

BUILDING SAVINGS AND GOVERNMENT BONUSES

Ing. Peter Oravec

In the light of the frequent changes in the amount of the government bonus payable to building-savers, it should certainly be interesting to have a closer look at the system of building saving in the Slovak Republic.

From the point of view of savers, the popularity of building saving lies, first and foremost, in:

- The advantages of building saving. In 2001, for example, the rate of return on deposits at building savings banks was more than 10%, which means that building saving is an appropriate form of saving for the solution of housing problems and is accessible to the lower income groups of households as well

- Access to building loans. According to building-savers, the greatest advantage of building saving is the possibility of obtaining an advantageous building loan for housing purposes, at a constant rate of interest, independent of interest rate fluctuations on the financial market. If a home-saver decides to use the savings for other purposes, he is entitled, after a period of six years, to use the savings, including government bonus and interest, for any purpose. In spite of this, almost 90% of building-savers use their savings to buy some form of housing.

- Safety of building savings deposits. Under Act No. 118/1996 Z.z. on the protection of bank deposits, deposits at building savings banks are insured up to an amount 40 times the average monthly wage in the SR, which is an adequate guarantee of deposit protection for the customers of building savings banks.

Apart from being an advantage to building-savers, building saving is also beneficial from the macro-economic point of view:

- The funds of building-savers are tied up by government bonuses. In 2001, Sk 1 billion granted in the form of government bonus tied up as much as Sk 9.8 billion in building savings deposits, interest, and building loans. These funds are used predominantly for the construction and/or reconstruction of flats and houses. Government bonuses flow back, in large part, into the State Budget in the form of tax payments (VAT, income tax).

- Building saving leads to the accumulation of funds. Building saving contributes directly to the accumulation of household savings, reduces consumption, and thus has a positive effect on inflation as well.

- Another significant aspect is the stabilisation and creation of new jobs, particularly in the construction sector.

The housing policy of the Government

The basic documents specifying the objectives of the Government on the housing front are:

- The concept of housing development and construction, approved by the Government of the SR in Resolution No. 1026/1999;

- Concept of housing policy for the period until 2005 with an outlook until 2010, approved by the Government of the SR in Resolution No. 355 of 24 May 2000;

- Action plan for housing development and construction for the period until 2005.

According to the first of the above concepts, building saving is one of the three components of the system of housing finance based on long-term loans. Building saving is the oldest and most stable form of financing available to housing development. The Building Savings Act of the Slovak National Council (No. 310/1992 Zb.) was passed as early as 6 May 1992. Building saving can be characterised as financing at constant interest rates, independent of interest rate fluctuations on the financial market, with government support in the form of bonuses granted to home-savers.

Furthermore, the system of building saving introduced in 1999 has made it possible for building-savers (natural persons) to obtain building loans and intermediate loans with a maturity of up to 18 years, at an interest rate of 6%. After the expected entry of Slovakia into the European Union, the financing of housing construction will, in all probability, be dominated by mortgage lending; building saving will function as a form of supplementary finance and the participation of the State in the system of building saving via state subsidies is expected to diminish.

Furthermore, the concept lays down that the Government should, with regard to the country's economic situation and the possibilities of citizens, allocate a much greater amount of funds for housing construction in the transition period, up to 2005. In that peri-

Tab. 1 Number of flats under construction and completed in 1994 – 2002

	1994	1995	1996	1997	1998	1999	2000	2001	2002
Number of flats under construction	3 809	6 541	6 443	12 844	16 857	11 168	9 884	12 128	14 607
Number of flats completed	6 709	6 157	6 257	7 172	8 234	10 745	12 931	10 321	14 213



Tab. 2

Method of finance	1992 – 1998	2005	2010
Mortgage lending	3 %	39 %	71 %
Building saving	52 %	39 %	20 %
State Housing Development Fund	45 %	22 %	9 %

od, building saving should also be supported by the State Budget in the form government bonuses. In the years 2000 to 2010, all three systems of funding (including own finance) are to be applied in the finance of housing construction. The expected changes in the structure of financing are shown in Table 2.

Funds from building savings banks are expected to play a significant role in the financing of housing construction. According to data from building savings banks, their volume from 2000 to 2010 is expected to range from Sk 6.7 billion (in 2000) to Sk 9.9 billion (in 2010). In accordance with the latest amendment to the Building Savings Act, according to which corporate entities may also participate in building saving (but without a claim to government bonus), funds from corporate entities are expected to reach Sk 2.6 billion to Sk 4.7 billion.

