The Influence of Transition Economy Peculiarities on the Formation of Housing Price Level

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The article deals with a global problem – the influence of transition economy peculiarities on the formation of a housing price level. Real estate market takes a significant share in global economics which suggests the important position of the real estate market in global economic processes. Processes of world globalisation strengthen the links between the real estate market and cycles of overall economics. These links are less understandable and less apparent in transition economies trying to successfully integrate into the communities of market economies and catch up with developed countries. Processes in the real estate markets in transition economies have not been fully researched, and they differ from the processes of the real estate markets in developed economies with their peculiarities, possible market participants’ reactions to economic shock and outcomes for the country’s economy.

Common problems with property privatization, formation of legal and financial systems, real estate market cycle are specific and the countries with transition economy face them. Specificity of a narrower real estate market share – housing market – is determined by the need of housing market participators to procure and possess own housing unsatisfied during the period of command economy. The need for housing is constant and reflects the present level of people’s wellbeing, however, in the case of transition economies, the authors find it necessary to carry out the research to include the processes of housing market, the tendencies of housing price level formation and the impact of bank policy directions on housing market participants and a housing price level. The scientific literature has not still provided a clear answer to the question “What transition economy peculiarities are the most important and have the greatest impact on housing price level variations?”.

The aim of the work is to determine the most important peculiarities of transition economy country that have the greatest influence on the formation of a housing price level, and with this aim the authors seek to review the conditions and factors determining the formation of a housing price level in transition economies, study theoretical features and peculiarities of the transition economy country which could have an impact on the formation of housing price level, establish the main factors determining the formation of a housing price level in the transition economy country in the case of Lithuania, use the method of expert evaluation in order to verify the impact of the most important factors, typical of transaction economy, on the formation of a housing price level.

The analysis of the scientific literature proposes the conclusion that the main peculiarities determining the formation of housing price level in transition economies are targeted formation of housing market market participants’ behaviour and high money supply. The authors have revealed the connection between the formation of legislative base and tax policy as well as between bureaucratic barriers of land management and change of housing price level. They have also revealed the link between the number of real estate market participants and housing price level increase. The more speculative objectives real estate market participants have, the higher demand is stimulated and housing prices rise. The research has also shown that there is interdependence between change of housing prices and irrational behaviour of consumers. It is worth highlighting the fact that the formation of housing price level in transition economy country is influenced by a complex of different factors.

Keywords: housing market, country with transition economy, housing price level.

Introduction

Importance of the problem. Real estate market share in the global economy suggests the important position of the real estate market in economic processes of major economies, especially in the processes of financing. World globalization processes strengthen the connections between
the real estate market and general economic cycle as the connections are less transparent and clear in transition economy countries which are taking their efforts to successfully integrate into the market economy countries’ communities and reach the level of developed countries. Globalization and international competitiveness has brought a new era in the construction industry as well as in housing market (Jaafar et al., 2008; Snieska, 2008; Pilinkiene, 2009; Snieska & Bruneckiene, 2009) and become especially relevant in a real estate market in the countries with transition economy. Real estate market processes in the countries with transition economy differ from real estate market processes in the countries with developed economy in their peculiarities, possible reactions of market participants to economical shocks and consequences to country’s economy. Common problems with property privatization, the formation of legal and financial systems, a real estate market cycle are specific and the countries with transition economy face them. Specificity of a narrower real estate market share – housing market – is determined by the need of housing market participants to procure and possess own housing unsatisfied during the period of command economy. The need for housing is constant and reflects the present level of people’s wellbeing, however, in the case of the countries with transition economy a big share of new players who allow making irrational investment decisions because of the lack of historical experience and information interfere with processes in a housing market. Problematic of a housing market in countries with transition economy is enforced by international capital, increasing investment flows and favorable lending policy. The role of banks in this process is especially significant, whereas they are not only the main sponsorship mediators, but also risk sources in financial system of the country (Festic, et al., 2009; Zukauskas & Neverauskas, 2008).

While in a country with transition economy the need for housing grows, theoretical and practical researches covering housing market processes, household’s investment as well as savings behaviour (Bikas, 2008), housing price formation tendencies, the influence of banking policy trends on housing market participants and housing price level are necessary as it is very important to know what types of risk can be met and what level of risk is related with one or another investment operation (Aniunas & Nedzveckas, et al., 2009) especially in housing construction decision making (Antucheviciene, et al., 2010).

