulty.

“I think that it was because, first of all, these firms that supply energy had a more powerful lobby. Some, like the energy company, were still in the hands of the state and clearly the fact that rent increases were always made on July 1 played a role here. It seems strange, but I think it was because the state budget was passed in November, December, when they determined the estimated inflation including energy prices; there was agreement on the level of the increase in energy costs. And rent always came along later on having missed the boat, there was no room left for it. This is my layman’s view, but I think that’s it. So a role was played by politics and company lobbying. The private landlords never had that kind of lobby, nor did the tenants even, definitely that union of landlords at the time, or whatever they were called, the association of landlords, was not operating yet they way it did in later years. The fact that rents were frozen, that there were no increases at all, I think that was a fatal error.”

More than a few times the argument was raised about people’s expectations, inherited behavioural patterns, and consensual politics. The main parameter of housing policy success under the previous regime was the scope of housing construction, the number of newly built flats. This ‘performance indicator’ was also adopted in the transition-era housing policy – it was not important for whom housing was being built, the quality of housing construction, or whether public subsidies might have some negative effects on the functioning of the market; what was important was the scope of housing construction.

“It’s politics, so there’s a certain feeling here in society, and it’s not, at least that’s the way we saw it, it’s just not possible to cut things off so easily. Especially when the premier just couldn’t accept it and labelled us as deregulators.”

“Capitalism yes, but with a human face, the socialist kind....”

“The aim generally was to activate housing construction itself. No one was building. So it was just to get some construction going, generally just to shake up the market....At least that’s how politicians saw it.”

In response to the direct question of whether the respondent agreed that a certain role could have been played by the fact that housing conditions in the Czech Republic were relatively good and essentially ‘everyone had a place to live’, one respondent agreed but the remaining two respondents rejected this factor, as they were convinced of the existence of a housing shortage. In one interview the argument arose that there was enough public financial resources compared to other transition countries.

“When there was little money, then they thought more about where it went. Here billions were flowing all the time, so no one was really interested in where; there was always enough to hand out. The curves were going up, right? The main emphasis was on expanding housing construction, whatever it takes, that kind of nominal, social engineering view, that more and more is being built, but that involves how much it costs, how it’s inappropriately set, how it’s actually acting as an inhibitor...no one was much interested in that.”

As expected, what often surfaced in these interviews were evasive responses, excuses, or even a refusal to respond to direct questions about inefficiency.

“I’ll tell you, I really don’t know how to answer that for you, I don’t know and I don’t want to speculate.”

“I must admit, I wasn’t that high up in top politics that I’d have been able to do that.”

“How am I supposed to answer to you for Klaus?”

“That’s true. We didn’t work that out, there was too little time.”

“I can’t judge that, I must admit I’m a bit one-sided in that area. I always used to look at housing savings – at that time and with that concept and so forth – as an instrument of housing policy, that’s true. And I can’t really compare it with anything.”

“I was vehemently opposing (the privatisation of municipal flats), I took a stand against it in the government, but I soon figured out that I was talking to myself. Because it was good for the Ministry of Finance, it was able to rid itself of the pressure from the municipalities looking for subsidies from the state budget.”

“..and even now I still say, my God, were you or weren’t you the minister?”

There are two types of factors that may lie behind the low level of efficiency and effectiveness of housing policy: *explicit factors* (expressed by the actors themselves) and *implicit factors* (structural, latent). Explicit factors include mainly the lack of sufficient qualifications on the part of political representa-

tives and their 'politicking'; the distrust politicians felt towards the research sphere and towards recommendations from ministry officials; on the political right an unwillingness to accept long-term concepts, and on the political left an inability to come up with a conceptual solution; the strong influence of municipal mayors on central housing policy; the need to find solutions quickly without the opportunity to test them; and the relatively strong lobbying engaged in by interest groups.

Also cited among explicit factors was the need to take into account the attitudes and expectations of Czech citizens, who simply could not be 'cut off' from previous experiences and behavioural patterns; this is consistent with the way in which the transition to democracy is understood as a transformation or reconstitution of old institutional conditions in a new environment, but also its relatively strong influence in the Czech environment falls within the framework of 'consensual politics' (to a certain extent populism) practised by the first Czech transition governments of right-wing parties.

By way of illustration, according to the survey *Housing Attitudes 2001* carried out on a national sample of the adult population, a full 44% of the respondents who answered the question still believed in 2001 that the state should regulate the housing market more than it had been to that time, and over 36% were inclined to agree that the state should regulate the housing market as much as it had been to that time – 62% of respondents believed that the state should regulate the price of building materials; 57% of respondents believed that the state should regulate the price of flats and houses for sale; 78% of respondents felt that it should regulate the rent levels and 87% of respondents the costs of energy connected with housing. It is clear that regulation in connection with the housing market, however ineffective it may have been, enjoyed the wide support of the public. These opinions changed over time as the ineffectiveness of regulations became more apparent (see, for example, the results of the survey by the Public Opinion Research Centre (CVVM) in 2006 at www.soc.cas.cz/seb), but the change was more gradual and over the long term.

Things were no different with respect to the housing savings scheme – regardless of the fact that higher-income households received the largest public benefits, in the CVVM survey on a national sample of roughly 1,000 adults conducted in 2006, 83% of respondents felt that the housing savings scheme was a very or rather effective instrument for solving housing problems (housing savings were evaluated best out of all the state's housing policy instruments assessed in this survey); conversely, respondents evaluated the targeted housing allowance as the least effective.

The targeting of public housing subsidies to those who need it and the efficiency of such support were not demanded by the public, were not monitored or questioned in the media, were not the subject of political debate and essentially did not come up at all in public discourse. It was automatically expected

that expenditures in housing policy would be ineffective and have character of universal eligibility. Housing savings scheme was popular because it allowed people to obtain support from the state simply on the basis of a household creating savings; rarely did anyone question whether the state should use tax revenue to support people's savings, but the majority of middle class members were probably glad that they are getting something from the state back. Housing policy was not viewed as being part of social policy but rather as something separate from it, which cannot target just the needy; perhaps because the problem of housing affordability is common to everyone (housing is unaffordable even for the substantial middle-income category of the population), because the allocation of flats was universal and free until not too long ago, and because everyone had been entitled to some state assistance at the time. The concept of housing policy extensively focusing on the scope of housing construction was similarly adopted: what was important is the number of newly built flats. It did not matter where they were built, for whom, at what level of quality, how they were allocated and whether any public support could have a negative impact on the market or social inequality.

The case is the same with rent regulation and the privatisation of flats – a survey like *Housing Attitudes 2001* demonstrates that there is, for example, a large group of people who disagreed with the privatisation of municipal flats (usually tenants living in private rental flats or people oriented towards the political left), but who, on the other hand, vehemently supported rent regulation; equally there was a large group of people who disagreed with rent regulation (usually the homeowners and people oriented towards the political right), who vehemently supported the privatisation of municipal flats. 'Regulation' is a term of the political left, while 'privatisation' is a term of the political right, and no one dug further into the fact that the result is essentially the same untargeted economic subsidy for current inhabitants of municipal flats, which divides the market into 'privileged' and 'unprivileged' housing. The ideological clash between the 'ideal' right (neoliberalism) and the 'ideal' left (a generous welfare state), which, however, has often gone no further than just a clash of narratives, has so exhausted the political and public discourse that there has been little space left for criticising public expenditures within housing policy in terms of effectiveness and efficiency (both of which lie outside ideology). The interviews demonstrated that the perspective (evaluation) of efficiency and effectiveness of public subsidies was never considered, was never a topic of discussion, and for many (including former members of the government) it was an entirely new idea, even partly incomprehensible.

The question is why this perspective never entered into public or political discourse, why it remained outside the area of housing policy? Part of the reason may be that in the search for 'ideological purity' on both sides of the political spectrum and the rhetorical conflict there was little room left for it, but the answer is also clearly connected with another group of factors that

are implicit, unexpressed, and latent. Is the reason the fact that there was no acute housing shortage in the Czech Republic, even though respondents tended to reject this factor? Or is what lies behind the unstable governments the persistence of an unreformed form of communism, the culture of clientelism and corruption? It is very difficult to answer these questions; probably each suggested reason had a certain amount of influence, and only in combination did they lead to the given outcome. The factor of the relatively strong political representation of the unreformed Communist Party in Parliament certainly ranks among the weaker factors (given the successful effort to cut the Communists off from any real political influence), while conversely the stronger factors, though this claim remains on a hypothetical level, are likely to include clientelism in the transformation culture and the strong influence of lobbying filling in for the absence of any independent research, or the retention of inherited behavioural patterns, 'consensual politics', unaltered expectations relating to universal state assistance in the area of housing and an emphasis on extensive indicators of housing policy success (the scope of housing construction).



6.2 Policy recommendations

The theoretical imperative behind public intervention in the area of housing consumption should be the creation of a rational mix of supply and demand-side subsidies that reacts as flexibly as possible to changes in the housing market and economy in general. Other imperatives should be efficiency and effectiveness (horizontal and vertical effectiveness) of subsidies (with the knowledge that fulfilling both these imperatives at the same time is often impossible), neutrality in the allocation of public support in relation to various housing tenures (owner-occupied or rental housing), the transparency of rules on subsidy distribution and especially the ability to monitor adherence to such rules, sustainability (support should satisfy the needs of all those who are eligible for it and thus should not create waiting lists or result in a shortage of finance, etc.) and equality among the mediators in the subsidy distribution (in the sense that all potential 'mediators' in the allocation of support, in particular the private and public institutions, should be treated in equal standing).

The Czech housing policy was far unequivocally skewed in favour of owner-occupied housing (which violates the neutrality imperative) and in favour of demand-side subsidies (which may violate the imperative of rational mix of demand and supply-side subsidies, though deeper analyses would be required to draw such a conclusion). The explicit priority of the policy to support demand was balanced by large economic subsidies that by their latent nature are forms of supply-side subsidies (in both rental and in the owner-

Table 6.1 An evaluation of selected housing subsidies in the Czech Republic, 2007

Programme	Efficiency	Vertical effectiveness	Horizontal effectiveness
Rental housing			
Supply-side subsidies			
Support for construction of municipal rental housing to end of 2002	Low <i>EST</i>	Low <i>EST</i>	Low <i>EST</i>
Economic subsidy in the form of rent regulation	Low	Low	Low
Support for construction of municipal rental flats since begin 2003	Middle <i>EST</i>	Middle/High <i>EST</i>	Middle/High <i>EST</i>
Support for construction of supported housing	Middle/High <i>EST</i>	High <i>EST</i>	High <i>EST</i>
Support for construction of rental housing as an investment incentive	Low <i>EST</i>	Low <i>EST</i>	Middle <i>EST</i>
Demand-side subsidies			
Housing allowance valid to end of 2006	Low – High	High	Middle
Housing allowance valid since begin 2007	Middle/High	High	Middle
Owner-occupied housing			
Premium on building savings	Low/Middle <i>EST</i>	Middle/Low <i>EST</i>	Middle <i>EST</i>
Interest subsidy	Low – High <i>EST</i>	Low <i>EST</i>	Low <i>EST</i>
Tax subsidy	Low – High <i>EST</i>	Low	Low
Qualified state loans for young first-time buyers	Low – Middle <i>EST</i>	Middle <i>EST</i>	Middle <i>EST</i>
Economic subsidy from privatisation of municipal flats	Low/Middle <i>EST</i>	Low <i>EST</i>	Low <i>EST</i>
Support for modernisation of prefab buildings (the PANEL programme)	Middle/High <i>EST</i>	Low/Middle <i>EST</i>	Low <i>EST</i>

Note: *EST* = estimate;  = programmes with the best evaluation;  = programmes with the worst evaluation.

occupied housing sectors); however these forms of support are temporary and will soon come to an end. Czech housing policy is in violation of the imperative of transparency owing to the high, though latent and often overlooked economic subsidies, the division of responsibility for housing policy among three ministries, and especially the absence of any evaluation or monitoring of subsidy distribution. The majority of programmes, however, are sustainable from the perspective that eligible applicants do obtain the support they are entitled to within a reasonable period of time.

Table 6.1 presents a summary of evaluations of how well specific instruments of housing policy in the field of housing consumption applied in the Czech Republic meet the selected theoretical imperatives for how housing policy should operate. This is not an exhaustive list. The evaluation is very

Flexibility, simplicity infrastructure	Transparency	Equality of mediators	Sustainability
Middle	Low	Low	Low/Middle
Low	Low	-	Low
Middle	Low	Low	High
Middle	Low/Middle	Low	High
Middle	Low	Low	Low/Middle
High	High	-	Middle
High	High	-	n.a.
Low	Low	Low	Low/Middle
Middle	Low	Middle	Low/Middle
Middle	Low	-	Middle/Low
High	Low	-	Middle/Low
Low	Low	-	Low
Middle/Low	Low	Low	Middle

general and in many cases, owing to the absence of information, is based on logical estimates or secondary information (data). The programmes evaluated best are marked in medium grey, and the programmes evaluated worst are in dark grey. On the basis of this evaluation, the best include the programme for the construction of supported housing and the housing allowance; to some extent also the programme for the construction of municipal rental flats for limited-income households (based on conditions valid since 2003) and preferential loans for young first-time buyers. The worst evaluated forms of public support include economic subsidies in the area of rental and owner-occupied housing (rent regulation and the privatisation of flats) and support for the construction of municipal rental flats based on conditions valid up to the end of 2002; to some extent as well support for the construction of rental housing

as part of foreign investment incentives, the state premium on building savings, the interest subsidy and tax subsidy.

