

**József Hegedüs: Will the social rental<sup>1</sup> sector emerge as a pillar of the social welfare system in transitional countries?**

**Presentation at the workshop  
on “Options and Perspectives of Social Rental Housing in the  
Central and East European Region  
Budapest, 6-7 October**

The main statement of my paper is that the social rental sector has disappeared from transitional countries, which seriously limits the social efficiency of their housing and welfare system. The paper will consider what we can learn from the experiences of western countries taking into consideration the differences in economic development. I will give an explanation for constraints on financial, political and institutional interest in creation of a new social rental sector in transitional countries. International and national donor agencies are facing the same problems and the efficiency of their work is undermined by the lack of a well developed legal, financial, and institutional environment. As a conclusion I will call for a *joint effort* to help the development of social housing in transition countries.

The paper intends to be a provocative one in order to inspire discussion amongst researchers, politicians, consultants, national and international NGOs, etc. I will formulate the arguments with a high level of ignorance about particular details of the housing situations of different countries -- but I do it for the sake of a logical presentation of arguments and in order to provoke a productive debate. The role of the workshop is to clarify the differences and the optional strategies in social housing policy.

**I. What can we learn from the experiences of developed countries?**

1. From the 1980s, the *share of social housing in developed countries has been shrinking*, because (a) the society is becoming richer enabling more and more households to buy homes; (b) the neutrality of the housing tax and subsidy system could not be reached; (c) the lasting real estate price increase made an additional incentive for people to become homeowners. This trend, however, emerged in very different ways in the various Western European countries, because the historically determined institutional structure resisted the privatization trend (and expansion of owner occupation), e.g. in Holland, Switzerland, Austria, etc. Moreover, the trends for price increase in the European housing market varied greatly – there are important regional differences (price trends and tenure structure).

2. The **share of social housing in Europe** is around 15%; typically it does not go below 10%. However, there are countries where social housing has a smaller share, e.g. Spain, Portugal, Greece and Italy. The reason for this is partly the historical development in the individual countries (“path dependency” from the 70s), but there is a widely accepted view that these systems are socially not efficient.

3. The creation of the social rental sector in developed countries *took a long time* (30-50 years) and *cost a lot of money*, though the level of subsidy decreased over time. In Britain, it took 25 years for the housing associations to reach 10% of the total stock, and in the beginning the grant per unit was very high. In Holland, the sector (after a huge capital investment partly financed from central budget) is now financed from rents (and rent allowance) making cost recovery possible. However, there are countries, where the social rental sector even today receives a large subsidy (e.g. France.)

4. In developed countries there is a sub-social rental sector for very vulnerable and marginalized groups (“*very social housing*”). The existence of this sub sector generates serious social conflicts (social integration) and costs much more than the social rental sector in general. Social landlords typically tend to avoid accommodation of these groups unless special financial and legal instruments are used. The debate on mixed neighborhoods or priority of the needy is rooted in this conflict averse attitude of social landlords, and is well expressed in the debate between two agencies present in this conference (CECODHAS and Feantsa).

---

<sup>1</sup> The social rental sector includes both public and private rental as far as the rent is subsidized and/or the allocation is regulated.

5. To sum up: there is a need for a social rental sector in developed countries, because (a) there are situations where the owner occupied (and private rental sector) cannot provide accommodation for households, e.g. for those that cannot make rational decisions (vulnerable groups); (b) there are household situations where the social rental sector offers a solution which is much cheaper and more advantageous socially than a „forced” homeownership (mobility, etc.); (c) the housing market distortion (partly because of the speculative house price increase) makes housing for „key workers” (typically public employee whose income is not flexible to adjust to house price increase) unaffordable. There is a discussion among experts and policy makers as to what extent housing for the social rental sector is needed in a society, which depends on several factors, e.g. level of urbanization, etc. **Generally a level of 10-15% of the social rental sector seems to be acceptable.**

6. However, before adopting any social housing model in the region we have to take into consideration that these countries have a GDP 3-4 times higher than we have, and at least 80-100 years experience for institutional and legal development. Does the factor of “advantages of backwardness” work in the area of social housing?

## II. Social rental sector after transition

7. The social rental sector has basically disappeared from most of the transitional countries. It is not clear whether the exceptions (e.g. Czech Republic, Poland, and Russia) represent another model, or it is only that privatization in those countries has a slower pace. The social rental sector has become a residual sector, which concentrates the most vulnerable groups of the society. The sector is changing in terms of tenure rights, rent regulation and allocation rules, but for political reasons these changes do not seem to move towards a transparent and sustainable system.

