

IV. HOUSING ECONOMICS AND AFFORDABILITY

A. Housing and the national economy

1. Highlights of recent macroeconomic developments

Following a 7.3 per cent drop in GDP in 1992 and a 1.5 per cent drop in 1993, the aggregate output of the Bulgarian economy increased by 1.8 per cent in 1994 and 2.5 per cent in 1995. This is a significant development not only for Bulgaria, but for other central European countries in transition. In most of these countries the economy picked up even faster during this period than in Bulgaria, reflecting the uneven progress of market reforms and differences in economic policies (table 10). The 1994 upturn marked a long-awaited reversal of recessionary trends, which had dominated the country since the transition started.

TABLE 10
Economic growth in selected European countries in transition, 1992-1996
(in per cent)

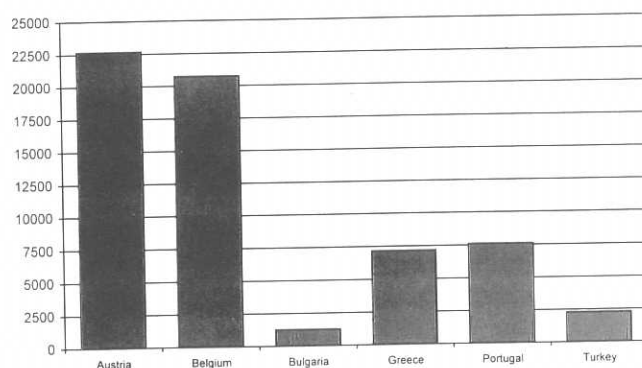
Country	1992	1993	1994	1995	1996 (forecast)
Bulgaria	-7.3	-1.5	1.8	2.5	3.0
Czech Republic	-6.4	-0.9	2.6	5.2	4.8
Poland	2.6	3.8	5.2	7.0	5.5
Romania	-8.8	1.5	3.9	6.9	4.5
Slovenia	-5.4	1.3	5.3	4.8	5.0

Source: *Economic Survey of Europe in 1995-1996*, UN/ECE, 1996.

At the same time, it should be noted that the level of Bulgarian GDP per capita is considerably lower than in the market economies of western Europe (fig. XI).

FIGURE XI

GDP per capita according to 1993 prices and US\$ exchange rate



Source: UNDP, *Bulgaria, Human Development Report*, 1995.

The expansion of the private sector is believed to be the main driving force behind the recent recovery in output. However, the share of the private sector in GDP in Bulgaria was 23 per cent in 1994 compared with 62 per cent in the Czech Republic, 70 per cent in Hungary and some 50 per cent in Poland. (Source: *Economic Survey of Europe in 1994-1995*, UN/ECE, 1995.)

Inflation in Bulgaria seems to be more resistant than in some other countries in transition as a result of substantial currency devaluations and large budgetary spending, as well as increases in domestic tax rates and energy prices. Among the east European countries, only in Bulgaria was consumer price inflation in 1994 higher than in 1993 (96 per cent in 1994 compared with 72.9 per cent in 1993).

New investments and, in particular new fixed investments, are essential for economic recovery in any economy in transition and are a major determinant of its medium-term growth patterns. In the last few years, in some countries in transition (Czech Republic, Poland, Romania, Hungary) investment rose. However, in Bulgaria, investment trends declined steadily, probably because of the slow pace of reforms and the high level of uncertainty, which is an indicator that economic recovery in Bulgaria might not be sustainable (table 11).

TABLE 11

Investment in selected countries in transition
(annual percentage change)

Country	Gross capital formation			
	1992	1993	1994	1995
Bulgaria	-11.0	-20.2	-10.1	..
Czech Republic	-17.6	-2.2	22.1	34.7
Hungary	-21.7	35.5	16.3	..
Poland	-13.0	14.9	9.0	..

Source: *Economic Survey of Europe in 1995-1996*, UN/ECE, 1996.