If the programmes have something in common, then it is their relative lack of transparency deriving mainly from the inability to execute any simple subsequent monitoring/audit of subsidy use (with the one exception of housing allowance); also, the equality of 'mediators' in the allocation of subsidies is violated in many respects given that support can only be distributed among some actors (municipalities in the case of support for the construction of rental flats; specialised banks in the case of the state premium on housing savings; and owners of prefab flats in the case of support targeting the modernisation of the housing stock).

In the case of public support of any kind, most important is its effectiveness, that is whether the support is directed at those who really need it; efficiency is merely a 'safety catch', indicating whether these people could be helped by less costly means. Effectiveness is evaluated both vertically and horizontally. Support for the construction of municipal rental flats in the form valid to the end of 2002 has a limited degree of vertical and horizontal effectiveness (owing to the absence of targeting and to specific abuses detected later), as does rent regulation and the large amount of untargeted subsidies for owner-occupied housing: the interest subsidy, the tax subsidy, the economic subsidy derived from the privatisation of municipal flats, and to some extent also the support for the modernisation of prefab buildings. In all these cases it has either been demonstrated or it can be expected that subsidies are regressive in nature, that support is not income or otherwise targeted.

A high degree of vertical effectiveness is evident only in some forms of support for rental housing, particularly housing allowance, but also in the case of construction of municipal supported housing; and to some extent also for the construction of municipal rental flats for limited-income households (based on the conditions valid since the start of 2003). Among the programmes directed at owner-occupied housing an acceptable degree of effectiveness is observed only in the case of favourable state loans to young first-time buyers and to some extent also in the case of the state premium on housing savings (given its limited maximum and, based on secondary data, that it is not as regressive as, for example, tax subsidy).

A simple infrastructure and the flexibility of instruments were evaluated not only with respect to the established rules, but also to the need to construct a more complex infrastructure for the allocation of support, to the future possibility of changing both rules and the infrastructure, as well as to the assumed or real opportunities for potential mediators or ultimate recipients of this support to effectively lobby for given conditions to be retained even when the conditions need to be changed. The majority of public forms of support, with the exclusion of economic subsidies, attain a middling or high degree of flexibility, while those evaluated highest were the housing allowance

and favourable state loans. Payment of the housing allowance responds flexibly to the current economic situation (even though the notional housing costs need to be amended) and as in the case of state loans one can expect that the effect of lobbying will not be so strong as to threaten any change in the terms attached to it. The theoretical possibility of changing conditions is somewhat lower in the case of support directed at the construction of municipal rental flats, because municipalities can act together to exert strong pressure (as has been demonstrated by interviews); in the case of interest subsidies and tax subsidy, where a strong pressure group can be formed by large financial groups (however the amount of the tax subsidy is also determined by the income tax rate, and here the influence and interests of financial groups are more complex); and in the case of the programme of support for the modernisation of prefab buildings, where housing cooperatives in particular represent this kind of pressure group (their influence is evident especially under the governments of political left). The state premium on housing savings is characterised by a very low degree of flexibility and a very rigid infrastructure; it is very difficult to carry out any change in this area and lobbying is thus very effective.

From the perspective of sustainability (the relative sufficiency of financial resources even in the long term for the ultimate recipients of support) the forms of support evaluated best were the subsidies for construction of supported housing and municipal rental housing based on the conditions valid since the start of 2003; conversely, those evaluated the worst were both economic subsidies and to some extent also support for the construction of municipal rental flats based on the conditions valid to the end of 2002; support for the construction of rental flats as part of foreign investment incentives, the interest subsidy; and the state premium on housing savings. Subsidies in the area of owner-occupied housing, in particular the interest subsidy, but also the premium on housing savings, tax subsidy, favourable loans, and support for the modernisation of prefab buildings have the potential to become a heavy burden on the state budget.

Support for the construction of municipal rental flats based on the original conditions (valid until the end of 2002) and the interest subsidy have been already cancelled or halted. A new form of support for the construction of municipal flats, valid since 2003, is already income or otherwise targeted, and is directed at an area in which the private rental sector usually expresses little interest (and therefore private investment has not been crowded out).

In 2006 we saw preparations for a new Deregulation Act which was passed by Parliament at the beginning of 2007. This act aims to gradually deregulate regulated rents up to the end of 2010. It should end the inherited 'first generation' rent control system and subsequent untargeted economic subsidies. The same applies for economic subsidies in the field of privatization of public housing. Due to rent deregulation the municipalities began thinking about

ending privatisation of their housing (or continuing privatisation, but under market conditions).

Support for the construction of rental flats as a foreign investment incentive, the premium on housing savings, and tax subsidy were evaluated the worst instruments of Czech housing policy still existing in 2008, which need significant reforms of the terms by which they are applied. Owing to shortcomings from the perspective of horizontal effectiveness, the current housing allowance also requires partial changes to its terms. This reform could take the following form:

- The state premium on housing savings should be reduced and income-targeted (only households under a certain income limit should be entitled to it); it should be automatically tied to interest rate changes, so that the amount of the premium responds flexibly to macro-economic changes, or it should be made possible for the government to decide on its amount.
- Subsidies for the construction of flats as part of foreign investment incentives should be abolished; this is also evident from the results of a study by Lux *et al.* (2007, 2007a).
- Tax subsidy should be abolished or strongly limited given that it significantly strengthens tax inconsistency, affects the tenure neutrality and is highly regressive. There are numerous examples of such restrictions: these can be applied through the notional tax rate used for the purpose of relief, through a reduction of the maximum amount of deductible interest, and through time limits within which this support can be taken advantage of (e.g., it would only apply for the first several years following the purchase of dwelling).
- The part of housing allowance that relates to the notional housing expenditures should take into account the existence of 'unprivileged' market rental housing. There should be reductions in the level of allowances provided among homeowners in order to avoid unnecessary wastage.

The exclusive orientation of Czech housing policy towards owner-occupied housing needs to be changed, and this should be done with the creation of other targeted programmes and subsidies in the area of rental housing. Given that housing policy is currently explicitly focused on demand-side subsidies, a strengthening of public support for rental housing on the supply side is one particular option. This kind of support can, for example, take the form of simply creating a legislative framework and effective grant system for non-profit rental housing, the shortage of which will become fully evident in coming years. Another form could be the creation of the kind of motivational incentives that would lead municipalities towards more responsible policy in managing their housing stock and towards finding effective solutions to social problems – the creation of a segment of social flats located in various buildings owned by the municipality or in buildings containing already privatised

housing units, in order to prevent social segregation. It is also necessary to reduce the fragmentation of housing policy among different ministries. Initiating a serious discussion on the scope and consequences of latent economic subsidies (and a discussion of the future, after these are gradually eliminated) and especially strengthening neutrality and transparency with subsequent monitoring of efficiency and effectiveness of subsidies appear to be the main challenges that Czech housing policy is now faced with.

7 Summary and conclusions

7.1 Main topic and goals

The book focuses on a description of the unique process of housing system establishment (reform) that formed a part of the general economic transition towards market economy in the Czech Republic. As the process of an establishment (reform) of the housing system itself is very complex, it was necessary to narrow the topic to some particular facts. The transition has been understood as the process of building a new social environment, new policies and new institutions. Such a process is highly regulated and shaped by the leading political power, representatives of the state. The strong role of the state is one of the prerequisites of transition even though its ultimate aim might be to substantially decrease the power of the state. During transition the ideological myths of the past are abandoned and empty 'interpretation' space has to be filled. In highly centralised post-socialist societies, representatives of the state played the decisive role in such a process. Thus the behaviour (actions, interventions) of the state in the field of housing formed the main research focus of this book; sometimes this type of analysis is labelled state-centered analysis or policy analysis.

The activities of the state in the field of housing, however, vary largely as there are many fields in which the state may intervene. Both governments and citizens in transition societies pay special attention to the 'housing-needs problem' or 'housing affordability problem'. Due to the fact that worsening housing affordability could endanger public support for the whole transition project, the housing affordability became the most recurrent housing issue and policy target during the transition. Though again a complex issue, housing affordability is especially connected with the level and quality of housing consumption and therefore the state interventions directed to influence housing consumption (explicit or implicit subsidies to hold or increase housing affordability) were chosen as the focus of my book.

The goal was to describe, evaluate and analyse state housing policy in the field of housing consumption between 1990 and 2005 in the Czech Republic. For this purpose I made:

- a description and evaluation of housing policy in the field of housing consumption in the Czech Republic between 1990-2005; basing the evaluation on policy outcomes (performance) and placing it in a comparative context; and
 - an analysis of possible causes of particular Czech transitional housing policy in the field of housing consumption (derived both through international comparison of relevant factors as well as an analysis of societal norms, ideologies and institutions peculiar to the Czech Republic).
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7.2 Theoretical and methodological background

In the theoretical introduction I noted that state housing policies in the field of housing consumption are theoretically led by the effort to eliminate market failures and ensure that the housing market functions more efficiently, and by the effort to redistribute housing consumption or, to put it more precisely, to ensure that standard (healthy) housing is affordable to all groups of society. This double role of the state has been defined as the state acting both as a rational economist and an understanding paternalist. The role of rational economist derives in particular from the definition of the economic optimum developed by Vilfredo Pareto. According to it, the market finds itself in an optimum if there is no other possible allocation of goods that could increase the utility of one of the participants without decreasing the utility of the others. The state thus functions as the guarantor of market efficiency and the optimal allocation of goods. The state enters the housing market also as an understanding paternalist, with certain (divergent) concepts of a welfare state. It is clear that the scope and type of public interventions depend largely upon which type of welfare concept a particular administration favours.

The dual role of the 'ideal' state can be practically written into the policies directed towards the (economic) efficiency of housing-market functioning on the one hand, and towards the (social) effectiveness (equity) in distribution of housing services on the other; both thus simultaneously include allocative efficiency and income distribution. I wrote that common trade-off situations arise between efficiency and effectiveness; redistributive interventions, though very effective, may distort efficient housing market functioning, that is being at the same time inefficient.

Effectiveness (equity) is closely associated with the idea of equity, social justice, and the welfare state; it relates to 'fair' income distribution. As such, it is closely connected with a particular (unique) welfare state regime, particular social norms, and particular traditions. However, this concept has been, at least partially, generalised into the assumption that whatever state redistribution of wealth is finally applied, it should reduce social inequality in society, that is the redistribution policies should help those worse off on the costs of those better off. Welfare economics distinguishes between vertical and horizontal effectiveness. Vertical effectiveness measures the degree of redistribution of income, consumption and wealth from the rich to the poor. For a particular housing subsidy it measures the extent to which the subsidy is actually allocated to those who really need help, that is to low-income households, and in this way reduces social and income inequalities in society. Horizontal effectiveness is connected especially with the idea that all needy (poor) households have equal and unrestricted access to public subsidies. For

a particular housing subsidy it measures whether there is any needy (poor) household that is explicitly or implicitly excluded from the possibility to apply for the subsidy.

The theoretical concept of effectiveness has been fully applied in this book; including the evaluation of both vertical and horizontal effectiveness. However, the concept of efficiency is much broader. It relates also to the state interventions connected with the general functioning of the housing market and not specifically in the field of housing consumption. Therefore I narrowed my analysis to solely the efficiency of those state interventions that have direct influence on housing consumption. In this way I related the concept of efficiency to the concept of effectiveness and, from some perspective, I subordinated the concept of efficiency to the concept of effectiveness.

The main assumptions used to evaluate effectiveness and efficiency of housing subsidies were as follows:

Main assumption 1: Effective subsidies assist lower-income (needy) households more than higher-income (less needy) households. (Vertical effectiveness)

Main assumption 2: Effective subsidies do not exclude any lower-income (needy) household. (Horizontal effectiveness)

Main assumption 3: Subsidies are efficient when it is not possible to meet the redistributive goals in the field of housing consumption in a less costly way, that is, under an alternative setting of the subsidy or an alternative setting of the whole set of subsidies.

These assumptions were used to measure the effectiveness and efficiency of selected transition housing subsidies in the Czech Republic; various data sources, econometric simulations (especially in the case of 'hidden' economic subsidies) and sets of statistical measures of inequality were employed for this purpose. Besides the detailed evaluation of subsidies in the national context, a similar methodological device though somewhat restricted in its assumptions was also used to measure and compare the efficiency and effectiveness of selected housing subsidies in five other Central and Eastern European countries. This international comparison respected the imperative of 'individual openness' during comparative research; the lack of it is mentioned here as the main reason behind misunderstanding in some comparative studies.

The second important orientation of the book was to find the answer to the question of what were the main factors influencing the particular efficiency and effectiveness of housing subsidies in the Czech Republic? The first goal of the book lay thus in the evaluation of housing subsidies and the second one in the explanation of the evaluation results. To meet the second goal, I need-

ed to provide the detailed context of housing policy formation (reformation) and apply the appropriate housing system theories. In this respect, I took inspiration especially from those theoretical studies that stressed in context of housing system formation the importance (influence) of:

- ideology, social norms;
- traditional problem solution patterns (*path dependence*);
- current social and political structures.