Scientific literature analyses different factor groups of housing market peculiarities in transition economy countries (Guzanova, 1997; Smith et al., 2003; Anderson, 2000; Brauers et al., 2007; Popov, 2009; etc., the list summarizing characteristics of real estate market in a country with transition economy is presented (Venclauskiene & Snieska, 2010), however there is no clear answer which peculiarities are the most important and have the greatest influence on the change of housing price level.

**The problem of the article:** what peculiarities of transition economy country are the most important and have the greatest influence on the change of a housing price level.

**The aim of the article** is to determine the most important peculiarities of a transition economy country that have the greatest influence on the formation of a housing price level.

**The object.** Housing market in a country with transition economy.

**The following tasks were set:**
1. To analyze the peculiarities of a transition economy country that could have influence on the formation of a housing price level.
2. To analyze peculiarities determining the formation of a housing price level in the transition economy country Lithuania.
3. To verify the influence of the most important factors of transition economy on the formation of a housing price level.

**The methods of the analysis** are as follows: logic, systematic analysis of scientific literature based in comparative and summary methods. The methods also include qualitative peculiarities determining the formation of a housing price level hardly based on statistical models were distinguished; Pearson’s, Cronbach’s alpha coefficients were calculated. The calculations were performed using Statistical Package for the Social Sciences (SPSS) and Microsoft Excel software package.

**The first part of the article** is based on scientific literature and deals with the theoretical characteristics of the transition economy country. The second part is based on the expert evaluations and deals with the investigation of the most important factors of transition economic on the housing price level formation.

**Aspects of Transition Economy characteristics in Housing Market**

Scientific literature suggests little about the problems of transition economies and in particular the formation of a house price level in the countries with transition economy. Some scientists draw attention to the level of house price formation characteristics in the transition economy countries (Atkinson & Micklewright, 1992; Guzanova, 1997; Lanjouw et al., 1998; Melo & Ofer, 1999; Anderson, 2000; Smith et al., 2003; Popov, 2009).

Transition period from a command economy to a market economy state creates an extra costs category for housing households (Lanjouw et al., 1998). This is confirmed by Svejnar (1991) findings on the features of a command economy in respect of the housing market: there is no legal land ownership control, regulated rent prices, which are set unreasonably low or unjustifiably high and cannot be explained by market-driven equilibrium, housing

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1 In the research the term „a country with transition economy“ is defined as a country shifting from command economy to market economy emphasizing changes in real estate market development and factors determining accommodation price level and their peculiarities during transition period.

2 The term “factors” in the present research is used to refer to specific factors, characteristic to the real estate market in the transition economy countries taking into consideration the peculiarities typical for the transition economy countries.
prices take relatively small share of consumption expenditure for most households, residential operating costs are sufficiently low, there is a significant surplus of housing demand. Relatively low share of consumption expenditure for housing can be explained by the fact that most housing is provided to employees by local governments or the employers free of charge (Palacio & Shelburne, 2005). Another feature of the command economy is the excess of labour productivity effects on the housing market (Hacker, 1999).

Many authors agree on that high money supply for the acquisition housing in transition economies is an important factor in the real estate market development (Anderson, 2000; Mihaljek, 2006; Polterovich & Popov, 2006). Renaud (1996) argues that financial reform is a major transition factor from a command economy to a market economy. The author also highlights the influence of the banks’ liberalization policy, foreign investors, with significant international experience in lending, acquisitions of country’s banks on the rapid growth housing market and level of housing price.

Emerging housing market determines the processes at national level: legal and fiscal policy development (Anderson, 2000). The foundation of the legal system is required during real estate recourse distribution for private home ownership validation and registration, changes in fiscal system for administration of new taxes of real estate.

Mihaljek (2006) draws attention to another problem in transition economies - bureaucratic barriers for the redistribution of property. This causes the housing supply deficit. The activation of liberal lending and bureaucratic land disgorge to the legal owners barriers mechanisms, a significantly increased demand and decreased supply could cause sharp increase in house prices.

Guzanova’s (1997) study showed that during the privatization process, high-quality housing demand is significantly higher in urban centres than in other parts of the city. Critical factors for the acquisition of housing during privatization process are the quality and location, but no less important are household demographic characteristics - values, education and an income level. The ensuing Anderson’s (2000) study also emphasizes the impact of district level housing prices - downtown housing price level significantly higher than in other areas during privatization.