2. Investments in housing

One of the key factors in raising the capacity for growth-with-employment is the rate of fixed investments, in particular in the construction sector of the economy (including housing). However, housing was clearly given low political priority in the transition strategy of the first democratically elected Government. Before transition, the housing sector was the third largest item in national budget expenditure (after education and

health). In 1995, housing was last but one (before the item on culture). The share of housing in total investment declined from 13.0 per cent in 1980 to 8.7 per cent in 1991 and 5.0 per cent in 1993 (table 12). In western European countries investments in housing constituted some 20-30 per cent of total gross fixed capital formation in 1990-1995. The collapse of housing construction is clearly evident within the general decline of the construction industry.

TABLE 12
Investment in housing in some central
and east European countries
(as percentage of total investment)

Country	1980	1991	1993
Bulgaria	13.0	8.7	5.0
Hungary	17.8	22.3	14.8
Poland	20.9	27.8	22.2
Romania	9.3	10.1	5.9

Source: Annual Bulletin of Housing and Building Statistics for Europe and North America, 1995, UN/ECE.

In 1993 the value of total outstanding *housing loans* was only 1.85 per cent of all debts to commercial and public financial institutions. The data on new credits for housing purposes in 1993 confirm the low financial activity in the housing sector.

Private sector investment activity has suffered a heavier decline than the public sector, in a country where individual housing construction was much more prominent before the transition period in comparison with other countries in transition.

TABLE 13
Total investment in housing as share of GDP, 1990-1993

	1990	1993
Housing investment	1.5 per cent	0.8 per cent

Source: NSI, Statistical Yearbook, 1991, 1994.

TABLE 14
New housing credits, 1993

Housing credits as share of total new credits	2.4 per cent
-----------------------------------------------	--------------

Source: The Indicators Programme, "Central-East European Regional Housing Indicators", Hungarian Metropolitan Research Institute (MRI).

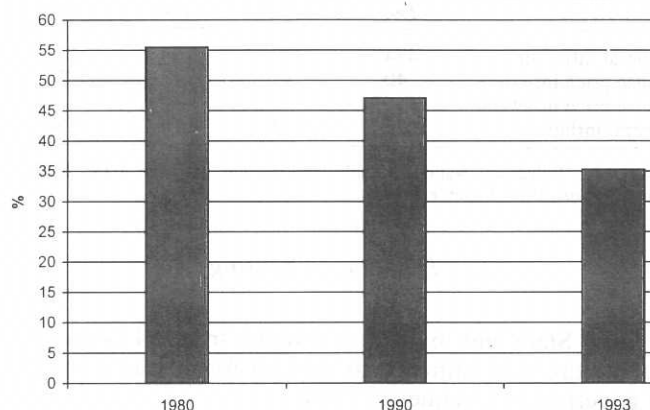
TABLE 15
Private investment as share of total investment
in dwelling construction, 1980-1994

1980	1990	1994
48 per cent	49 per cent	30 per cent

Source: The Indicators Programme, "Central-East European Regional Housing Indicators", Hungarian Metropolitan Research Institute (MRI).

FIGURE XII

Housing as share of total output of the construction industry,
1980-1994



Source: The Indicators Programme, "Central-East European Regional Housing Indicators", Hungarian Metropolitan Research Institute (MRI).

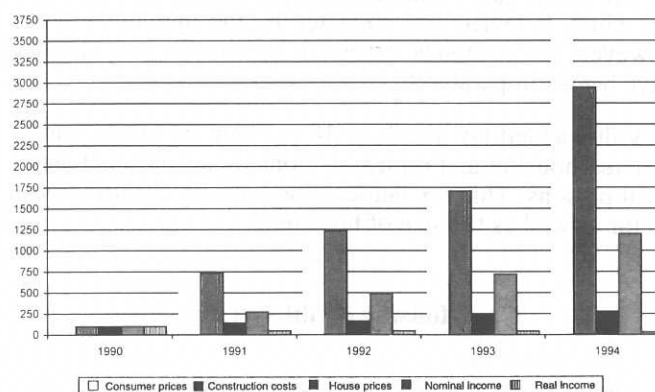
B. Housing economics 1980-1994

1. Housing and inflation

The high inflation during the transition period has been accompanied by a rise in nominal income. The gap between income and prices has, however, grown continually since 1990. Real income has not kept pace with construction costs and house prices. Real income, which was low even before 1989 in comparison with the industrialized countries, has fallen sharply during the transition (fig. XIII).