Path dependence refers to the tendency of problem solutions to become locked in and difficult to change. In other words, past experience, past form and content of public discourse, past methods to problem solutions, past policies and ideologies and past forms and behaviour of institutions strongly influence the present situation. The concept is related to the regulation approach trying to find long-standing specific national patterns of housing policies reflected in specific types of social regulation (social policies). Political structuralism, conversely, stresses more the role that interests of specific political parties may have on the shaping and development of diverse housing policies in various countries; it stresses the political context of housing provision and creates the typology of possible state interventions. The role of social norms (ideology) in specific housing system development (especially in tenure structure) is also very important. The social constructivism puts its main emphasis on meanings (ideas, norms) assigned to reality than to reality in itself; the ideological framework affects 'political tenure strategy' and thus governments create environments that favour one or another type of tenure and strongly influence the tenure decisions of its citizens. The above-mentioned theoretical concepts helped me to take an analytical view on the causes of particular transition housing policy in the Czech Republic.

7.3 Research questions and main findings

In this part of the book final chapter I will repeat all my research questions and present the main findings that seek to answer them. The following summary thus forms the overview of main results of my research.

7.3.1 The wider context of housing subsidies in the Czech Republic

My first research question was as follows:

What was the background to the development of the specific housing policy and housing system in the Czech Republic? What were the ideologies (norms), traditional problem solution patterns and institutional as well as political structures that might influ-

ence the formation and development of the housing system (including the formation of general social policy and its history)?

Reforms in the field of housing in the Czech Republic were, as one might expect, numerous and often the by-products of wider economic (price liberalisation) or political (decentralisation of power) transitional reform strategies. If I were to select the main features, I would propose the following list.

The revenue subsidies for existing state rental dwellings and capital subsidies for new state rental housing construction known from the period of socialism practically disappeared; prices of construction materials were liberalised and quickly increased; and both factors led to radical house price growth and a sharp drop in housing construction volumes (till 1996). Despite that the Czech Republic had 424 dwellings per 1,000 inhabitants in 2001. Comparison with other developed and transitional countries confirms its relative housing sufficiency.

Though officially the state denied to continue in the socialistic concept of cheap state rental housing considered to be a pure public good outside of market relations, it abolished many former regulations and allowed for housing market institutions to emerge, several important decisions of the early transition governments, such as preservation of the socialist type of rent control and tenant protection, represented surviving patterns of the ideology of socialism under new market environment.

The state decentralised some powers and responsibilities in the housing field to the municipal level (more than 6,000 independent local governments per 10 million inhabitants of the Czech Republic emerged, representing an example of the highest decentralisation of power among post-socialist countries) and this decentralisation of power was accompanied by a free transfer of former state rental housing to the ownership of municipalities. The restitution of expropriated property to former owners or their descendents, the free transfer of state housing into municipal ownership and its subsequent privatisation (sale) under advantageous conditions mostly to sitting tenants (though no central right-to-buy policy was applied), the transformation of cooperative housing and exclusion of vacant dwellings from rent regulation all led to significant changes in tenure structure. These changes, however, were not as substantial as in many other transition societies – increase in homeownership rate (by more than ten percentage points between 1991 and 2001) and conversely a reduction in the share of rental flats (by almost 11 percentage points). While the share of cooperative housing decreased, the share of private rental housing increased.

Rent regulation was maintained in all occupied rental flats (whether restituted or public) and its deregulation proceeded relatively slowly during the early phase of transition (governments led by the main right-wing political party till 1998). Later on the regulated rents were even frozen in real val-

ues (1998-2002) and also in nominal values (2002-2006) by governments led by left-wing social democrats. The deep gap between regulated and 'market' rents was preserved till the end of 2006 and this created the grounds for many social tensions. Rent regulation and favourable privatisation of municipal housing were the main allocation sources of substantial economic subsidies which became the most important housing subsidies during the transitional period. Among the new explicit subsidies worth mentioning are the housing allowance, several supply-side subsidies for construction of municipal housing, tax relief on housing loans, interest subsidy to mortgage loan and the state premium to housing savings scheme.

Chapter 2, starting with a brief comparison of housing policy and housing system changes in several transition societies, has already argued that one group of subsidies is generally not measured and definitely not demonstrated in official statistical figures: economic subsidies. These often hidden subsidies are equal to the difference between market and actual price for goods and services. In other words, people pay less for some service (housing) than they would pay under market conditions.

In my analysis of selected transition countries I showed that the same part of the population (existing occupants of public housing) received basically similar economic subsidy – either in the form of owner-occupied flats purchased for a very low price (or even obtained for free) or in the form of rental housing with low regulated rent and strong pre-transition type of tenancy protection. The economic subsidies probably formed the main housing subsidies during the transition. The income or social situation of eligible households was not deemed important; the only criterion was the occupancy title. These subsidies therefore divided households into two very disparate groups. The 'insiders' enjoyed low housing costs and tenancy protection (with no regard to their social needs or income levels) while the 'outsiders' were often left to the uncompromising market forces. 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 'insiders' to move or rationalise housing consumption. In this context, I wrote about the segmentation of housing market into the 'privileged' and 'unprivileged' segments – housing expenditures for otherwise comparable housing in these two segments differed strongly.

The reforms (price liberalisation, end of state housing construction) led to a worsening of housing affordability, especially for households living in the 'unprivileged' market segment (with no access to economic subsidies). As has been demonstrated by thorough analysis of developments in housing affordability in the Czech Republic, the housing expenditure-to-income ratio for households in 'unprivileged' owner-occupied housing was roughly 10 percentage points higher than that of housing owners in the 'privileged' market segment, and the ratio for household in 'unprivileged' rental housing was roughly 8 percentage points higher than that of households in the 'privileged'

segment of the rental market. According to the adjusted housing expenditures-to-income ratio, 44% of households in the 'unprivileged' rental market segment (as opposed to 17% of households in the 'privileged' rental market segment), and 57% of households in owner-occupied flats in the 'unprivileged' market segment (as opposed to 20% in the 'privileged' segment) would have a housing expenditures-to-income ratio that exceeds the normative affordability limit of 25%.

With regard to the wider context in which housing policy was shaped and reshaped after 1990, and taking into account the selected theoretical concepts described above, the following contextual features were found to be especially important in understanding particular housing policy actions and their effectiveness/efficiency in the Czech environment:

- The parliamentary character of the political system, the proportional type of electoral system to the main Chamber and the necessity of investiture of the incoming government all had important consequences on government stability in the Czech Republic; since 1996 lack of effective government (unstable due to the very weak majority support) has been the main feature of the political situation.
- The right-wing ('market-strong') political party ODS led the government in the period 1992-1998; the left-wing ('market-weak') political party ČSSD led the government in the period 1998-2006.
- The communists, the second and later third most powerful political party in transitional politics did not transform themselves into a democratic left-wing party and continued to be embedded by communist rhetoric and day-to-day politics in the pre-1989 past; on the other hand, they were successfully cut off from any real influence on political and/or institutional reforms (unlike in many other transition societies).
- Clientelism (influential informal networks, establishment of powerful lobbying networks), the inherited culture of illegal income (shadow economy, 'preying on the state') and corruption were among institutional patterns that survived the change of regime and were very characteristic of the transitional time; clientelism, corruption and the law-breaking culture were the main reasons for the rather negative evaluation of enterprise privatisation. During privatisation, former managers of state companies (often unskilled but well-established in networks) received relatively large powers. Many new owners of investment funds established in the course of voucher privatisation abused the capital invested by the public.
- The early transitional Czech government led by right-wing ODS is often considered to be 'stuck in social democratic, consensual politics' though its rhetoric was quite the opposite – advocating free market and economic liberalism. In other words, 'right-wing liberalism' seemed to be acceptable to Czech society only when it was limited to rhetoric and accompanied by social-democratic practice ('think left, vote right').

- One of the main consequences of ‘consensual politics’ was ‘banking socialism’ or ‘state capitalism’. State-owned banks were forced to extend risky credit to ineffective industry, thus maintaining an artificially low unemployment rate; after a short period of ‘functioning’, this system saw the emergence of a huge banking crisis, unexpected economic recession and massive state budget expenditure to stabilise the banking sector (1996-1997).
- Czech society is traditionally suspicious of nobility and the Church (it is very atheistic) and, since the period of the Austrian Empire and especially the period of the first Czechoslovak Republic established after WWI, it is very sensitive to social issues, social problems, and social equality (this may be connected specifically to Czech nationalism); even now the Czech level of income inequality and poverty rate are among the lowest in the European Union. The social and economic consequences of the economic recession in 1930s became an important part of the collective memory of Czech society.
- Although during communism it was almost folklore to blame the state for low living standards and for any shortcoming (logically, the state was *omnipotent*), in reality the dependence on the paternalistic and monopolistic state was a powerful social norm. The ‘social contract’ contained the people’s tolerance of ideological, cultural and political suppression in exchange for the other party in the contract, the state, continuing to provide them with promised gifts – employment, free housing, free education, free health care and so forth. This contract could not be deleted from people minds as quickly as it was dissolved in practice.
- Transitional social policy (till 2005) had to reflect the traditional attention paid to social issues and the living collective memory of the generous state: its goal was to create a relatively soft ‘welfare state cushion’ to preserve social order by such means as highly progressive income taxing, high social insurance payments, regular valorisation of the subsistence minimum, a two-component structure of subsistence minimum and relatively generous social benefits. The system remained highly redistributive, with an especially high burden put on the middle classes (‘excessive solidarity’). The establishment of this generous social state was part of the ‘consensual politics’ of the early transition governments led by the right-wing ODS and contrasted strongly with the political rhetoric of its representatives.
- The imperatives of efficiency, effectiveness and long-term sustainability in policy interventions were not taken into account in the early transition phase. Governments (led both by right-wing and left-wing parties) established a comfortable ‘welfare state cushion’, which helped to preserve low income inequality and a low poverty rate in a society. However, when the stream of income from enterprise privatisation started to dry up the costs of the social state became unbearable and led to increasing state deficit;

another price paid for this generous social policy was the prolongation of the people's false expectations of the *omnipotent* and paternalistic state.

- 'The demographic revolution' started after 1989 when natality and nuptiality rates substantially decreased. Since 1994 the population has shown negative natural growth; total fertility rate fell to less than 1.14 children in 2001, which is one of the lowest rates in the world.

7.3.2 Evaluation of housing subsidies in the Czech Republic

My second research question was as follows:

How effective and efficient were state interventions in the field of housing consumption during the transition in the Czech Republic if the theoretical framework and methodological device of welfare economics is used for such assessment? How effective were such interventions from the point of view of both vertical and horizontal effectiveness? How efficient were such interventions if we narrow the wide concept of efficiency to the cost-benefit analysis of state interventions in the field of housing consumption (i.e., subordinate efficiency to effectiveness)? How efficient and effective were these interventions when assessed against the assumptions on efficiency and effectiveness of subsidies?

The effectiveness of three selected housing subsidies was especially evaluated: economic subsidy stemming from rent regulation, tax relief and housing allowance. Given that in both the Rawlsian and Utilitarian concepts of the welfare state effectiveness is linked to equality, the analysis of effectiveness was based on two criteria. The first criterion was the evaluation of to what degree did the three instruments contribute to a reduction of the level of inequality in society. To this end several indicators of income inequality were used (standard deviation, the coefficient of variation, the variation of the income logarithm, the mean income ratio of 5% of the lowest-income households and 5% of the highest-income households, and the Gini coefficient illustrated by the Lorenz curve). The second criterion was based on a comparison of the real distribution of subsidy among various income groups with a normative criterion of effective distribution. Effective distribution of a subsidy was regarded as distribution of the subsidy where 90% of the sum of resources was distributed among 50% of the lowest-income households, while 75% of the subsidy sum was distributed among 30% of the lowest-income households.

The results of the tests showed that households most likely paying regulated rent were relatively evenly distributed across the individual income deciles. It also confirmed that the economic subsidy following from regulated rent was significantly higher among the highest-income households in com-

parison with the lowest-income households. The Lorenz curve illustrates that this form of subsidy was closest to the curve of equal income distribution, that is, households across the income spectrum benefited from it to roughly the same degree. This economic subsidy did not fulfil the normative criterion of effectiveness, as 50% of the lowest-income households received approximately 46% of the sum of the subsidy, and 30% of the lowest-income households received approximately 25% of the sum of the subsidy.

The main group of recipients of indirect fiscal support in the form of a tax relief was formed primarily by highest-income households, and therefore the effectiveness of this form of subsidy was very low. Clearly the percentage of households that took advantage of this form of support was significantly higher among the highest-income households. The Lorenz curve shows that of the instruments evaluated here this form of subsidy was unequivocally directed mostly in favour of the highest-income households.

Unlike the other instruments the housing allowance is a means-tested benefit. Naturally the percentage of households entitled to the housing allowance was highest among lowest-income households, and no highest-income households qualified to receive housing allowance. The indicators of income inequality revealed that housing allowance do contribute to a reduction in the level of income inequality in society. This was confirmed again in the depiction of the distribution of the subsidy in the Lorenz curve. The housing allowance also satisfied the selected normative criterion of effectiveness, given that 50% of the lowest-income households would be the recipients of 99% of the sum of the subsidy, and 30% of the lowest-income households would be the recipients of 97% of the sum of resources paid out as housing allowances. However, housing allowance did not meet the criterion of horizontal effectiveness as some needy households were actually excluded from eligibility (households paying market rents).

Although the available data sources did not allow me to verify this directly, it could be detected from other survey data sources that other selected housing subsidies (economic subsidy stemming from privatisation of public housing, state premium to housing savings scheme and supply-side subsidies for construction of 'municipal' housing) also displayed very low effectiveness.