A number of additional issues related to the privatization in transition economies were identified by Mustil (1995). He claims that in the Czech Republic, the old system was liberalized, but the basic principles and practical actions formed for the functioning of the housing market were uneven and inefficient. The author believes that the supply elasticity is the main imbalance source in the housing market. Mustil (1995) believe that the short-term supply curve during privatization is relatively inelastic, while the demand curve can be more elastic, depending on the rapidly rising prices and lack of adequate supply in the short term.

Popov (2009) suggests that the key factors that promote successful development of transition economy countries are the privatization of state-owned enterprises, foreign aid measures, immigration, liberalization of financial system, democracy of the political institutions. The author is one of the first who analyses not only the privatization of real estate but also state enterprises. Strategically important state-owned enterprises’, such as controlling country's energy economy, privatization and future energy networks formation influence the housing price level movements.

In transition economy countries, one of the prominent social aspects determining housing price movements are skilled and unskilled labour migration (Dhonte et al., 2000) and revenue changes. Labour migration rate depends on the country and its government development level (Popov & Polterovich, 2006). Increased revenues not only provide the opportunity to take a mortgage loan, but are also detrimental to economic growth in two ways: confront social groups and worsens the investment climate (Alesina & Rodrik, 1994; Alesina & Perot, 1996). This creates lobbying, rather than structural reform and macro-stability (Fernandez & Rodrik, 1991; Persson & Tabellini, 1994). Popov (2009) argues that social inequality is a consequence of economic redistribution of wealth and capital, but not their growth.

Venclauskienė and Snieska (2010) sum up and list the peculiarities of transition economy country which influence the real estate processes: 1) formation of the legislative and tax base, (2) bureaucratic barriers of land return to the rightful owners, (3) the privatization process, (4) formation of the control of the common prospective plans formulation of the area, (5) untapped potential of living space per capita (6) the expectations of joining the international community (7) the expectations of national currency change, (8) unused borrowing capacity; (9) formation of energy network, (10) targeted formation of the housing market participants’ behaviour, (11) high money supply, (12) the reduction of free movement barriers; (13) the increasing share of expenditure for housing, (14) the use of financial support instruments in order to reach the average level of the EU community.

It must be noticed, that the authors have made the list of the peculiarities of a transition economy country which was orientated to the real estate market as a whole, but the paper analyses only the narrower part of real estate market – housing market. Therefore the last peculiarity from the list (No.14 The use of financial support instruments in order to reach the average level of the EU community) is not applicable to a housing market as in the particular Lithuanian housing market case direct financial support to the housing market was not provided. However, the EU structural support and its impact of on Lithuania’s progress were significant for the development of real estate market (Tamosiuniene, et al., 2007). EU structural support was provided for other real estate types, e.g. for marshy landscapes, turning them into tourist locations, and forests, for reforestation purposes.

To sum up the results of the research, it may be concluded that the most important peculiarities of the country of transition economy (that are influencing real estate market price level changes) might be quantitatively denominated by specific factors that are characteristic of transition economies. Narrower real estate market in this context refers to the change of housing market price level.
The Indication of the Most Important Factors Determining Housing Price Level Formation in Transition Economy Country in Case of Lithuania

According to the research, it might be assumed that the most important factors of a transition economy country that determine narrower real estate market, i.e. the change of a housing market price level, could be psychological and high money supply factors. Therefore, the following hypotheses have been raised, approval or disproof of which will identify the key factors and peculiarities that have a decisive impact on the housing price level formation in the transition economy country:

Hypothesis 1: the peculiarities determining the rise in a housing price level in a transition economy country are the targeted formation of housing market participants’ behaviour and high money supply.

Hypothesis 2: there is a connection between the formation of a legislative base and tax policy and change of housing price level.

Hypothesis 3: the more speculative aims participants of the real estate market have, the more demand is stimulated and housing price rise.

Hypothesis 4: there is interdependence between change of housing prices and irrational behaviour of consumers.

The approval (disproof) of the hypothesis was assessed by expert assessment method. The expert group consisting of 70 real estate market experts were assessed questionnaire propositions by 1 (disagree) 2 ... 5 (agree) scale. The selected real estate market experts-respondents were real estate managers, real estate assessor, real estate sales agents and others whose work experience (more than 6 years in real estate market) and the qualification (e.g. real estate assessor) as well as knowledge in such areas as real estate market research, real estate brokerage transactions, real estate agency management, banking, economics, allow them to be considered Lithuania’s real estate market experts and their the views to be qualified as experts’ that hard-quantifiable tendencies of housing price level formation process were determined in the case of transition economy country.