FIGURE XIII

Consumer prices, construction costs, house prices
and nominal and real income per capita, 1990-1994^a



Source: The Indicators Programme, "Central-East European Regional Housing Indicators", Hungarian Metropolitan Research Institute (MRI).

^a All indices based on yearly recorded change (31.12-31.12).

The increase in house prices is below general inflation. This decrease in the real value of housing makes private investment in the housing sector unattractive in the short and medium term (table 13).

TABLE 16

General inflation and inflation of house prices, 1990-1994

	1991	1992	1993	1994
General inflation	474	79	64	122
House price inflation	40	17	42	20
House price inflation/ general inflation	0.08	0.22	0.16	0.66

Sources: Bulgarian National Bank, *Information Bulletin 1/19*. SSB, *Annual Report*, 1994. Expert estimates.

2. Taxation on housing

Total State and municipal revenue from all types of income tax was estimated to account for 0.5 per cent of all government revenues in 1994.

Both central and local government imposed only property tax and transfer tax on housing consumption in 1994. New constructions are exempt from property tax for the first five years.

TABLE 17

Average property tax rate for a housing unit, 1993

	National	Sofia
Average property tax (leva)	270	320
Average price, housing unit (leva)	625 000	975 000
Tax rate	0.04 per cent	0.03 per cent

Source: Real estate agencies, expert estimates.

The Income Tax Law provides for the taxation of rents derived from real estate. If the claim that a large part of the rent is paid under the counter is true, this means that it cannot be taxed.

The Local Taxes and Fees Act provides for a building tax which is levied and collected by the municipalities, however the revenues received by the municipalities have been comparatively small.

Value added tax stands at 18 per cent on newly constructed housing and on transactions by all physical and legal persons. This tax burdens the housing construction sector as well as the sale of housing.

C. Housing credit systems

Although all commercial banks in Bulgaria are legally able to undertake housing financing, in practice none have so far done so. The pre-transition monopoly of the State Savings Bank (SSB) in housing financing is, in effect, still in existence. The SSB itself believes that it covers 95 per cent of the housing construction market and 100 per cent of mortgage lending.

Given Bulgaria's present income situation, interest rates, mortgage instruments, construction costs and house prices, few households can afford loans covering

any significant proportion of housing costs. The bulk of the extremely low private investment in housing is provided by household savings. Such new production is promoted by private landowners in collaboration with small private developers.

The only existing mortgage instrument is an annuity credit offering a loan with a fixed rate of interest, fixed period of repayment and equal instalments. At the end of 1994 the principal conditions for such mortgages from SSB were:

- (a) Maximum credit: 70 per cent of total investment;
- (b) Rate of interest:
 - (i) If borrower has a long-term bank deposit: 72 per cent p.a.;
 - (ii) If borrower has no long-term bank deposit: 77 per cent p.a.;
- (c) Maximum period of repayment: 20 years;
- (d) Maximum monthly instalments: 50 per cent of monthly household income.

On these conditions the purchase of a flat costing 430,000 leva with a maximum mortgage loan would require a monthly repayment of 13,536 leva. The necessary household income per year to repay this mortgage would be:

- If repayment covers 20 per cent of gross income: 812,160 leva;
- If repayment covers 30 per cent of gross income: 514,446 leva;
- If repayment covers 40 per cent of gross income: 406,080 leva;
- If repayment covers 50 per cent of gross income: 324,864 leva.

Since national average household income stood at 116,754 leva in 1994, it is not surprising that only 5,557 private clients applied for housing mortgages that year.