For the efficiency part of the housing policy evaluation I dealt with economic subsidies stemming from rent regulation, housing allowance, state premium to housing savings scheme and tax relief. The efficiency of all these subsidies is sub-optimal with the possible exception of tax relief which I could not judge directly; especially low efficiency was detected in the case of economic subsidy stemming from rent regulation and in the case of state premium to housing savings scheme. Through the application of robust econometric methods the analytical results pointed especially to the profound gap between 'efficient' and real rent prices in the rent-controlled housing sector. I also demonstrated the low efficiency of state premium to housing savings by

the performance of both housing savings banks (low loan-to-savings balance, competition constraints) and savers (switching savings from other deposits by holding overall savings rate constant). In the case of tax relief I was able only to show that the Czech Republic belongs among countries with the highest inconsistency in taxing on housing (in favour of homeownership), that is among countries with maximal fiscal subsidies to promote homeownership. The efficiency itself was not evaluated as data were not available at the time.

In conclusion, the overall evaluation of Czech housing policy from the point of effectiveness and subordinated efficiency was relatively negative. Housing policy was based on one-time untargeted economic subsidies that could not be sustained, even for pure financial reasons, in the long-term and were shown to be ineffective/inefficient; other explicit housing subsidies also had serious drawbacks from the viewpoint of vertical effectiveness (tax relief, supply-side subsidies, state premium to housing savings scheme), horizontal effectiveness (housing allowances) and/or efficiency (especially state premium to housing savings scheme). Though the Czech Republic entered the transition period with relatively sufficient housing stock and, compared with other transitional societies, relatively better housing quality, housing subsidies in the field of housing consumption were overwhelmingly ineffective and inefficient. They increased social and income inequalities in Czech society and also strengthened the division of the housing market into 'privileged' and 'unprivileged' housing segments.

7.3.3 Partial evaluation of housing subsidies in other transition countries

My third research question, designed to help me understand the specific situation in the Czech Republic was as follows:

How efficient and effective were state interventions in other transition countries (if the imperative on individual openness of researchers during the international comparison of housing policies is met)? What explanations for particular levels of effectiveness and related (subordinated) efficiency of state interventions in the field of housing consumption in the Czech Republic can be found in a partial international comparison? Can such a partial international comparison help me to understand the specific situation in the Czech Republic?

A partial international comparison of housing policy changes in six transition countries (Poland, Czech Republic, Slovakia, Estonia, Bulgaria and Romania) conducted in 2001 shows that the Czech Republic belonged to the group of countries with the least effective demand and supply-side subsidies. Though in this case the assumptions on effectiveness and efficiency were somewhat narrow, due to limited information and data accessibility, it was clear that the

targeting and efficiency of housing subsidies in the Czech Republic were evaluated as more badly off than in neighbouring transition countries.

Based on criteria outlined in the fifth chapter, Poland was the only country with a relatively high level of efficiency/effectiveness of both demand and supply-side subsidies. It had a legal definition for social housing, housing association legislation and it allocated subsidies mainly for new social rental housing construction among non-profit housing associations. The subsidy took the form of a qualified loan and covered only part of total construction costs (the remainder had to be covered from private sources). The allocation of social flats was subject to means-testing and associations made regular income inspections of beneficiaries (every two years). 'Old' rent regulation was slighter and the housing allowance model counted with actual housing costs limited by indirectly set ceilings (reflecting the regional differentiation in rent prices). The applied normative rate of burden increased with income level and a gentle taper did not lead to the poverty trap. The total payment due was co-financed from both state and municipal budgets.

Similarly, the Estonian housing allowance (subsistence benefit) model did not use flat notional costs. The maximum notional cost was set at the local level (reflecting regional differentiation in housing costs), therefore it provided more effective help to those in need than the Czech or Slovakian models. However, its high degree of taper and exclusive state financing disadvantaged the model in comparison with the Polish housing allowance model. On the one hand, Estonia had abolished the central system of 'old' rent regulation and introduced the legal definition for social housing; on the other hand the government supported only purchase/construction of owner-occupied housing regardless of the applicant's income and introduced no types of non-profit housing associations.

Romania and Slovakia introduced programmes for new 'social' rental housing construction (means testing was applied during the dwellings' allocation) but both countries neither introduced non-profit housing associations at that time nor carried out regular income inspections, nor did they abolish 'old' rent controls. The Slovakian housing allowance model did not reflect regional price differentiation. Programmes supporting purchase/construction of owner-occupied housing were not always sustainable in the long term. Romania had no significant demand-side subsidy while Bulgaria was the only country without decisive supply-side or demand-side subsidies (with the exception of temporal energy allowance) implemented at that time.

The relative position of the Czech Republic was surprising. The Czech housing allowance model used only flat notional housing costs which took no regard of regional differentiation in prices/rents and did not reflect the higher level of market rents. Allowances were paid solely from the state budget. There was no legal definition for social housing, no legislation on non-profit housing associations and the 'old' system of untargeted central rent control

was maintained in both the public and private rental sectors. Though the programme for new municipal rental housing construction allowed for private capital participation, it often led to some kind of 'quasi-rental' tenure. As it did not include means testing, the effectiveness of this programme was low. No other municipal social housing development programmes following the rules of Slovakian case were introduced at that time.

The most effective/efficient subsidies were thus implemented in the country where the general policy orientated towards the rental model was accompanied by decentralisation in the rental sector of housing (Poland). If I exclude Bulgaria and Romania from the comparison (as some types of subsidies were missing), the least effective/efficient subsidies appeared in the country where policy orientated towards the rental model was accompanied by a low level of decentralisation in the rental sector of housing (Czech Republic). However, this is not just because higher decentralisation in itself leads to higher efficiency/effectiveness of subsidies. It may also be due to the fact that if some old inefficient practices are decentralised to the local level or indirectly abolished (e.g., through housing privatisation) central administration very probably has simply stopped being attacked by various interest groups wanting to keep those old practices alive. This might allow the central government to prepare new, more efficient/effective subsidies with no need to look for any kind of hybrid solution between past relics and new initiatives. Decentralisation may thus help central governments to clear the table and start afresh. Until the government is, however, occupied by problems connected with cultural patterns surviving from the previous regimes, there is little political will to prepare or introduce new, more effective/efficient subsidies.

From the comparison of housing conditions in particular countries we can discern another empirical implication. Relative housing sufficiency (Czech Republic, Slovakia, and Estonia) leads to lower effectiveness/efficiency of housing subsidies whereas relative housing insufficiency (Poland) leads to the opposite. The factor of housing need (housing shortage) may thus have some influence on actual efficiency and effectiveness of state subsidies because a country in an acute need of new housing cannot afford to experiment with hybrids of new and old practices. However, further empirical work on a bigger sample of transitional countries would be needed to confirm such a conclusion.

7.3.4 Other factors of low effectiveness and efficiency of housing subsidies in the Czech Republic

I hypothesised that the relatively poorer efficiency/effectiveness of housing subsidies in the Czech Republic may be caused by the fact that the general policy orientated towards the rental model was not accompanied by real decentralisation in the rental sector of housing (especially in the field of rent

setting); the relative housing sufficiency might be also an important factor. There may be, however, several other reasons for the ineffective/inefficient character of policies in the field of housing consumption in the Czech Republic; reasons that could be raised only from a detailed study of the specific policy context in the Czech Republic. My fourth research question was thus as follows:

What general conclusions can be drawn about the application of the role of ‘understanding paternalist’ by the Czech state between 1990 and 2005? What reasons for particular levels of effectiveness and related (subordinated) efficiency of state interventions in the field of housing consumption can be found from housing system evolution analysis? What influence did ideologies (norms), traditional problem solution patterns and institutional as well as political structures have on the development of specific state interventions in the field of housing consumption, and what effects did they have on the efficiency and effectiveness of these state interventions?

From the detailed description of the context briefly mentioned above I found the following specific ‘national’ factors (reasons) as potential explanations for the low effectiveness and efficiency of housing subsidies in the Czech Republic:

- political factors
 - government instability stemming from the proportional election system (since 1996);
 - small politically weak and centre-orientated Christian democrats (KDU-ČSL) often taking the post of Minister for Regional Development (responsible for housing policy) in various coalition governments;
 - high degree of decentralised power and an increasing influence of often unqualified mayors of smaller cities on central policies;
 - fragmentation of the responsibility for central housing policy among three ministries and lack of efficient cooperation between them;
 - lack of qualified economists (as well as experts in general) in the main left-wing political party (ČSSD);
 - long period (1998-2006) of governments led by ‘market-weak’ social democrats (ČSSD) trying to establish a strong welfare state and in housing policy representing mainly the interests of sitting tenants.

- ideological factors
 - traditional egalitarianism of Czech society (‘think left-vote right’) coming from traditional animosities to the nobility and Catholic Church;
 - distrust of long-term strategies (concepts) in the ideology of leading right-wing political party (ODS) stemming from the experience with planning economy;
 - ‘populism’ (‘banking socialism’, ‘state capitalism’) of leading right-wing

political party (ODS) preferring short-term achievements (safety nets, soft welfare-state cushion, *ad hoc* reactions), over-employment and excessive wealth redistribution to long-term sustainable economic growth (and leading later to public budget deficits accelerating when the stream of privatisation income dried up);

- general fear of political representation that to alter behaviour patterns common during communism in this field might cause social disorder, breach social peace and endanger the transitional project;
 - the hard-line communists (KSČM) taking second rank in parliamentary elections till 1998 continued to follow the ideology of general equality and universal applicability even under the circumstances of growing income and social inequality.
- path dependence
 - the inherited institutional culture of clientelism and corruption opposing higher transparency in government spending (efficiency and effectiveness of policies has not been investigated, measured, analysed, or monitored);
 - the inherited expectations of the Czech population to receive free 'gifts' from the 'omnipotent' state, especially when it concerns the housing;
 - the inherited focus of policymakers and politicians on extensive housing indicators (e.g., scale of housing construction with no attention being paid to where and whom it was allocated) and only very slow recognition of the need to define new types of policy assessment means.
 - institutional (social) factors
 - due to the large shadow economy means testing (targeted to those in need) became highly unreliable;
 - relatively good housing conditions supported by low number of foreign immigrants;
 - the objective effort to help the highly taxed middle class that received only a little from the otherwise generous social support system.

An enormous amount of empirical data would be required to perform a real structural analysis of the significance of individual factors but such data were not available. Therefore I had instead no other option but to determine the significance of these factors indirectly, that is, from the opinions of those people who implemented housing policy during the observed period. I conducted in-depth interviews with two former ministers responsible for the preparation and implementation of housing policy in the Czech Republic, and one interview with a high-ranking public official working in the field of national housing policy.

Basically, we can define two categories of factors that may lie behind the

low level of efficiency and effectiveness of housing policy: explicit (expressed by the interviewed actors themselves) and implicit (structural, latent). According to the interview results, explicit factors mainly include: the inadequate qualifications of political representatives and their 'politicking'; the distrust politicians felt towards the research sphere and towards ministry officers; an unwillingness on the political right to accept long-term concepts, and an inability to come up with a conceptual solution on the political left; the strong influence of municipal mayors on central housing policy; the need to find solutions quickly without the opportunity to test them; and the relatively strong lobbying engaged in by interest groups.

Included among other cited explicit factors belongs the need to take into account the attitudes and expectations of Czech citizens, who simply could not be 'cut off' from their previous experience and behavioural patterns; this was consistent with so called 'consensual politics' practised by the first Czech transition government led by the right-wing ODS. The targeting of public housing subsidies to those who need it was not demanded by the public, nor monitored or questioned in the media. Housing policy was not viewed as being part of social policy but rather as something separate from it, which should not target the needy especially; perhaps because the problem of housing affordability is common to everyone and because the allocation of flats was universal and free up until not too long ago.

The concept of housing policy focusing extensively on the scope of housing construction was similarly adopted: what was important is the number of newly built flats, and it did not matter where they were built, for whom, at what level of quality, or how they were allocated. Officials did not care that public support of such housing construction had a negative impact on the market functioning and/or strengthens income and social inequalities. It became apparent during the interviews that the perspective (evaluation) of efficiency and effectiveness of public subsidies was never considered, was never the subject of discussion, and is for many an entirely new idea and partly even incomprehensible to them.

The question remains why this perspective never entered into public or political discourse, why it remained outside the area of housing policy? The answer is clearly connected with another group of factors that are implicit, unexpressed, and latent. Is the reason the fact that there was no acute housing shortage in the Czech Republic, even though respondents tended to reject this factor? Or is it what lies behind the unstable government, the persistence of an unreformed form of Communist Party or the persistence of the culture of clientelism and corruption? It is very difficult to answer these questions; probably each factor has had a certain amount of influence, and only in combination did they lead to the given outcome. The factor of the relatively strong political representation of the unreformed Communist Party in parliament certainly ranks among the weaker factors. Though this converse claim

remains on a hypothetical level, the stronger factors are likely to include relative housing sufficiency, the long period of government led by 'market-weak' Social Democrats, and the inherited culture of clientelism leading to increasing power of lobbying filling in the absence of any independent research. The retention of inherited behavioural patterns, 'consensual politics', was surely also influential; such politics found especially good ground in the Czech context, traditionally critical of 'differences' (nobles, alternative values, inequalities in wealth) and giving much attention to social peace and uniformity.