In order to verify H1 hypothesis, the propositions were formulated: K1.1 information during the accession of Lithuania to the EU that real estate prices will increase, and disclosed examples income-generating encouraged people to invest in real estate; K1.2 publications in media might affect the behaviour of buyers and sellers of real estate in making real estate operations; K1.3 investment decision to purchase an estate is influenced more by the opportunity to get a mortgage than the market price of the estate; K1.4 estate price level in transition economy country is determined by reduced requirements for credit. As money supply is dependent on lending extent, therefore the money supply is valued through the growth of credits number for housing.

In order to verify H2 hypothesis, the proposition K2.1 was formulated: the introduction or increase of real estate tax would reduce the number of housing buyers.

In order to verify H3 hypothesis, the proposition K3.1 was formulated: housing buyers whose income allows taking a few bank loans purchase home living as well as another real estate for sale, if there is a trend of rising prices.

In order to verify H4 hypothesis, the proposition K4.1 was formulated: housing prices are affected by the level of customer expectation that the investment is profitable, which leads to enthusiasm and optimism making the investment decision.

The questionnaire that experts answered can be regarded as reliable because the calculated Cronbach alpha coefficient is 0.725. It demonstrates the reliability of questionnaires and formulated propositions’ compliance with the paper topic. The compatibility of the expert opinion is described by Kendall concordance coefficient which was calculated as 0.17. This reflects the consensus of experts on the importance of the peculiarities. Standard deviation values of expert evaluation results ranged from 0.66251 to 1.20729, which show a very good degree of dispersion of the empirical average values.

Considering the agreement of expert’s view on the diversity peculiarities determining the level of housing price, it can be argued that the housing price level is influenced by a complex of peculiarities.

Summarizing the results of expert evaluations, it can be argued that among the peculiarities determining a housing price level, the most influential are media and other channels that shapes the behaviour of real estate market participants (to proposition K1.2 experts agree by 88.6 %) and customer expectations (to proposition K4.1 the experts agreed, 85.7 %).

Comparing the expert assessments and summary in a theoretical level, similar conclusions are obtained: the main peculiarities determining the formation of housing price level in transition economy country are a focused formation of the behaviour of real estate market participants and expectations of the real estate market participants, i.e. possibly irrational behaviour or the consumers. These findings confirm the first and fourth hypotheses. 88.6% of expert-respondents agreed with the proposition (K1.1) information during the accession of Lithuania to the EU that real estate prices will increase, and disclosed examples income-generating encouraged people to invest in real estate. 61.4 % of expert-respondents agreed with the proposition (K1.3), that the investment decision of purchasing an estate is influenced more by the opportunity to take a mortgage than the housing market price. 75.7 % of the interviewed experts agreed with the statement (K1.4) that the estate price level in a transition economy country is determined by reduced requirements for credit. This confirms the hypothesis H1 that the rise in a housing price level in a transition economy country is determined by the targeted formation of housing market participants’ behaviour and high money supply.

It can be argued that the real estate market growth in Lithuania 2002-2008 can be partly explained not only the regional growth of FDI in Lithuania (Brock & Urbanavicius, 2008), but also increased investment in construction and real estate sector and favourable lending terms from banks, which were created during that period. This confirms that the main peculiarities determining the formation of a housing price level in transition economy counties are targeted formation of housing market participants’ behaviour and high money supply.
62.8% of expert-respondents agreed with the proposition (K2.1), that the introduction or increase of real estate tax would reduce the number of housing buyers. The determination of the connection allow to claim, that there is a link between legislative base formation and tax policy as well as between bureaucratic barriers to own a land and housing price change. Therefore H2 hypothesis is confirmed.

74.2% of experts agree with the proposition (K3.1) housing buyers whose income allowing to take a few bank loans purchase home living as well as another real estate for sale, if there is a trend of rising prices, and confirm that the number of speculative market participants increase attracted amateur housing market participants that has a possibility to get a loan and invest for future profits. The link between the real estate market and increased housing price level was approved; the more speculative the real estate market participants are, the more the demand for housing is exited and housing price is increased (hypothesis H3).

85.7% of experts endorsed the proposition (K4.1) housing prices are affected by the level of customer expectation that the investment is profitable, which leads to enthusiasm and optimism making the investment decision. Increased housing demand determines the increase in a housing price level, suggesting that there is a relationship between housing price changes and irrational consumer behaviour. Hypothesis H4 approved.