8. In countries where restitution was possible, a new private rental sector emerged (most significant in Prague) which has become a very conflicting arena between the “windfall” private tenants and private landlords. In most of the countries the owners were successful enough in increasing rent and putting the burden on the tenants and the governments (rent subsidy). (E.g. Slovenia, Slovakia, Poland and to a smaller extent in the Czech Republic).

9. In almost each country in the region, politics (and housing policy) realized the need for social housing after mass privatization and recovery of the economy. There were several programs aimed at the increase of the social rental sector, but none of them seem to have lead to a real break-through in this area. (A frequently quoted good example is the TBS in Poland, but in Czech Republic, Slovakia, Romania, Hungary and Serbia also there were some programs with interesting, but sometimes questionable results.) The extension of the sector has been typically nominal, but what is more important, the social and financial sustainability of the new social housing stock has been very weak. The pure operation of the sector needed huge subsidies (to bridge between the difference between market rent and “social” rent), extensive tenure rights remained, allocation principles were not transparent, down-payment requirement as a pre-condition to enter the sector made an indirect regressive selection among possible tenants, and a number of negative elements (e.g. non-payment, deterioration, etc. ) emerged. (One of the main purposes of this workshop is to overview the results of the programs.)

10. The social rental sector is largely affected by development of the housing market. Housing prices in large cities (mainly in capital cities) and in popular holiday resorts have been influenced by speculative demand created by investment interests of the newly rich and international actors. Thus these prices have been very far from the internal capacity to pay – but the degree varies across countries. On these sub markets the motivation on the demand side is not necessarily housing consumption, but much more savings and speculation. This market development can lead to a price bubble in a flexible housing loan system (a case in point is the Baltic states).

(Some experts estimated apartment house prices of capital cities at 1500-2800 EUR/square meter, and household incomes at 800-1000 EUR/month, which amounts to price/income ratio equal to 9 in the case of a 60-square meter apartment– minimum twice as much as the European average ratio.)

11. Household choices among tenures (renting or purchasing) are mostly affected by the tax and subsidy systems of the housing regime. The generally held view of “cheaper to buy than to rent” has emerged as a

consequence of a housing policy with distorted, short-term political considerations, which is not exclusively an Eastern European phenomenon. Also developed countries have been struggling with the problem of a neutral housing regulation since the beginning of the 80ies, and have had some successes (e.g. in Great Britain), but have not yet managed to create one.

12. Whereas Western European countries tend to compensate the distortions in tenure structure by a systematic support to the social rental sector (rent and housing cost allowance), this practice is difficult to adopt in Eastern Europe, where measurement of incomes is unreliable due to a large share of black and gray economy. Officially reported incomes in the lowest income group are so low that an affordable rent (let us say 20% rent/income ratio) would yield very little compared to market prices (market rent and maintenance cost). Thus the difference between market rent (or cost rent) and social rent is enormous, creating an unrealistically high, unaffordable subsidy demand. Households are willing to pay much more in the private rental market; even a 40% rent/income ratio is accepted there (plus other housing costs).

„Therefore, the current situation at the rental dwelling market, due to the regulation, can be characterized by two different levels of rents, one regulated by the “price ceiling” and the other freely negotiated free-market rents. Regulated rents reach, on average, only about 1% of an acquisition price of an apartment. However, newly constructed municipal rental apartments with non-profit cost rent (3%) are “too expensive” for low income people, while rich people live often in cheap “regulated” apartments. This situation is an economic paradox! But removing of these distortions is “politically very sensitive”, this was permanently postponed. “ (Grabmuellerova, 2006)

13. Therefore directing the subsidy programs toward the owner-occupied sector, at first sight, seem to be more efficient, as a certain amount of subsidy generates more household contribution. However, the equity of distribution of public resources cannot be guaranteed, as the poorest, most needy groups with no family support do not have access to ownership subsidies. Due to increase in housing costs (first of all energy cost, and the cost of housing related services) the poorest are forced to move into worse quality housing, often into urban or village slums, which fossilizes their disadvantaged housing market position and combines it with disadvantages of other areas such as education, labor market, health, etc. (E.g. in squatter settlements completely occupied by gypsies and the poor).