7.3.5 Policy recommendations for higher effectiveness/efficiency of housing subsidies

My last research question, designed to represent the application of feedback from the results of all the analyses presented in this book, is as follows:

Do the main findings of the research conducted for this book show whether it is possible to increase efficiency and effectiveness of state intervention in the field of housing consumption in the Czech Republic? If so, what would be the policy recommendations?

In its final part, the book elaborates on a most important set of policy recommendations that would help to enhance the efficiency and effectiveness of housing subsidies. As mentioned earlier, Czech housing policy was unequivocally skewed in favour of owner-occupied housing (which violates the neutrality imperative) and in favour of demand-side subsidies (which may violate the imperative of rational mix of demand and supply-side subsidies). The explicit priority focus of the policy to support demand has been balanced by large latent economic subsidies that by nature are forms of supply-side subsidies (in both rental and owner-occupied housing sectors); however they are temporary in duration and will come to an end very soon. Owing to the high, though latent and often overlooked, economic subsidies, the division of responsibility for housing policy among three ministries, and especially due to the absence of any form of evaluation and monitoring of subsidy distribution, Czech housing policy is in violation of the imperative of transparency.

Based on this evaluation, the best programmes would include one such for the construction of supported housing and the housing allowance; to some extent also a programme for the construction of municipal rental flats for low-income households (based on conditions valid since 2003) and preferential loans for young first-time buyers. The worst evaluated forms of public support included economic subsidies in the area of rental and owner-occupied housing (rent regulation and the privatisation of flats) and support for the construction of municipal rental flats based on conditions valid up to the end of 2002; also to some extent, support for the construction of rental housing as part of foreign investment incentives, the state premium on housing

savings, the interest subsidy and the tax subsidy.

If the programmes have something in common, then it is their relative lack of transparency deriving mainly from the inability to execute any simple subsequent monitoring/audit of the subsidy use (with the sole exception of housing allowance); also, the equality of 'mediators' in the allocation of subsidies is violated in many respects given that support can only be distributed among some actors. Particularly the transparency of the conditions for all housing subsidies must be substantially improved as well as the subsequent control of real subsidy take-up. Often there is no information about the real distribution of subsidies, that is information about the final beneficiaries. The monitoring systems simply do not exist. Such a fact excludes any possibility of effective control of state-intervention goals.

Support for the construction of rental flats as an foreign investment incentive, the premium on housing savings, and the tax subsidy were evaluated as the worst instruments of Czech housing policy, still existing in 2008, that arguably need significant reform. The housing allowance, owing to shortcomings from the perspective of horizontal effectiveness, would also require partial changes to its terms. This reform could take the following shape:

- The state premium on housing savings should be reduced and income-targeted. It should be automatically tied to interest rate changes so that the amount of the premium responds flexibly to macro-economic changes, or it should be made possible for the government to decide on its amount.
- Subsidies for the construction of flats as part of foreign investment incentives should be abolished.
- The tax subsidy should be abolished or strongly limited given that it significantly strengthens tax inconsistency, affects the tenure neutrality and is highly regressive.
- The part of the housing allowance that relates to notional housing expenditure should take into account the existence of 'unprivileged' market rental housing. There should be some reduction in the level of allowances provided among homeowners in order to avoid unnecessary wastage.

Given that housing policy is currently explicitly focused especially on supporting owner-occupied housing by demand-side subsidies, a strengthening of public support for rental housing on the supply side has been suggested. This kind of support can, for example, take the form of creating a legislative framework and a system of grants for non-profit rental housing. Another form could be the creation of motivational incentives that would lead municipalities towards more responsible policy in managing their housing stock – the establishment of a segment of social flats. It is also necessary to reduce the fragmentation of housing policy among different ministries. Initiating a serious discussion on the scope and consequences of economic subsidies and strengthening neutrality and transparency with subsequent monitoring of

the efficiency and effectiveness of subsidies appear to be the main challenges now facing Czech housing policy.

Appendix A Public housing policy and instruments

Public housing policy

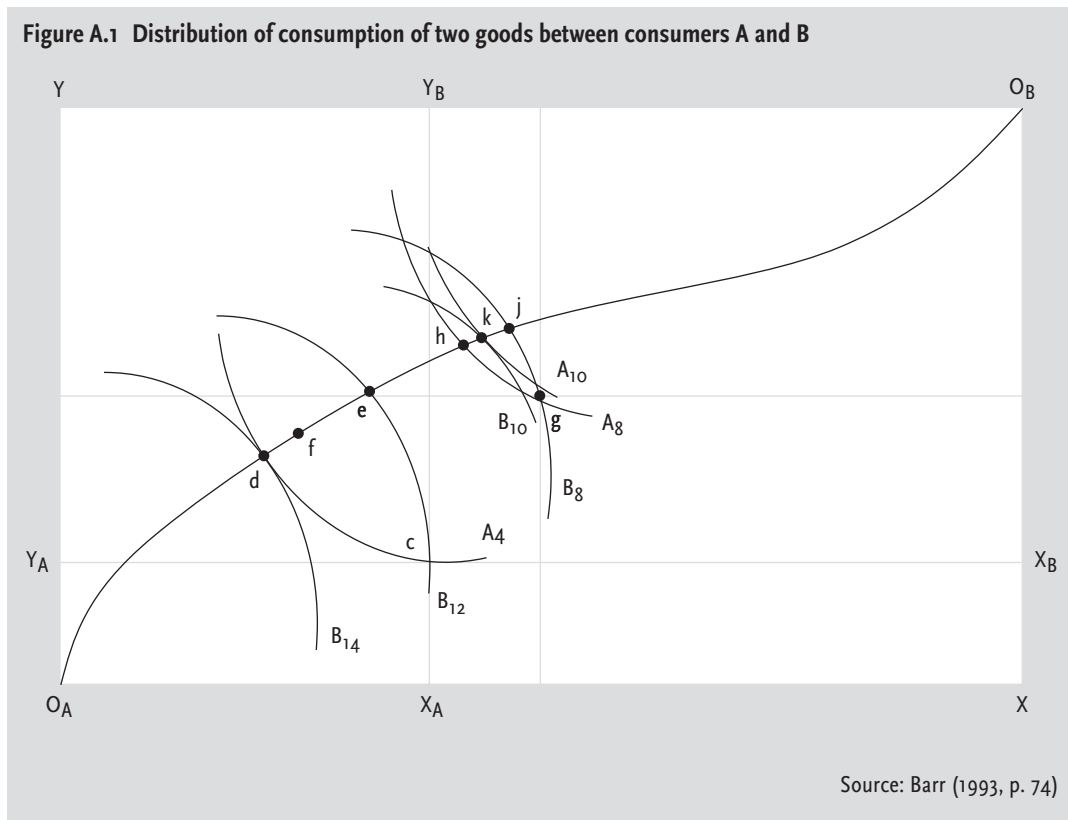
The double role of public authorities as *rational economists* and *understanding paternalists* may be illustrated from the point of view of the welfare economy in Figure A.1 (Edgeworth box), which is based on the analysis of the welfare function W :

$$W = W [U_1 (x_{11}, X_{12}, \dots, x_{1m}), U_2 (x_{21}, x_{22}, \dots, X_{2m}), \dots, U_n (X_{n1}, x_{n2}, \dots, x_{nm})]$$

where U_1 through U_n indicate the level of total utility given by consumption x_1, \dots, x_m of goods by individual n citizens. Figure A.1 shows a situation in which there are only two consumers in society (A and B) and two consumer goods (X and Y); the consumption of good X by consumer A is captured on axis $O_A X$ and by consumer B on axis $O_B X$, and the consumption of good Y by consumer A on axis $O_A Y$ and by consumer B on axis $O_B Y$. The total consumption of consumer A is then measured from the starting point O_A and the total consumption of consumer B from the opposite starting point O_B . Curves A_n create indifference curves of consumer A (i.e., the combination of goods X and Y bringing consumer A the same utility), curves B_n create indifference curves of consumer B. The 'contraction curve' connecting points O_A and O_B indicates all combinations of consumption of X and Y where the value of the marginal substitution in consumption of goods X and Y is the same for both consumers (i.e., it connects points where the indifference curves of both consumers meet and any movement outside this curve means a worsening of the situation for at least one of the consumers).

Let me assume, for example, that the initial division of consumption of goods X and Y is located at point c in Figure A.1 where consumer A consumes X_A units of good X and Y_A units of good Y and consumer B consumes X_B units of good X and Y_B units of good Y (it is obvious that consumer B is far richer than A since he may consume far more goods X and Y than consumer A). If, through market improvement (intervention of public authorities) the division of consumption moves from point c to point d , consumer B becomes 'better off' (he moves up to a higher indifference curve from B_{12} to B_{14}) and consumer A does not become 'worse off' (since he remains on the same indifference curve A_4 , i.e., he achieves the same total utility). The shift from point c to point d constitutes a Pareto improvement. Similarly, a shift from point c to point e also constitutes a Pareto improvement and this time the poor consumer A becomes 'better off'; consumer A arrives at a higher indifference curve and consumer B remains on the same indifference curve B_{12} . Shifts from point c to points d and e always lead to greater allocation efficiency, a more optimal division of goods, while points d and e are equal with respect to pure efficiency (i.e., from the point of view of a public authority as *rational economist*). If a public authority performed only the role of rational economist, its role would end by improving the efficiency of market function-

Figure A.1 Distribution of consumption of two goods between consumers A and B



Source: Barr (1993, p. 74)

ing (e.g., elimination of a monopoly) leading from point c to point d or e.

Public entities, however, also enter the housing market as understanding paternalists and come with a certain concept of a welfare state. Since there are several concepts of the welfare state, let me outline briefly the potential conduct of a public authority 'headed' by libertarians, utilitarians, egalitarians, and socialists:

- **Libertarianism** – For libertarians the only way to improve social welfare is a Pareto improvement, that is a shift from point c to any point on the contraction curve (but not shifts along the contraction curve as such). Any pressure or policy leading to a further redistribution of wealth (e.g., a shift from point d to point k) is not desirable from a traditional liberal point of view (English political economy of the 18th century) or from the neo-liberal point of view represented by Hayek and Friedman in the second half of the 20th century.
- **Utilitarianism** – The objective of utilitarians is to maximise the total utility of everyone. Thus, similar to libertarians, utilitarians would support the shift from point c to any point on the contraction curve. Unlike libertarians, however, some utilitarians consider the utility to be a cardinally measurable variable (i.e., one that can be expressed in monetary or other measurable units). If both consumers A and B have an identical marginal utility of income functions (i.e., an income growth by an unit brings both of them the same growth in utility) the starting point for seeking the optimal distribution of goods is point g where both consumers consume the same

amount of goods X and Y. A Pareto improvement is possible from point g to point k , where the two consumers would be located on the same level of measurable utility functions (indifference curves A_{10}, B_{10} , (i.e., each of them would achieve 10 units of measurable utility); consumption distribution corresponding to point k on the contraction curve would thus, according to their perception of the welfare state, correspond to the ideal. If, however, the marginal utility of the income functions differed among individual consumers, the optimum allocation point would be different.

- *Rawls's egalitarianism* – According to Rawls (1995), goods should be distributed according to rational social justice while assuming the existence of a 'veil of ignorance' concerning the future position of all society members on the market; that is, distribution of goods should be adjusted as long as each new structure improves the total utility of the poorest member on the market. Rawls' theory of social justice is based on the imperative to improve the situation of the most disadvantaged person in the market (therefore, a shift from point c to point d would not be desirable although it does constitute a Pareto improvement). The shift from point d to point k is desirable from the point of view of Rawls' theory, although it does not constitute a Pareto improvement because the 'poorer' consumer A benefits to the detriment of the 'richer' consumer B. Like some utilitarians, egalitarians would consider the distribution corresponding to point k to be ideal.
- *Socialism* – According to the basic thesis of socialism, all goods should be allocated completely equally; that is, like Rawls, socialists consider any shift towards point k to be desirable although it does not constitute a Pareto improvement and the situation of one may improve to the detriment of another.