According to the second of the above housing policy concepts, the instruments applied for the support of housing development must be modified according to the individual forms of housing construction, intended for the relevant income groups of the population. Building saving with government support is one of the forms of finance used to build flats for sale in apartment buildings and family homes for households with average income. Building saving without government support is a form of financing the construction of rented flats in privately owned apartment buildings and flats for sale in buildings or family houses, for the highest income groups of the population. Building savings can also be used for the reconstruction of the existing housing.

The second concept assumes that government bonuses will be paid to building-savers from the State Budget until the year 2005. With the gradual stabilisation of the economy, however, the share of funds invested in housing construction by the State is expected to fall steadily and that of mortgage financing to increase to an appreciable extent, with state support being gradually reduced and/or cancelled as an interest rate bonus on mortgage loans, placing long-term demands on the State Budget. Funds from building savings banks are expected to become only a supplementary source of finance for housing construction (with corporate entities also allowed to participate in building saving).

After assessing the feasibility of these concepts at a meeting in July 2002, the Government stated that, over the past period, a system of

instruments had been created for the support of housing development, enabling the Government to provide and combine various forms of state support, according to the building-saver's income. The Government also said that building saving was the oldest instrument available for housing finance with unchanged interest conditions, independent of interest rate fluctuations on the financial market, and had made a significant contribution to the finance of housing construction and the reconstruction of the housing fund in particular (roughly 75%). The Government acknowledged that the creation of resources and people's interest had been negatively affected by the frequent amendments to the law (in 1996, 1999, and 2000), reducing the government bonus from the original 40 to 25%. Similarly, the maximum amount of annual deposit used in the calculation of the government bonus had been changed from Sk 6,000 to Sk 4,000, with effect from 1 January 2002.

The government bonus

In the following period, the trend of frequent amendments to the Building Savings Act continued. In November 2002, another amendment to the Act introduced a further cut in the government bonus, from 25 to 20% of the annual deposit, with effect from 1 January 2003. At the same time, the State Budget Act for 2003 reduced the maximum amount of the government bonus granted to a building-saver from the State Budget, to Sk 3,000. Such changes tend to have a negative effect on building saving.

For comparison, we may refer to the example of the Czech Republic, where the government bonus granted to building-savers has not changed since the enactment of the law on building savings in 1993. The government bonus amounts to 25% of the annual deposit, but to no more than CZK 18,000 (this means that the maximum amount of government support is CZK 4,500 in the CR).

At present, another amendment is being prepared to the Building Savings Act, in which one of the principal changes proposed is a further reduction in the government bonus, from 20 to 15% of the annual deposit. This proposal is explained by a further fall in the interest rates of the National Bank of Slovakia and subsequent changes on the financial market, and which should be reflected in the amount of the government bonus. Interest rates on time deposits at banks are substantially lower than the effective rate of interest on deposits at a building savings bank (including government bonuses). Thus, the

Tab. 3 Government bonuses granted in 1993 – 2003

	1993 – 1996	1997 – 2000	2001	2002	2003	07/2003
Government bonus in %	40	30	25	25	20	15 *)
Maximum amount in Sk	6 000	6 000	4 500	4 000	3 000	3 000
Annual deposit	15 000	20 000	18 000	16 000	15 000	20 000

*) According to the draft of a new amendment to the law.

government bonus is seen as a form of interest rate improvement, designed to make building saving more attractive to building-savers than the standard deposit rates at banks (current or time deposit accounts, passbooks, etc.) and to motivate people to accumulate funds for the extension, reconstruction, and improvement of housing.

We, however, do not think that the primary and sole function of a government bonus is to improve the rate of interest on building loans and so motivate households to set aside funds for building saving. Until the effective rate of interest for building savings deposits is higher than the rate for standard deposit products, certain sections of the population will continue speculating in building saving, with the intention of improving their financial situation without actually solving a housing problem.