14. Subsidy programs for the owner occupied sector can be efficient in rural areas, thus it can be preferred to the social rental sector, but targeting and rationality have to be guaranteed through special organizations (for example, NGOs).

### **III. Potential stakeholders of social rental programs: their interests and constraints**

15. The active participation of local governments in programs is hindered by two factors: high costs, on the one hand, and social conflicts generated by the social rental sector, on the other. In a decentralized system, high costs related to the public rental sector means that local politicians have to re-distribute resources taking away some from other politically important areas such as education, infrastructure development, etc. Therefore, even though they may be committed, the high costs of social housing are a constraint for the development of the social rental sector. (Though the situation may be different country by country.) The incentive structure of the public housing management companies (social landlords) and the political bodies of local governments could complicate the situation, sometimes strengthening the effect of this factor. Social housing policy generates social conflict between the very poor people and the lower middle class over the use of subsidies and use of “space”. Some local governments are willing to face and cope with social conflicts, but often it is easier for them to evade and “export” these problems instead. Consequently, social welfare issues (including social housing policy) should not be totally decentralized.

16. There are no NGOs in the region, in the Western European sense, because most of the NGOs are directly financed from government resources, which limits the autonomy of these organizations. (The Polish TBS is a good example, but even this type of organization is very much dependent on the municipality.) The development of the NGO sector in the region was very much influenced by donor assistance programs. However, in the future, once a neutral grant allocation system is in place and they will be able to manage housing, they could become important pillars of the social rental system.

17. Potential private investors could be a source for social housing stock. Two types of private landlords have to be differentiated: the institutional landlord and the individual one. The bottom line here is that landlords have to have trust that the risks related to the social rental sector (deterioration, non-payment, vacancy) are reasonably managed by the legal system or some public bodies. To attract these players, however, there are some challenges: in addition to the high costs mentioned earlier and having to handle “difficult households”, a further one is to deal with the rampant tax evasive attitude characteristic of the private rental market sector.

18. The construction industry is typically very interested in the expansion of the social rental sector as it means for them a secure (sometimes soft) market for their product. However, the political decision makers should not exclude rental options that do not generate new construction (e.g. the use of existing but vacant privately owned flats.) In Hungary, the Society for Housing Construction is one of the most active proponents for social housing programs – based on new construction.

19. The banking sector has a vital role in financing the social rental sector as the “pay as you use” type of financing (that is loan financing) could set the rent at a real cost level making the expansion of the sector possible. (The rent for houses financed from grants can lead to an unrealistically low rent.) Moreover, banks are interested to produce products which enjoy state support, and not necessarily regressive types. (Example of the role of the Bausparkasse in housing renovation.)

20. Organizations supporting national and international housing programs may play an important role. There are programs aiming to enlarge the social rental sector, such as UN-Habitat’s program in Serbia, Austrian and Dutch NGOs, HOLCIM Foundation in Hungary (though the latter one does not have a technical assistance component), etc. Programs of the Council of Europe Bank may also be significant, but these do not only limit their activities to social rental housing. The housing policy of the EU may also have an important impact. International organizations may affect current processes, but cooperation should be increased among them, because, at the moment, each organization focuses on meeting their own criteria for success (and occasionally on the interests of some lobbies behind them). In order to successfully implement their programs, they make some compromises, which decreases the impact of the programs.

#### **IV. Recommendations**

21. National governments should have a long-term vision of needs for social rental housing and its institutional structure. A clear political will across parties is an inevitable condition for a long-term policy. However, a long-term solution cannot be envisaged without an efficient housing finance system, where the majority of households can afford access to owner-occupied housing.

22. The cost of the social rental sector should be calculated both in terms of the subsidy and tax system in the whole housing sector and in terms of expected social benefits. Hidden indirect cost and liabilities do help social housing policy only in the short run.

23. Distinction should be made between a narrower area (“very social housing” or “supportive housing”) where housing should be supplemented by social work and a wider one, which includes the “non-profit” social rental sector. (Supportive housing is affordable housing with on-site support service.)

24. It is important to provide and guarantee financial incentives for institutions entering the social rental sector meaning compensating for some macro or micro economic conditions (e.g. tax evasion or distorted tax and subsidy system). Legal and social measures have to be introduced to decrease the risks of the sector.

25. The social rental sector should be monitored. Legal regulations and financial measures should be continuously revised according to the experiences in the system.