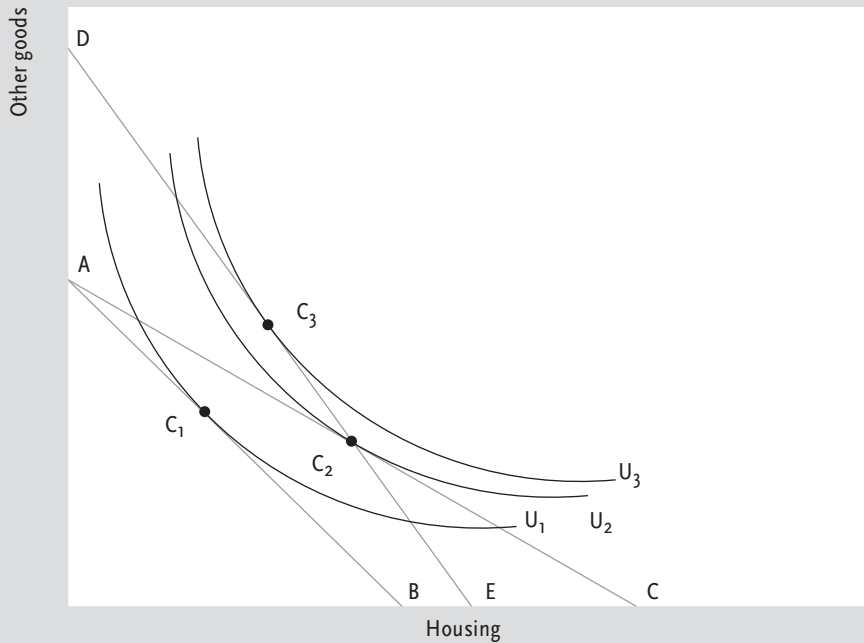
Public housing instruments

Let me assume that the preference of a given needy household is reflected in indifference curves U_1, U_2 and U_3 which connect all combinations of the consumption of housing and other goods that bring the household the same utility. Curve AB indicates the income limit curve of the household, mathematically speaking:

$$y = p_1x_1 + p_2x_2$$

Here y is the income of the household and p_1, p_2 are the prices of both goods and x_1, x_2 are the consumed amounts of both goods (x_2 represents the amount of consumed housing services, housing). The household that desires to maximise its utility will opt for a consumption combination that will correspond to point C_1 , where the income limit curve touches the highest possible indifference curve. Let us now presume that state intervention will result in a decrease in the cost of housing to p_2' . The income limit curve will then, thanks

Figure A.2 Comparison of the efficiency of cash allowance vs. price regulation



Source: Fallis (1985, p. 131)

to the decreased cost of housing, move from AB to AC. The new income limit curve AC can be mathematically captured thus:

$$y = p_1x_1 + p_2'x_2$$

Because only the cost of housing decreases, point A remains the starting point of the income limit curve on the axis measuring the consumption of other goods. In such a case, a rationally thinking household will opt for a combination of consumption in point C_2 on the higher indifference curve U_2 ; it will spend more on housing ($x_{2,2}$) and may consume more of the other good (though what happens depends on the shape of the indifference curve). Let me now presume that the public authority, instead of decreasing the cost of housing, gives the needy household an income-tested cash allowance, the payment of which is as costly for public budgets as the original intervention consisting of decreasing the market prices of housing. Then the income limit curve moves from AB to DE, and mathematically we can describe curve DE thus:

$$y + (p_2 - p_2')x_{2,2} = p_1x_1 + p_2x_2$$

Since point C_2 is the point where the income limit curve AC touches the indifference curve U_2 and since indifference curves are usually convex toward the beginning, part of the income limit curve DE must be above the level of

indifference curve U_2 . Consequently, the household receiving an equally costly cash allowance is able to achieve a greater indifference curve (U_3) than it could if the intervention were to result in a decrease in the cost of housing, and opts for a combination of consumption corresponding to point C3 in Figure A.2.

Appendix B Programmes to meet the social objectives of housing policies

The following is a list of the main possible social objectives of local government or national housing programmes:

- higher affordability of housing for middle and low-income households;
- higher quality of housing;
- social mix;
- higher labour/tenant mobility;
- sustainable development of housing conditions;
- specific shortages (housing care, sheltered and supervised housing for disabled, handicapped, elderly, homeless people and children without parents);
- tenant participation.

Higher affordability of housing for middle and low-income households

The examples of possible local or national housing programmes include:

- Housing allowances (HA)
 - *Effectiveness* – Has the programme fulfilled the objectives of its developers (a decrease in the average rent-to-income ratio and the household structure of HA beneficiaries can be used)? Is the percentage of households receiving HA high enough to have a decisive influence on higher affordability of housing for middle and low-income households? Are some households excluded from HA due to the formula or other restrictive provisions (e.g., needy households living in the market rental sector)? What is the share of households that apply for HA out of the total number of households eligible for HA? If the share is low, why don't households want to apply for HA? Do HA really help those who are expected to be helped (low income households) or does the insufficient targeting lead to a relatively high share of higher income households among the HA beneficiaries?
 - *Efficiency* – What is the share of HA expenditure on total state/local housing expenditures? Is there an empirical test of the correlation between the introduction of HA and rent price growth in an uncontrolled (market) rental sector? What is the estimated impact of HA introduction on rent price inflation? What other state/local expenditures rose due to the inflation caused by the introduction of HA? Is there any econometric analysis comparing the overall demand side expenditure (HA) with the situation when the same amount of sources is used for supply side subsidies (e.g., new construction of social housing, improvement of current housing stock, etc.)? Does a higher HA (in association with higher rents), when factored according to the particular formula of HA applied in a particular country, raise the probability that the household will choose not to work instead of pursuing economic activity? Is there clear evidence of demotivation from a particular HA model (poverty trap)? Is this problem quantified in some way?

- Rent regulation/setting/pooling
 - *Effectiveness* – Is rent regulation truly targeted at socially needy populations? Are some socially needy groups of households excluded from the sector where rents are controlled by public authorities (by excess demand or insufficient monitoring of rent-controlled housing stock)? Are there provisions allowing for a rise in regulated rents when the income of households living in the controlled sector rises? Do rent deregulation processes reflect the different levels of social needs of the different households?
 - *Efficiency* – What is the effect of rent control on labour mobility (e.g., number of re-lets in a controlled sector and market sector or the results of household mobility studies can be used)? What is the amount of reconstruction/improvement investments in the controlled sector compared to the market sector? What is the average difference between rents in controlled and uncontrolled housing sectors for the same kind of dwellings in the same locations (or, at least, same size of residence)? Do rents reflect the property values of dwellings in a controlled sector? Is there any evidence of under-occupation/over-consumption in the rent-controlled sector? How much do households from old dwellings subsidise the households living in new dwellings in the case of rent-pooling? What are the complementary public expenditures connected with the rise of rents (e.g., rise in Retail Price Index → rise in public expenditures on pensions or social transfers)?
- Allocation policy
 - *Effectiveness* – Are dwellings with lower rents allocated among households with lower income and vice versa (in cases of municipal or alternative management rental housing)? Is the maximum income limit applied in the allocation of social housing (means testing)? Are any groups of households excluded from the allocation of current social housing? Do municipalities require a period of permanent residence in the area of the local authority when households apply for social housing? Is there a stigma attached to social housing leading to a situation whereby other needy households decline to apply for social housing? Does a point system reflect the real social needs in different localities?
 - *Efficiency* – If the rent-setting mechanism is based on income, what incentives are given to encourage members of a household to begin or continue work instead of being unemployed? How is the difference managed between the housing costs of social landlords and income flowing from rent, related to applicant income? Is there any econometric analysis comparing the expenditures of a specific allocation policy to expenditures on HA when the same level of rent-to-income ratio is assured? Are higher income households forced to leave the social housing sector?

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- New social housing construction (provided by various management forms)
 - *Effectiveness* – Has the programme fulfilled the objectives of its developers (e.g., housing for low and middle-income households)? Is the maximum income limit applied in the allocation of new social housing (means testing)? Does the programme lead to filtering (e.g., households applying for new social dwellings must let their former municipal rental dwellings for allocation to new socially needy households)? Can the programme be used (or abused) for other purposes due to bad legislation, rules or insufficient control (e.g., quasi-ownership housing instead of rental housing, housing for higher income households instead of housing for low or middle-income households, etc.)? Are there effective provisions to prevent this situation? Are any households from target groups excluded from new social housing allocation, if so, then why?
 - *Efficiency* – What are the construction costs per square metre of new social housing compared to the construction costs of other private or public sector providers, including other authorities offering housing of similar type and quality and on a similar scale, while excluding the land price (comparative cost analysis)? Are construction-cost limits applied when public subsidies are allocated? Do rents in new social dwellings cover the total costs connected with maintenance, administration, repairs and construction after the deduction of subsidies, low or zero land price, tax advantages, etc.? Do rents reflect the property value of dwellings (location, quality, and services)? What is the average rent price of new social housing for differently sized dwellings in comparison to the rents of new rental dwellings in other controlled or uncontrolled rental sectors in the same location? What is the average net present value (NPV) of new social housing investment (counting grants, interest subsidies, etc.) compared to the NPV of investments in the construction of new private rental dwellings? Are there any studies quantifying the scale of the crowding out effect of social housing construction? Are there any econometric tests comparing the overall expenditures of demand side subsidies (HA) with the same level of supply side subsidies (social housing construction)?
 - Privatisation of rental dwellings (higher affordability of ownership housing)
 - *Effectiveness* – Did lower and middle-income households privatise their dwellings? Were they interested in the privatisation process? What incentives were created by state or local authorities to encourage lower and middle-income households to privatise their dwellings?
 - *Efficiency* – What was the average difference between the market price of dwellings and the price of dwellings used for privatisation, broken down by size of residence or location? Do new owners take care of their properties (i.e., pay enough to the repair funds to assure the maintenance and improvement of the dwellings)? What percent of privatised dwell-
-

ings were sold immediately after privatisation? What are the measures applied to prevent speculation or the dilapidation of buildings being privatised?

Higher quality of housing

Examples of possible local/national housing programmes include:

- Refurbishment/reconstruction of dwellings
 - *Effectiveness* – Has the programme fulfilled the objectives of its developers (e.g., improvement in the locations where it was expected, the expected scale of improvement works, etc.)? Do tenants (or other people directly influenced by the programme) participate in the design and practical application of the programme?
 - *Efficiency* – Are costs of refurbishment/reconstruction lower than the costs of demolition and new housing construction (including direct costs plus higher maintenance costs and risk premiums in the case of refurbishment/reconstruction of low-quality dwellings)? Were the costs of the programme covered or at least partially funded by private capital? In the event homeowners benefit, will they cover a substantial part of the improvement costs? In the event tenants benefit, will the costs of improvements to the dwellings be covered (at least partially) through higher rents in the improved dwellings?
- Regeneration of neighbourhood
 - *Effectiveness* and *efficiency* can be evaluated by answering the same questions as in the case of refurbishment/regeneration of dwellings.
- New social housing construction
 - *Effectiveness* – Are there explicit requirements concerning the quality of new social housing dwellings (e.g., size of dwelling, materials used, and insulation standards)? Could the developers avoid meeting these provisions? How are the developers encouraged to increase the quality of housing?
 - *Efficiency* – see above.

Social mix

Examples of possible local/national housing programmes include:

- Allocation policy
 - *Effectiveness* – Does the allocation policy in current and/or new municipal housing and/or housing managed by new legal forms (with the important role of municipality) assure the maintenance or recovery of the social mix in different locations/blocks of flats? How? When analysing the time series, is the effect of allocation policy on the maintenance of the social mix only short-term or can it be expected to remain long term? Is any trend raised from time-series analysis that could serve as evidence for the answer of the previous question?

-
- *Efficiency* – see above.
 - Rent setting/regulation/pooling
 - *Effectiveness* – Is the rent-setting mechanism or rent regulation designed in a way that leads to a social mix of population and prevents social exclusion? Is the effect of rent policy on the maintenance of social mix only short-term or it can be expected to last? Is any trend raised from time-series analysis that could serve as evidence for the answer of the previous question?
 - *Efficiency* – see above.
 - Refurbishment/reconstruction of dwellings and regeneration of dwellings
 - *Effectiveness* – Are there any social survey results confirming that improvement programmes helped to maintain the social mix in particular districts or blocks of flats? Are the inhabitants living in areas or dwellings chosen for improvement participating in the project design and application? Do social landlords conduct regular tenant-satisfaction surveys? Is the effect of refurbishment projects on the maintenance of social mix short-term or it can be expected to last? Is there any trend raised from time-series analysis that could serve as evidence for the answer of the previous question?
 - *Efficiency* – see above.
-

Appendix C Optimisation programme on public housing construction costs

The programme is looking for the minimum of the following equation:

$$\text{MIN} \left[\left(J_{Ki} \times \frac{i_{Kmax}}{1 - \frac{1}{(1+i_{Kmax})^n}} - J_{Ki} * \frac{i_{Ki}}{1 - \frac{1}{(1+i_{Ki})^n}} \right) * \frac{1 - \frac{1}{(1+i)^n}}{i} \right], \text{ where}$$

i_{Kmax} - maximum interest rate on qualified loan (5% p.a.);

i - discount rate (5% p.a.);

n - loan maturity (25 years);

J_i - loan principal for region i ;

J_{Ki} - qualified loan principal for region i ;

i_{Ki} - optimised interest rate of a qualified loan for region i .

under the following conditions:

$$J_i \geq 0$$

$$J_{Ki} \geq 0$$

$$0,0000000001 \leq i_{Ki} \leq 0,05$$

$$P_i = J_i + J_{Ki}$$

$$J_i \times \frac{i_T}{1 - \frac{1}{(1+i_T)^n}} + J_{Ki} \times \frac{i_{Ki}}{1 - \frac{1}{(1+i_{Ki})^n}} + OC_i \leq NR_i, \text{ where}$$

P_i - cost price of an average new dwelling in region i ;

i_T - market interest rate for mortgage loans in 2002 (6.7% p.a.);

OC_i - running costs (management and maintenance costs) - 2% of P_i ;

NR - normative rent (equal to rent in rent-controlled sector at a particular stage of simulation).

If the equation does not have a solution even when $i_{Ki} \approx 0$ and $J_i = 0$, then the principal of a qualified loan gradually decreases using the following relation: $J_{Ki}(1-z)$, where $z = 0,0001$. A qualified loan is thus substituted by a grant. In each step of iteration the decrease in principal of a qualified loan is connected to the decrease of total construction costs till the moment when costs are lower or equal to normative rent (or when the full qualified loan is substituted by a grant). Only if under such a condition the normative rent still does not cover the construction costs (subsidised by grant), then the difference between costs and normative rent is supposed to be covered by regular revenue subsidies.