The basic function of a government bonus is to promote housing construction (including reconstruction, home improvement, etc.), i.e. to provide funds from the State Budget for the construction of flats and houses. The question whether housing construction should or should not be backed in this form by the State, is also justified. If the Government decides to continue supporting building saving (in the above mentioned housing policy concepts for the period until 2005, the answer to this question is positive), it is necessary to realise that the current level of state support for building saving (max. Sk 3,000 per building-saver per year) is inadequate with regard to the costs of housing construction and represents no real motivation for building-savers. The government bonus should represent a real help for people trying to solve their housing problems, and should not be simply an interest bonus for anyone who wants to save money. This problem, however, cannot be resolved through permanent changes in the amount of the government bonus.

We should keep in mind that a considerable portion of the government bonus flows back into the State Budget in the form of tax payments (VAT, income tax). For illustration, we present a table containing a comparison of state contributions to building savings in the form of government bonuses with the total amount of funds channelled into housing construction through building savings banks (Tab. 4).

The frequent and abrupt changes in the government bonus also fail to help to stabilise the financial market. In the interest of building-savers as well as financial market stability, the level of the government bonus should remain

Tab. 4

Sk billions

	1999	2000	2001	2002
Total amount of government bonuses	2 500	2 600	2 536	2 850
Funds provided for housing construction through building savings banks	21 748	18 961	18 166	18 808

in unchanged, at least over the period of the given year.

In 2001, government support for housing construction was extended to new forms – subsidies for the construction of municipal flats, technical infrastructure, and for the elimination of systemic defects in apartment houses; schemes to support housing construction via the provision of bank guarantees for loans. In spite of this, building saving has maintained its dominant position within the system of housing finance. In 2001, more than two thirds of all funds invested in housing came from building savings banks. The share of mortgage finance is steadily increasing, while that of building saving is on the decline.

The proportion of total state support for building saving in the form of government bonuses in relation to other forms of state assistance, is relatively stable. Table 5 shows that the relative share of state contribution to mortgage lending in the total amount of state support for housing, is on the increase.

Tab. 5 Financing of housing in Slovakia as a share of total spending on housing

	1992 – 2000	2001
Building saving	81 %	67.4 %
Mortgage lending	5.8 %	17.9 %
State Housing Development Fund	13.1 %	14.7 %

Building savings banks

At present, building saving products are offered by three building savings banks in the Slovak Republic. The First Building Savings Bank, plc. (Prvá stavebná sporiteľňa, a. s.) was established on 15 October 1992 and commenced operations on 16 November 1992, as the first building savings bank in Central and Eastern Europe. VÚB Wüstenrot, plc., was founded on 26 May 1993. ČSOB Building Savings Bank, plc. (ČSOB stavebná sporiteľňa, a. s.) was set up on 8 November 2000, and commenced operations on 1 December 2000. Basic data on

Tab. 6 State contributions to individual forms of housing finance (in millions of Sk)

	1999		2000		2001		2002 *)		2003 *)	
	Sk million	in %	Sk million	in %	Sk million	in %	Sk million	in %	Sk million	in %
Building saving (government bonus)	2 500	67.6	2 600	48.1	2 536	47.8	2 850	48.8	2 670	46.8
Mortgage lending (state contribution)	0.013	0	13.64	0.3	73.6	1.3	226.5	3.9	490	8.5
State Housing Development Fund	1 200	32.4	2 790.7	51.6	2 700	50.9	2 762.8	47.3	2 550	44.7

*) According to the State Budget for the given year.



the activities of these institutions are presented in the tables below.

References:

1. Concept of Housing Development and Construction.
2. Concept of the Government's Housing Policy until 2005 with an Outlook until 2010.
3. Action Plan for Housing Development for the Period until 2005.

4. Report on Fulfilment of the Government's Housing Policy Concept until 2010 and the Action Plan for Housing Development until 2005.
5. State Budget of the SR for 2003.
6. Annual reports of building savings banks for 2001.
7. TASR, SITA, Trend, Pravda, Economic Journal.
8. www.finance.gov.sk