1. The mortgage loan situation

The available statistics on mortgage loans during the period of transition from 1991 to 1994 show clearly the sharp decline in the private sector's use of this only available credit facility for housing purposes (table 18).

The mortgage debts to SSB (outstanding loans) of municipalities and other public investors amounted to 4,941 million leva at the end of 1993. The lack of funds in the municipal budgets led to an increase in overdue loans from 238 million leva in 1991 to 1,778 million leva at the end of 1993. The situation worsened in 1994 to 2,559 million leva. Faced with the impossibility to continue financing unfinished public housing, the central Government has been forced to cover a large portion of public overdue loans at the end of each fiscal year. For 1994 this grant amounted to 885.4 million leva, covering the principals of all municipal overdue loans.

TABLE 18

Loans for the construction and purchase of housing, 1991-1994

		1991	1992	1993	1994
TOTAL LOANS					
Amount of granted loans	million leva	981	1 283	912	..
Total debt (outstanding loans)	million leva	4 116	7 332	7 135	..
Overdue loans	million leva	248	721	1 831	2 628
Mortgage arrears (per cent)		6.02	9.83	25.67	..
Housing investments	million leva	2 146	2 890	2 529	..
GDP	million leva	131 058	195 000	298 934	..
Housing investments as share of GDP (per cent)		1.60	1.50	0.80	..
LOANS TO HOUSEHOLDS					
Number of granted loans		40 180	12 077	9 636	5 557
Amount of granted loans	million leva	346	194	331	240
Average amount of loans	leva	8 609	16 006	34 305	43 241
Amount of outstanding loans	million leva	64	47	32	..
Number of outstanding loans		3 370	2 995	2 194	..
<i>of which:</i>					
old housing loans, granted before 28 January 1991	million leva	..	2 323	1 515	..
Share of old outstanding loans (per cent)		..	78	69	..
Amount of overdue loans	million leva	10	24	53	68
Mortgage arrears (per cent)		..	0.79	2.41	..
Foreclosures (numbers)		509	783
LOANS TO MUNICIPALITIES AND PUBLIC ENTITIES					
Number of granted loans		116	53
Amount of granted loans	million leva	635	1 090	582	493
Number of outstanding loans		403	382	391	..
Amount of outstanding loans	million leva	..	4 337	4 941	..
Overdue loans	million leva	238	697	1 780	2 559
Mortgage arrears (per cent)		..	16.07	35.98	..

Source: NSI, SSB, *Annual Report*, 1992, 1993. Expert estimates.

2. New credit systems

Cityfund HC has recently introduced a housing saving scheme. It issues home savings bills. Each note is valid tender for the purchase of one square metre of Citycom Standard area. It bears an annual interest of 5 per cent, payable again in housing area at 31 December, and is fully secured with mortgages. The notes are fully transferable. However, this mechanism is not attractive when housing prices do not keep up with inflation.

D. Affordability of housing 1990-1994

The standard indicators on the ability of the population to bear housing costs are all very unfavourable compared to industrialized countries. Rent affordability is, however, markedly different in the public and private rental sectors. In 1994, the rent level in the public sector was only 3.4 per cent of the private market rent (table 19).

The extremely high values of the indicators above presuppose that the level of the "Excessive housing expenditure" indicator is also high, but this is not the case in Bulgaria. According to the Sample Households Budgets Survey, conducted by NSI over eight years since 1985, average household housing expenditures have not exceeded 10 per cent of average household in-

come. This proportion has changed very slightly in comparison to the huge increase in prices (over 50 times) and the decrease in purchasing power (over three times). The biggest items in housing expenditures are still utility costs. Since 1993, utilities have been charged almost at cost-covering prices. Public rents are, however, kept far below costs. The estimated real cost of 60 leva/m²/month is over 36 times higher than the average public-sector rent at 1.65 leva/m²/month. This extremely low public-sector rent, with households on average paying 1.3 per cent of their income in rent, also directly influences the standard of the housing stock, as maintenance and repairs cannot be financed through the rents and are therefore not carried out.