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Summary

The objective of this book was to fill in the gaps and to some extent further the knowledge in accounts that reinterpret and evaluate the processes that occurred in the Czech Republic over the course of the economic transition. The book describes and analyses the housing system establishment (reform) in the Czech Republic after 1990. Transition was mainly the process of building new (or transforming old) social institutions. It was far from spontaneous; on the contrary, it was highly regulated and shaped by political power, especially by the representatives of the state. The behaviour (actions, interventions) of the state in the field of housing thus formed the main research focus of the book.

The state may intervene in many fields – housing production, housing consumption, land zoning, housing finance, distribution and redistribution, allocation, location. Both governments and citizens of transition societies paid special attention to the ‘housing needs problem’ or ‘housing affordability problem’; housing affordability became the most reiterated housing issue and policy target. Housing affordability is especially connected to the level and quality of housing consumption and therefore the book pays special attention to those state interventions directed at influencing housing consumption (explicit or implicit subsidies to maintain or increase housing affordability). These interventions were not only described but also assessed, because description alone does not allow full understanding of their impact on housing consumption or housing affordability. The prerequisite for such an evaluation was also the detailed description of social, economic and political contexts in which the Czech housing system emerged; and at least partial international comparison with situation in other transition countries.

The policies (interventions) were evaluated, on the background of wider context and international comparison, from the point of view of their efficiency and effectiveness. The efficiency was defined through the Pareto lens: if any alternative allocation of goods increases utility from consumption for at least one actor on the market and at the same time does not decrease utility from consumption for other actors then we say such allocation is inefficient and there is room for improvement in market performance. Such improvement may often be ensured only by state intervention. For housing markets, particular examples of market failure may be the existence of oligopoly or monopoly in housing finance or production, asymmetric information among market agents (information access barriers), externalities during housing production or consumption. An example of this inefficiency may, however, also be the situation when the state spends tax-payers’ money for production and allocation of goods or services that could be allocated similarly (or even more efficiently) by private entities, or the situation when alternative subsidy settings can produce, under the condition of holding the same quality and quantity of consumption distribution, public savings.

Effectiveness is closely associated with the idea of equity, social justice. As

such, it is closely connected with particular welfare state regimes, particular social norms, and particular redistributive policies. Effectiveness may be understood as the degree to which the originally defined redistributive goals of state intervention are met, that is, whether public funds are actually spent where they were allocated and whether those for whom they were intended actually are helped. However, the concept of effectiveness is not left to a vague 'definition infinity'; welfare economists did not want to leave the concept of effectiveness solely to the will of lawmakers or governments, who often do not define the intention of the intervention at all. The concept was thus, at least partially, generalised into the common shared assumption that whatever state redistribution of wealth is finally applied, it should decrease social inequality in society, that is, redistribution policies should help the worse-off with the costs of the better-off.

Welfare economics distinguishes between 'vertical' and 'horizontal' effectiveness. Vertical effectiveness measures the degree of redistribution of income, consumption and wealth from the rich to the poor. In the case of particular housing subsidy it measures the extent to which such subsidy is actually allocated to those who really need help, that is to low-income households. It measures whether it ultimately decreases social and income inequality in society. Horizontal effectiveness is connected with the idea of setting a minimum standard of consumption (income, wealth) that would be ensured for all members of society, as well as with the assumption that all needy (poor) households have equal and unrestricted access to subsidies, that is none of the poor (needy, low income) are excluded from such redistribution. In the case of particular housing subsidy it measures whether any needy (poor) household is not eligible to apply for the subsidy.

The concept of effectiveness was fully applied in this book, including the evaluation of both vertical and horizontal effectiveness. State actions in the field of income or wealth redistribution have a direct impact on housing consumption. However, the concept of efficiency is much broader. It also relates to state interventions concerned with the general functioning of the housing market, covering for example problems such as price speculations, oligopoly structures in housing supply, restrictive urban planning, asymmetric information, etc. Therefore, the concept of efficiency has been limited to the efficiency of those state interventions that have direct influence on housing consumption, or defined more precisely, those state interventions aimed at redistributing wealth, goods or income. Efficiency was limited to the analysis of possible public savings under an alternative subsidy setting, or under an alternative set of subsidies. Efficiency was thus subordinated to effectiveness and narrowed to potential public savings.

The first chapter of the book discussed theoretical and methodological device used to describe and evaluate the housing systems, housing subsidies, and the role of the state in the field of housing. This discussion helped to an-

swer preliminary questions and outline main research questions of the book.

The second, mainly descriptive chapter, focused on a partial international comparison of housing policies in the field of housing consumption in six selected transition countries. Its main purpose was to show what generally happened during transition in the field of housing policy and what similarities as well as differences among transition countries can be detected in this process. The main conclusion was that in all selected transition countries the same part of the population (existing occupants of public housing) received basically similar economic subsidy – either in the form of owner-occupied flats purchased for a very low price (or even obtained for free) or in the form of rental housing with low regulated rent and strong pre-transition type of tenancy protection. The economic subsidies probably formed the main housing subsidies during the early phase of transition. The income or social situation of eligible households was not deemed important; the only criterion was the occupancy title. These subsidies therefore divided households into two very disparate groups. The ‘insiders’ enjoyed low housing costs and tenancy protection (with no regard to their social needs or income levels) while the ‘outsiders’ were often left to the uncompromising market forces. In this context, the segmentation of housing market into the ‘privileged’ and ‘unprivileged’ segments has been pronounced – housing expenditures for otherwise comparable housing in these two segments differed strongly.

In the third chapter, again more or less descriptive, the context in which housing policy was formed and reformed during transition in the Czech Republic has been described. This included descriptions of the political, institutional, economic and demographic contexts as well as the history of both social and housing policies applied in the territory of the current Czech Republic in the past. This chapter also comprehensively described and discuss the changes in housing conditions (including tenure structure), housing policy, housing finance and housing affordability in the period 1990-2005 in the Czech Republic.

The main goal of the fourth chapter, analytical by nature, was to evaluate the effectiveness and subordinated efficiency of state interventions in the field of housing consumption (policies) introduced in the Czech Republic in the period 1990-2005. In conclusion, the overall evaluation of Czech housing policy was relatively negative. Housing policy was based on one-time untargeted economic subsidies that could not be sustained, even for pure financial reasons, in the long-term and were shown to be ineffective/inefficient; other evaluated housing subsidies also had serious drawbacks from the viewpoint of vertical effectiveness (tax relief, supply-side subsidies, state premium to housing savings scheme), horizontal effectiveness (housing allowances) and/or efficiency (especially state premium to housing savings scheme). Though the Czech Republic entered the transition period with relatively sufficient housing stock and, compared with other transitional societies, relatively bet-

ter housing quality, housing subsidies in the field of housing consumption were overwhelmingly ineffective and inefficient. They increased social and income inequalities in Czech society and also strengthened the division of the housing market into 'privileged' and 'unprivileged' housing segments.

The fifth chapter, again analytical, compared, albeit partially, the effectiveness and subordinated efficiency of housing subsidies among selected transition countries. Its main purpose was to detect at least some reasons for the application of specific policies in the Czech Republic, as well as the reasons for the particular effectiveness and subordinated efficiency of Czech housing subsidies. The aim was to discover which specific 'national' factors are visible only via network of several 'out-national' reference points. The most effective/efficient subsidies were found in the country where the general policy orientated towards the rental model was accompanied by decentralisation in the rental sector of housing (Poland). The least effective/efficient subsidies appeared in the country where policy orientated towards the rental model was accompanied by a low level of decentralisation in the rental sector of housing (Czech Republic). It may also be due to the fact that if some old inefficient practices are decentralised to the local level or indirectly abolished (e.g., through housing privatisation) central administration has simply stopped being attacked by various interest groups wanting to keep those old practices alive. This might allow the central government to prepare new, more efficient/effective subsidies with no need to look for any kind of hybrid solution between past relics and new initiatives. From the comparison of housing conditions in particular countries another empirical implication has been discerned. Relative housing sufficiency leads to lower effectiveness/efficiency of housing subsidies whereas relative housing insufficiency leads to the opposite. The factor of housing need (housing shortage) may thus have some influence on actual efficiency and effectiveness of state subsidies because a country in an acute need of new housing cannot afford to experiment with hybrids of new and old practices. However, further empirical work on a bigger sample of transitional countries would be needed to confirm such a conclusion.

The sixth chapter attempted to find other reasons (other than following from international comparison) for the introduction of particular types of policies as well as for the particular levels of effectiveness and subordinated efficiency of housing subsidies specific to the Czech Republic. According to the results of interviews with several housing policy makers, the factors mainly include: the inadequate qualifications of political representatives and their 'politicking'; the distrust politicians felt towards the research sphere and towards ministry officers; an unwillingness on the political right to accept long-term concepts, and an inability to come up with a conceptual solution on the political left; the strong influence of municipal mayors on central housing policy; the need to find solutions quickly without the opportunity to test them; and the relatively strong lobbying engaged in by interest groups.

Housing policy was not viewed as being part of social policy but rather as something separate from it, which should not target the needy especially. The concept of housing policy focusing extensively on the scope of housing construction was similarly adopted: what was important is the number of newly built flats, and it did not matter where they were built, for whom, at what level of quality, or how they were allocated. Officials did not care that public support of such housing construction had a negative impact on the market functioning and/or strengthens income and social inequalities. It became apparent during the interviews that the perspective (evaluation) of efficiency and effectiveness of public subsidies was never considered, was never the subject of discussion, and is for many an entirely new idea and partly even incomprehensible to them.

The seventh and concluding chapter of the book summarises the main findings and provides an overview of the conclusions (answers) to all research questions, including the most important housing policy recommendations.

Samenvatting

Volkshuisvestingsbeleid en woonsubsidies in Tsjechië tijdens de economische transitieperiode

Een voorbeeld van de kloof tussen het voortlevende verleden en de noodzaak tot hervormingen

Martin Lux

Het doel van dit boek is om de kennis die beschreven staat in artikelen, waarin de processen die in Tsjechië plaatsvonden tijdens de economische overgang opnieuw geïnterpreteerd en geëvalueerd worden, samen te brengen en waar mogelijk uit te breiden. Het boek beschrijft en analyseert (de hervorming van) het volkshuisvestingsbeleid in Tsjechië na 1990. De overgang bestond met name uit het opzetten van nieuwe danwel het omvormen van bestaande sociale instituties. En dat ging niet vanzelf; integendeel, deze overgang was sterk gereguleerd en geregisseerd door de politiek en met name door de vertegenwoordigers van de overheid. De interventies van de overheid op het gebied van de volkshuisvesting vormen de belangrijkste bron van onderzoek in dit boek.

De overheid kan interveniëren in verschillende gebieden: woningproductie, woonconsumptie, grondbestemming, woningfinanciering, verdeling en herverdeling, toewijzing en locatie. Zowel overheden als burgers in transitielanden besteden speciale aandacht aan de problemen op het gebied van 'beschikbaarheid' en 'betaalbaarheid' van woningen, waarbij het probleem van de 'betaalbaarheid' de boventoon voert en het vaakst als beleidsdoel genoemd wordt. De betaalbaarheid van woningen is sterk verbonden met de omvang en de kwaliteit van de woonconsumptie; het boek gaat dan ook dieper in op overheidsinterventies gericht op de beïnvloeding van de woonconsumptie (zoals directe of indirecte subsidies om de betaalbaarheid van woningen te handhaven of te verbeteren). Deze interventies worden niet alleen beschreven maar ook geëvalueerd, omdat een beschrijving alleen niet genoeg inzicht geeft in de impact van de maatregelen op de woonconsumptie of de betaalbaarheid van woningen. Voor een dergelijke evaluatie is een gedetailleerde beschrijving nodig van de sociale, economische en politieke context waarbinnen het Tsjechische volkshuisvestingssysteem zich heeft ontwikkeld, evenals een (gedeeltelijke) internationale vergelijking met de situatie in andere transitielanden.

De efficiëntie en effectiviteit van het beleid (de interventies) zijn geëvalueerd vanuit deze achtergronden en internationale vergelijking. De efficiëntie van het beleid is gedefinieerd door middel van het *Pareto-optimum*: als een alternatieve toewijzing van goederen het nut uit consumptie voor ten minste één speler op de markt verbetert en tegelijkertijd niet leidt tot een ver-

mindering van het nut uit consumptie voor andere spelers, is een dergelijke toewijzing inefficiënt en is er ruimte voor verbetering van de marktwerking. Een dergelijke verbetering kan vaak alleen door interventie van de overheid tot stand worden gebracht. Typische voorbeelden van marktfalen op de woningmarkt zijn het bestaan van een oligopolie of monopolie op het gebied van financiering of productie, asymmetrische informatie tussen spelers op de markt (waarbij sommige spelers geen toegang hebben tot bepaalde informatie), en externe omstandigheden die productie of consumptie beïnvloeden. Een ander voorbeeld van dergelijke inefficiëntie kan een situatie zijn waarin de overheid belastinggeld gebruikt voor de productie en toewijzing van goederen of diensten die net zo goed (of zelfs efficiënter) door private partijen toegewezen hadden kunnen worden. Of een situatie waarin een alternatieve verdeling van subsidies (aangenomen dat dit zou resulteren in een gelijkwaardige kwaliteit en omvang van de consumptieverdeling) besparingen voor de overheid zou kunnen opleveren.

