Public housing organisations in Germany: Public Interest or Private Interest?

By Stefan Kofner

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The German housing market differs in many respects from its British counterpart. The dominant type of tenure is private renting and the German homeownership rate is very low by international standards. A public interest type of suppliers akin to the British housing associations existed only until 1990. The remainders of the former public interest sector are housing co-operatives and public housing organisations. It is interesting to have a closer look at these organisations in terms of legal status, competitive environment, corporate finance and privatisation pressure.

The role of public housing organisations in Germany

The German public housing organisations of our day are mostly council owned and are subject to statutory territorial restraints for their business activities. The structure of their portfolios is still shaped by their historical role as social housing (Western Germany) or people-owned (Eastern Germany) housing providers. Their stock usually contains a large part of multi-storey buildings, often situated in larger settlements at the outskirts of the cities. Some of these settlements are focal points of social problems.

The share of the public landlords in total housing supply (including owner-occupied dwellings) is about 8 per cent. Their market share in the rental market alone is 13,4 per cent. All in all they hold around 3 million dwellings.

The public housing providers do not have a specific legal form or regulation. Their public owners are free to choose the legal form from the corporate law menu. ...

The business mission of the German public housing companies is ambiguous between public interest (= social return) and profit maximization. ...

The business mission of an individual organization depends on the local housing market and the local political situation. ...

The scope of the business activities of public housing companies is limited by financial restraints. Whilst their access to debt capital is limited by their own creditworthiness for the most part, they have usually no access to outside equity capital because their public shareholders are not able or willing to inject new capital in their holdings. Some heavily indebted communities are even trying to skim off liquidity. The organisations are thus restrained in investing, especially in new developments. Several public authorities have already sold their housing stock to private investors including the public pension insurance, the German railway and cities – like Dresden – in need of cash to re-balance their budgets. Merger activity between public housing organizations is still limited however.

The role of financial investors

A small group of financial investors (e.g. Fortress and Deutsche Annington) has built up large risk-dispersed housing portfolios by acquiring housing portfolios from the public sector.

GAGFAH S.A., a PLC under Luxembourg law acting as a holding company (listed on the German stock exchange) for the German housing companies GAGFAH, NILEG and WOBA taken over by the Fortress Private Equity Group is a case in point.

Private equity groups promise their investors to achieve rates of return between 10 and 15 per cent after inflation and taxes. Needless to say, with housing, such rates can only be attained with active portfolio management and surely not by simply "buying and holding".

The Gagfah group has incited loads of bad press in recent years. Numbers for their annual reports indicate when benchmarked that the Gagfah neglects maintenance and have almost stopped to modernize its housing stock. On the other hand the company has distributed high dividends per share even in years of loss. The case of the Gagfah has given rise to doubts whether an important market share of financial investors in the housing market is a good idea.

Efficiency

And what about the comparative efficiency of public housing providers? Both a study of Technical University Dresden and an analysis by Deloitte and Touche management consultants conclude that there are no significant efficiency differences between municipal and private housing companies.

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The future of public housing in Germany

The basic problem of the public housing companies is their limited access to investment capital. Because of this financial restriction they seem to be predestined for a passive rather than an active role in urban development, hence more demolitions than new developments. Further privatizations and mergers can be expected in the future, especially in cities with budget problems.

Professor Theo Kötter from Bonn University believes however that a municipal housing stock is an indispensable tool for a socially responsible urban development. Private providers would deliver social return only if specifically tailored subsidies were handed out to them. With a local housing stock these processes could be managed more efficiently in his view.

An important question in this context is whether the council-owned companies are adequately controlled for the fulfillment of the task to deliver adequate social return. To ensure this, the respective objectives must be concretized in their statutes (raising questions of measurability of these benefits by key figures). Also, the relevant institutions in the corporate governance system of public companies should review their compliance.

All in all, it seems to be more practical for local authorities and more effective if they could work together with major market participants in a cooperative relationship. This is particularly true on issues of urban redevelopment and demolition. The necessity of owning a large housing portfolio might be assessed differently depending on the local housing market situation.

Ultimately the question of the optimal type of supplier is a problem of institutional economics. ...

The author: Stefan Kofner is a German Professor for housing policy and housing finance. He is also a board member of a public housing organisation. Stefan was invited as an expert to the consultation of the Financial Committee of the German Parliament (Deutscher Bundestag) on the draft bill for the German Real Estate Investment Trusts held on the 28th February 2007 in Berlin. He is a member of the CIH and of the coordination committee of the European Network of Housing Research ENHR.