Repayment of housing loans is either not an expenditure item, or constitutes a negligible share of household expenses for 90 per cent of all households. For the 10 per cent of households who pay such expenses, 1993 data put this cost at about 27 per cent of household income. The average household expenditure on food, however, now takes up approximately 50 per cent of household income.

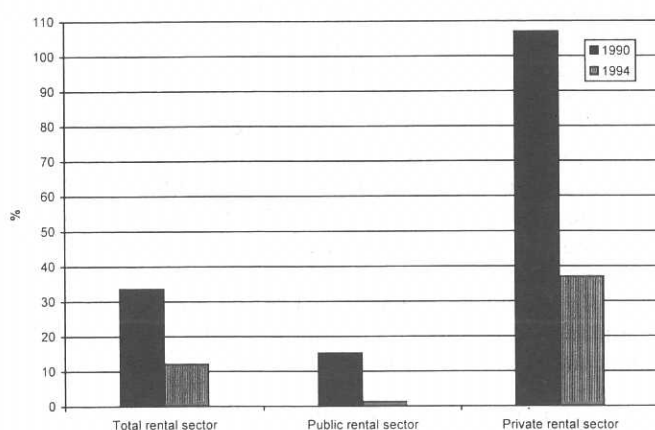
Statistics indicate that the 1992 and 1993 stability in house prices disappeared during 1994. The ratio between house price inflation and general inflation underlines, however, the real reduction in the value of housing assets. All these ratios point to the major forces of inflation in the economy being outside the housing sector.

TABLE 19
Affordability of housing, 1985-1994

	1985	1990	1992	1993	1994
Household income (leva/year)					
total	6 401	9 735	47 414	69 880	116 754
urban	6 240	9 203	43 547	65 292	105 458
rural	6 708	10 768	54 470	78 428	138 740
Sofia	6 240	9 203	43 547	65 292	105 458
House prices (leva for 75 m ² unit):					
total	21 000	243 750	397 500	562 500	675 000
urban	21 000	300 000	506 250	637 500	750 000
rural	21 000	37 500	112 500	135 000	150 000
Sofia	21 000	450 000	900 000	975 000	1 350 000
Public sector rent (leva/m ² /month)					
	0.19	1.65	1.65	1.65	1.65
Private sector rent (Leva/m ² /month)					
	2.0	11.5	33.5	42.5	48.0
Public sector rent/unit/year					
	171	1 485	1 485	1 485	1 485
Private sector rent/unit/year					
	1 800	10 380	30 150	38 250	43 200
House price/household income					
	3.28	25	8.38	8.05	5.8
Public sector rent/household income					
	-	0.15	-	-	0.012
Private sector rent/household income					
	-	1.07	-	-	0.37

Sources: NSI, "Household Budgets", sample survey, 1994. NSI, *Statistical Yearbook*, 1986-1993. SSB, *Annual Report*, 1992, 1993. Expert estimates.

FIGURE XIV
Rent-to-income, 1990-1994^a



Source: The Indicators Programme, "Central-East European Regional Housing Indicators", Hungarian Metropolitan Research Institute (MRI).

^a Data based on average rent and household income in each sector and weighted total.

The municipalities and other public bodies are responsible for the majority of outstanding mortgage loans (see table 18 above). The number of private households responsible for overdue loans has, however, risen during transition. In 1993 the mortgage arrears rate for private households was 2.41 per cent. In 1994, 783 private-sector mortgage loans were foreclosed. The reasons for the increase in arrears are assumed to be:

- Price/income index distortion 50 per cent
- Lack of subsidies 30 per cent
- "Bad" loans 15 per cent
- Inefficient claims system 5 per cent

E. Subsidies and allowance systems

Bulgaria has not, as part of the transition process, introduced any form of coherent system for housing subsidies or housing allowances. There are a few individual subsidy elements at central government level, but these do not belong to any standard type of subsidies, nor can they be considered part of a system based on clearly expressed political goals of a social or economic character.