Effectiviteit hangt sterk samen met het idee van gelijkheid, van sociale rechtvaardigheid. Het is dan ook sterk verbonden met bepaalde welvaartsamenlevingen, bepaalde sociale normen en waarden en bepaalde herverdelingsprincipes. Effectiviteit kan gezien worden als de mate waarin de oorspronkelijke herverdelingsdoelen die ten grondslag liggen aan overheidsinterventies gehaald zijn. Met andere woorden: of publieke gelden daadwerkelijk zijn uitgegeven aan die zaken waar ze voor bedoeld waren en of degenen voor wie deze gelden bestemd waren er ook daadwerkelijk mee geholpen zijn. Maar het concept effectiviteit is geen helder omschreven begrip: welvaartseconomen hebben dit niet willen overlaten aan juristen of overheden, die de achterliggende intentie van een interventie doorgaans niet helder definiëren. Het concept is dan ook (gedeeltelijk) gegeneraliseerd tot de algemene aanname dat herverdeling van welvaart door de overheid altijd zou moeten leiden tot vermindering van sociale ongelijkheid in een samenleving. Met andere woorden: herverdeling zou ertoe moeten leiden dat de sterkste schouder de zwaarste lasten dragen.

De welvaartseconomie maakt onderscheid tussen 'verticale' en 'horizontale' effectiviteit. Verticale effectiviteit meet de mate van herverdeling van inkomen, consumptie en bezit van de welgestelden naar de minder welgestelden. Bij bepaalde vormen van woonsubsidie meet verticale effectiviteit de mate waarin de subsidie daadwerkelijk terecht komt bij degenen die deze het hardst nodig hebben: de huishoudens met de laagste inkomens. Zo wordt gemeten of de subsidie de sociale en inkomensongelijkheid in een samenleving uiteindelijk vermindert. Horizontale effectiviteit heeft te maken met de idee dat er een minimale standaard van consumptie (inkomen, bezit) vastgesteld zou moeten worden die voor alle leden van de samenleving gegarandeerd zou moeten zijn, en met de aanname dat alle minder welgestelde huishoudens gelijkwaardige en onbeperkte toegang tot subsidies hebben en er dus geen

minder welgestelde huishoudens zijn die niet van deze herverdeling kunnen profiteren. Bij bepaalde vormen van woonsubsidie meet horizontale effectiviteit of er ook minder welgestelde huishoudens zijn die niet in aanmerking komen voor deze subsidie.

Het effectiviteitsconcept is in dit hele boek toegepast, inclusief de evaluatie van zowel verticale als horizontale effectiviteit. Interventies door de overheid op het gebied van herverdeling van inkomen of bezit hebben een directe invloed op de woonconsumptie. Het concept efficiëntie is echter veel breder. Dit omvat immers ook overheidsinterventies die te maken hebben met het algemene functioneren van de woningmarkt en die gericht zijn op problemen zoals prijsspeculatie, oligopolische structuren aan de aanbodkant, een restrictief stadsplanningsbeleid, asymmetrische informatie, enzovoort. Om die reden is het concept efficiëntie in dit boek beperkt tot de efficiëntie van overheidsinterventies die een directe invloed hebben op de woonconsumptie, oftewel overheidsinterventies die gericht zijn op de herverdeling van bezit, goederen of inkomen. Hierbij is alleen gekeken naar de analyse van mogelijke overheidsbesparingen bij een alternatieve verdeling van subsidies, of bij een alternatieve vorm van subsidies. Efficiëntie is dus ondergeschikt gemaakt aan effectiviteit en betreft hier alleen mogelijke overheidsbesparingen.

In het eerste hoofdstuk van het boek worden de theorie en methode uiteengezet waarmee de woonsystemen, woonsubsidies en de rol van de overheid op het gebied van wonen zijn beschreven en geëvalueerd. Met behulp van dit overzicht kunnen voorlopige vragen beantwoord worden en krijgen de belangrijkste onderzoeksvragen uit het boek hun vorm.

Het tweede hoofdstuk is voornamelijk beschrijvend van aard en behandelt een (gedeeltelijke) internationale vergelijking van volkshuisvestingsbeleid op het gebied van woonconsumptie in zes geselecteerde landen in een economische situatie van transitie. Doel hiervan is te laten zien wat er tijdens de overgang gebeurde op het gebied van woonbeleid en of er in dit proces verschillen danwel overeenkomsten tussen de onderzochte landen te ontdekken zijn. De belangrijkste conclusie hierbij is dat in al deze landen hetzelfde deel van de bevolking (bestaande bewoners van sociale woningbouw) eenzelfde soort subsidie ontving, hetzij in de vorm van koopflats die tegen een sterk gereduceerde prijs (of soms zelfs gratis) werden aangeboden, hetzij in de vorm van huurwoningen met een lage, gereguleerde huur en sterke huurbescherming op het niveau van voor de transitie. Deze economische subsidies waren de belangrijkste vorm van woonsubsidie in de beginfase van de transitie. Het inkomen of de sociale status van de huishoudens die hiervoor in aanmerking kwamen deed er niet toe; het enige criterium was de soort huisvesting (sociale woningbouw). Daardoor ontstond een sterke tweedeling onder huishoudens in deze landen. De 'insiders' profiteerden van lage woonkosten en hoge huurbescherming (ongeacht hun inkomen of sociale situatie), en de 'outsiders' werden overgelaten aan de grillen van de markt. In deze context is de

verdeling van de woonmarkt in bevoorrechte en onbevoorrechte segmenten duidelijk zichtbaar: de kosten voor – op andere fronten vergelijkbare – huisvesting in deze twee segmenten varieerden immers sterk.

In het derde hoofdstuk, dat eveneens min of meer beschrijvend van aard is, komt de context aan de orde waarin het volkshuisvestingsbeleid in Tsjechië tijdens de overgang gevormd en hervormd werd. Hierbij gaat het om beschrijvingen van de politieke, institutionele, economische en demografische context, maar ook om de geschiedenis van het sociale beleid en volkshuisvestingsbeleid in het gebied dat het tegenwoordige Tsjechië beslaat. Daarnaast beschrijft en evalueert dit hoofdstuk de veranderingen op het gebied van huisvesting (waaronder het huurstelsel), sociale woningbouwbeleid en financiering en betaalbaarheid van woningen in de periode 1990-2005 in Tsjechië.

Het belangrijkste doel van het vierde hoofdstuk, dat analytisch van aard is, is de effectiviteit en daarmee de efficiëntie van interventies in het volkshuisvestingsbeleid in Tsjechië in de periode 1990-2005 te evalueren. De conclusie luidt dat deze evaluatie van het Tsjechische volkshuisvestingsbeleid over het algemeen een relatief negatief beeld laat zien. Het beleid was gebaseerd op eenmalige, ondoelmatige economische subsidies die op de lange termijn niet gehandhaafd konden worden, zelfs niet om puur financiële redenen, en die bovendien ineffectief en inefficiënt bleken. Andere onderzochte volkshuisvestingssubsidies hadden eveneens belangrijke tekortkomingen vanuit het oogpunt van verticale effectiviteit (belastingaftrek, subsidies vanuit de aanbodkant, overheidssteun aan woningbouwprojecten) en horizontale effectiviteit (huursubsidie) en/of efficiëntie (met name door overheidsbijdragen aan woningbouwprojecten). Hoewel Tsjechië aan het begin van de transitieperiode relatief gezien over voldoende woningvoorraad beschikte in vergelijking met andere landen in transitie, en deze woningvoorraad van betere kwaliteit was, waren de woonconsumptiesubsidies zonder meer ineffectief en inefficiënt. De subsidies vergrootten de sociale- en inkomensongelijkheid in Tsjechië en versterkten bovendien de verdeling van de woningmarkt in bevoorrechte en onbevoorrechte segmenten.

Het vijfde hoofdstuk, ook weer analytisch van aard, bevat een (gedeeltelijke) vergelijking van de effectiviteit en daarmee de efficiëntie van woonsubsidies in geselecteerde transitielanden. Het belangrijkste doel van dit hoofdstuk is om mogelijke redenen te achterhalen waarom bepaalde beleidsmaatregelen in Tsjechië werden toegepast en waarom deze subsidies wel of juist niet effectief en efficiënt waren. Doel hierbij is om na te gaan welke specifieke 'nationale' factoren alleen zichtbaar worden door middel van een netwerk van verschillende 'buiten-nationale' referentiepunten. De meest effectieve en efficiënte subsidiemaatregelen waren te vinden in Polen, het land waar het algemene beleid, gericht op het huurmodel, gepaard ging met decentralisatie van de huursector. De minst effectieve en efficiënte subsidiemaatregelen waren te vinden in Tsjechië, het land waar het algemene beleid, gericht op het

huurmodel, gepaard ging met een lage mate van decentralisatie van de huursector. Het kan ook zo zijn dat de centrale overheid, wanneer bepaalde, inefficiënte praktijken gedecentraliseerd worden naar lokaal niveau of wanneer deze indirect worden afgeschaft (bijvoorbeeld door privatisering van woningen), simpelweg niet langer onder vuur wordt genomen door de verschillende belangengroepen die willen dat de bestaande praktijken gehandhaafd blijven. Hierdoor kan de centrale overheid nieuwe, effectievere en efficiëntere subsidies ontwikkelen zonder te hoeven zoeken naar een soort hybride oplossing die het midden houdt tussen overblijfselen uit het verleden en nieuwe initiatieven. Uit de vergelijking van het sociale woningbouwbeleid in bepaalde landen komt een andere empirische implicatie naar voren. Een relatief voldoende aantal beschikbare woningen leidt tot een lagere effectiviteit en efficiëntie van woonsubsidies, terwijl een relatief onvoldoende aantal beschikbare woningen leidt tot het tegenovergestelde. De factor woonbehoefte (tekort aan woningen) kan dus van invloed zijn op de feitelijke effectiviteit en efficiëntie van overheidssubsidies, omdat een land waarin een directe behoefte aan nieuwe woningen bestaat het zich niet kan permitteren om te experimenteren met hybride beleidsmaatregelen die oude en nieuwe praktijken combineren. Om een dergelijke conclusie te bevestigen is echter meer empirisch onderzoek in een groter aantal landen in transitie noodzakelijk.

In het zesde hoofdstuk is geprobeerd om andere redenen te vinden (die niet voortkomen uit de internationale vergelijking) voor de introductie van bepaalde soorten beleid en voor de specifieke mate van effectiviteit en efficiëntie van de woonsubsidies in Tsjechië. Uit de interviews met verschillende beleidsmakers uit de volkshuisvesting komen de volgende factoren naar voren: politieke vertegenwoordigers die niet naar behoren gekwalificeerd zijn en hun 'politieke spelletjes'; het wantrouwen van wetenschappers en ministeriële ambtenaren door politici; de onbereidwilligheid van politiek rechts om langetermijnconcepten te accepteren en het onvermogen van politiek links om met een conceptuele oplossing te komen; de grote invloed van burgemeesters op het centrale volkshuisvestingsbeleid; de noodzaak om voor snelle oplossingen te kiezen zonder dat er de mogelijkheid is om deze te testen; en de relatief sterke lobby van belangengroeperingen. Het volkshuisvestingsbeleid werd niet gezien als onderdeel van het sociaal beleid maar als een op zichzelf staand beleid dat niet noodzakelijkerwijs gericht was op de lage inkomens. Het beleid ten opzichte van nieuwbouw liet een vergelijkbaar beeld zien: het enige wat telde was het aantal flats dat gebouwd werd – het maakte niet uit waar ze werden gebouwd, voor wie, van welke kwaliteit ze waren of hoe ze vervolgens werden toegewezen. Het kon ambtenaren weinig schelen dat dit beleid een negatieve invloed had op het functioneren van de markt of leidde tot meer inkomens- en sociale ongelijkheid. Uit de interviews bleek dat evaluatie van de effectiviteit en efficiëntie van overheidssubsidies nooit was overwogen of zelfs maar onderwerp was geweest van discussie en dat dit voor ve-

len een geheel nieuw en gedeeltelijk zelfs onbegrijpelijk idee was.

Het zevende en laatste hoofdstuk van het boek vat de belangrijkste bevindingen samen, geeft een overzicht van de conclusies van (of antwoorden op) alle onderzoeksvragen en bevat een aantal belangrijke aanbevelingen voor het in de toekomst te voeren volkshuisvestingsbeleid.

Curriculum vitae

Martin Lux was born in Nový Jičín in the Czech Republic, in 1971. In 1994 he received his master title in economics at the University of Economics in Prague and in 1997 he received the master title in sociology at the Charles University in Prague. In 2005 he started his PhD studies at the OTB Research Institute for Housing, Urban and Mobility Studies of the Delft University of Technology in the Netherlands.

Martin Lux is currently head of the Department of Socio-Economics of Housing at the Institute of Sociology, Academy of Sciences in Prague. He was the leader of several international and national housing research projects and work as consultant for the Local Government Initiative (Budapest), UN/ECE (Geneve), the Czech government and the Czech banking sector. He is the editor of eight books, such as *Housing – Res Publica* (Prague, SLON, 2002) and *Housing Policy – an End or a New Beginning?* (Budapest, LGI, 2003). He is the author and co-author of articles in *Urban Studies*, *Journal of Housing and the Built Environment*, *European Journal of Housing Policy*, *Czech Journal of Economics and Finance*, *Czech Sociological Review*, *Politická ekonomie* and others. Martin Lux is a member of the European Network for Housing Research, the Association for Housing Market Development and the Advisory Board for the European Journal of Housing Policy. His main research interests include comparative housing policies, social housing, housing finance and housing economics.

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