Tab. 7 Comparison of basic data on building savings banks for 2001

	First Building Savings Bank (PSS)	VÚB Wüstenrot	ČSOB Building Savings Bank
Number of new contracts	295 525 ¹⁾	90 131 ²⁾	61 849 ³⁾
Target amount in new contracts	58.4 billion ¹⁾	15.2 billion ²⁾	12.1 billion ³⁾
Total number of contracts	862 734	209 598	x
Total volume of target amounts	187.5 billion	33.4 billion	x
Number of building loans and intermediate loan provided	36 627 ¹⁾	13 511 ²⁾	836
Volume of loans, intermediate loans, and funds provided for housing purposes	12.8 billion ¹⁾	5.1 billion ²⁾	0.3 billion ³⁾
Government bonus provided	2.3 billion	0.6	x
Deposits by building-savers per annum	10.19 billion	3.15 billion	1.28 billion ³⁾
Building Savings Fund as at 31 December	26.4 billion	8.8 billion	x
Balance total	42.7 billion ⁴⁾	10.9 billion ⁵⁾	2.0 billion ³⁾
Own capital	2.3 billion	1.2 billion	0.6 billion
Profit / loss	1.1 billion	0.8 billion	- 0.1 billion ³⁾
Number of employees	410	390	115
Market share in terms of the number of new contracts	66.0 %	20.2 %	13.8 %
Market share in terms of total target amount in new contracts	68.2%	17.7%	14.1%

x – No data is available.

¹⁾ In 2002, Prvá stavebná sporiteľňa, a.s. (PSS, a.s.) provided Sk 12.444 billion for housing purposes, in a total of 35.8 thousand loans and intermediate loans, and concluded almost 308 thousand new contracts with target amounts totalling Sk 64 billion.

²⁾ In 2002, VÚB Wüstenrot, a.s., provided Sk 5.6 billion for housing purposes, in a total of 16,789 loans and intermediate loans, and concluded 70,373 new contracts with target amounts totalling Sk 14.2 billion.

³⁾ In 2002, ČSOB stavebná sporiteľňa, a.s., provided Sk 764.3 million for housing purposes, and concluded almost 48,500 new contracts with target amounts totalling Sk 8.67 billion. The ČSOB stavebná sporiteľňa loss fell from Sk 120 million in 2001 to Sk 3.5 million in 2002; the balance total amounted to Sk 4.4 billion at 31 December 2002, and deposits from building-savers Sk 3.0 billion.

⁴⁾ At 31 December 2002, the balance total of PSS, a. s., amounted to Sk 43.8 billion.

⁵⁾ At 31 December 2002, the balance total of VÚB Wüstenrot, a. s., stood at Sk 9.6 billion.

Tab. 8 Number of new contracts and volume of target amounts

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
First Building Savings Bank (Prvá stavebná sporiteľňa)											
Number	55 932	151 322	183 519	299 678	267 376	129 803	148 912	195 518	238 592	295 525	308 000
Volume in Sk billions	7.51	17.63	23.07	30.88	35.80	22.54	23.18	35.68	44.82	58.43	64.0
VÚB Wüstenrot											
Number	–	22 735	33 357	42 134	71 156	27 643	33 581	43 904	68 805	90 131	70 373
Volume in Sk billions	–	3.03	5.03	6.44	9.46	3.53	5.20	7.46	11.24	15.22	14.2
ČSOB Building Savings Bank (ČSOB stavebná sporiteľňa)											
Number	–	–	–	–	–	–	–	–	x	61 849	48 500
Volume in Sk billions	–	–	–	–	–	–	–	–	x	12.10	8.67

Tab. 9 Funds invested in housing construction (in millions of Sk)

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
First Building Savings Bank	19.9	254.5	923.0	2 964.1	7 430.5	12 210.4	16 222.6	13 226.2	12 784.4	12 444.0
VÚB Wüstenrot	0.02	33.1	181.8	713.5	1 496.8	2 508.0	5 525.6	5 735.0	5 135.3	5 600.0
ČSOB Savings Bank	–	–	–	–	–	–	–	x	282.0	764.3



Tab. 10 Utilisation of building loans and intermediate loans by purpose (in %)

	First Building Savings Bank	VÚB Wüstenrot
Modernisation ¹⁾	37.0	35.1
Construction ²⁾	23.0	16.2
Acquisition, purchase ³⁾	39.9	33.1
Other forms ⁴⁾	0.1	0.4
Other	–	15.2

1) PSS, a. s. – modernisation, reconstruction, maintenance, or repairs;
VÚB Wüstenrot, a. s. – reconstruction and modernisation.

2) PSS, a.s. – construction, extensions and superstructures;
VÚB Wüstenrot, a. s. – construction of flats, houses.

3) PSS, a.s. – acquisition of flats and houses.

VÚB Wüstenrot, a. s. – purchase of flats, houses, land;

4) PSS, a.s. – other purposes related to housing;

VÚB Wüstenrot, a. s. – discharge of liabilities.