In 1994, 1.19 per cent of the total State budget was clearly earmarked for housing sector subsidies. These were in effect not subsidies; the Government covered the overdue mortgages for unfinished municipal housing schemes.

There is at present no direct public subsidy or allowance system in the housing sector for households with below-average income. The most significant indirect housing subsidy is the rent level of public-sector rental housing, with rents at 1-2 per cent of household income but real costs to the municipal landlord 30-40 times

higher. This is, however, a general subsidy. It does not correspond to a conscious political decision in terms of volume or target.

As the price of utilities for housing has been raised to cost levels, there is no hidden subsidy in these items of total housing costs.

F. Homelessness and social need for housing

There is as yet no official "poverty line" in Bulgaria. Indeed, the establishment of such a threshold would currently be of little help. The current minimum income is a useful guide. It is also a basis for the social assistance programmes. The social and minimum living standards can also be used as guides about absolute impoverishment. Their values are calculated on the basis of a "consumer basket" with certain quantities of goods and services. Over the past four years, the number of people with income below the *minimum social standard* has grown to more than four fifths of the population (88 per cent) and the number of people with income below the *minimum living standard* to two thirds of the population (67 per cent).

The Rent Act and the recently adopted Regulation for the allocation of municipal housing lay down the

eligibility criteria for social housing. The basic criteria include the following restrictions:

- No ownership of any dwelling anywhere in the country, or any other personal assets above a certain value;
- The market rent for an adequate available dwelling must be higher than 30 per cent of the disposable household income;
- Bulgarian citizenship; and
- Having been registered in the specific local area for the last four years.

The local governments are still responsible for maintaining and updating waiting-lists for housing. In 1992 they contained 323,524 households (109,959 in Sofia). After the adoption of a stricter set of eligibility criteria and the updating of the waiting-lists in 1994, this number was drastically reduced. Now no more than 89,000 households could be regarded as officially waiting for social housing.

Homelessness is neither officially acknowledged, nor monitored. Some local governments have taken the initiative to convert abandoned non-residential properties into shelters for homeless people, relying entirely on their own resources and sponsorship from local business. Homeless families, who have special needs, are usually put up in vacant public housing.

Summary of core issues

The major macroeconomic indicators highlight the potential contribution that the housing and construction sectors could make to economic growth in Bulgaria. High prices for new housing and the extremely low new investment in housing have accelerated the decline in the construction industry during the transition period.

The major reason behind the collapse in new private-sector investment in housing is the large and widening gap between household income and general inflation which has developed during the transition period. A further deterrent to investment in housing has been the decrease in the real value of housing.

The lack of a functioning system for mortgage loans is worsening the situation for private households and other investors in housing. Due to the present level of inflation the available system for housing credits is inaccessible for the vast majority of Bulgarian households. The newly introduced system of home savings bills is not attractive during this phase of transition when the real value of housing is decreasing.

Although most indicators on the affordability of housing in Bulgaria have worsened significantly during the transition period, the average Bulgarian household expenditure on housing does not exceed 10-15 per cent of household income. The major part of this expenditure is the cost of utilities, which has been priced at cost level since 1993. Expenditure on food now consumes about 50 per cent of average household income.

The rent level in public-sector housing stands at about 1.3 per cent of average household income. This politically decided, extremely low rent rules out any expenditure on urgently needed maintenance and repair of the housing stock. Putting off such work also threatens the future use of those parts of the housing stock that most badly need repairing.

The present rent policy in public housing does not have a meaningful political objective with regard to social targeting. This type of general indirect housing subsidy is inefficient from a political, social and economic point of view.

The absence of a clearly defined housing allowance system is probably the single most important factor hampering a more constructive and socially just rental policy in Bulgarian housing. Such a policy of differentiated rents based on an allowance system should be introduced urgently.

The present Bulgarian policy of not explicitly recognizing the existence of homelessness and the need for social housing is contrary to the acceptance of housing as an important contributor to the quality of life. Data on the scale of these problems and policies to solve them are urgently needed.