Summarising the results of expert evaluation, it can be concluded that the aim of the expert evaluation is achieved – hard-quantifiable peculiarities of a housing price level formation process were evaluated in the case of transition economy country Lithuania and the influence of those peculiarities on a house price level was examined.

Conclusions

In summary the following conclusions may be drawn:

1. The most relevant peculiarities determining formation of a housing price level in a country with transition economy are purposeful formation of behavior of housing market participators and a high supply of money. Growth of real estate market in Lithuania within the period 2000 to 2008 may partly be explained by increased investments into construction and real estate sectors and favorable conditions of borrowing from banks which were formed within the mentioned period. It proves hypothesis H1 stating that the most relevant peculiarities determining the formation of a housing price level in a country with transition economy are purposeful formation of the behavior of a housing price market participators and high supply of money.

2. 62.8% of the questioned experts expressed their consent with the statement that the introduction of real estate tax or its increase could reduce the number of housing buyers. This relationship allows to state that there is a connection between legal basis and tax policy under formation and the variation of a housing price level (hypothesis H2 was proved).

3. The more speculative objectives real estate market participators have, the higher demand is excited and housing prices raise (hypothesis H3). 74.2% of the interrogated experts expressed their consent with the statement that housing buyers whose income allows taking several bank loans acquire their housing for living, and one more real estate subject for sale in case prices grow purposefully, and proved that the number of housing market participators grows seeking for speculative goals; non-professional housing market players who simply have the possibility to borrow and invest seeking for profit in the future are also attracted.

4. 85.7% of the interrogated experts agreed with the statement that housing price level is influenced by the expectation of buyers that investments into housing are profitable, and it raises enthusiasm and optimistic attitude making an investment decision. Increased housing demand determines increase of a housing price level, therefore it may be stated that there is a direct dependency between the variation of housing prices and irrational behavior of consumers. Hypothesis H4 was proved.

5. The empirical research of a housing price level formation in a country with transition economy proved applicability transition economy peculiarities and their suitability for usage making investment decisions in the case of Lithuania 2000 to 2008.

References


Nekilnojamojo turto rinkos procesai pereinamosios ekonomikos šalyse ištisai išlieka išskirti nuo nekilnojamojo turto rinkos procesų globalizacijos procesai sustiprina nekilnojamojo turto ir bendrosios ekonomikos cikliškumo sąsajas, kurios yra mažai suprantamos ir aiškių perienamosios ekonomikos šalyse, besistengiantišose sektoriais integruotis į įvairias ekonomikos šalių bendrijas ir pasitvystyti įsivysčiusių šalių lygi. Nekilnojamojo turto rinkos procesai perienamosios ekonomikos šalyse nėra iki galo ištirti ir skiriasi nuo nekilnojamojo turto rinkos procesų įsivysčiusios ekonomikos šalyse savo ypatumais, galimomis rinkos dalvių reakcijomis į ekonominius šokus ir pasekmėmis šalies ekonomikai.

Bendrosios turto privatizavimosi, teisės ir finansų sistemų formavimosi, taip pat nekilnojamojo turto rinkos ciklo formavimosi problemas perienamosios ekonomikos šalyse yra specifinės. Šiauresnės nekilnojamojo turto rinkos dalies – būsto rinkos – specifikuomis iš dalies šalyje taikomą komandinės ekonomikos laikotarpio neįprastus būsto rinkos dalvių poreikius įsirūpinti ir valdyti nuosavą būstą, būsto poreikis namų ūkiams yra nuolatinius ir atspindžius įvairiausiomis ekonominiai priežasčių, tačiau perienamosios ekonomikos šalyse į būsto rinkos procesus ji laikoma didelė dalis nekilnojamojo turto rinkos žaidžių narių, kurie dėl istoties ir įvairių ekonominių stokos daro atitinkamos kokybinės investicinius sprendimus.

Nekilnojamojo turto rinkos formavimosi tendencijų suprataimas ir numatymas tampa ypač svarbus perienamosios ekonomikos šalyse, kuriose nėra susiformavusi nekilnojamojo turto rinkos teisinė bazė, tarp gyventojų yra mažai žinomi nekilnojamojo turto rinkos procesai ir nepakankamai suvokiamas jų poveikis šalies ekonomikai.

Nekilnojamojo turto rinkos formavimosi procesai pereinamosios ekonomikos šalyse nėra ištirti, tačiau gali būti pritaikyti įvairioms ekonominėms šalims, kurių ypatumai yra nekilnojamojo turto rinkos procesų įvairiūs. Nekilnojamojo turto rinkos formavimo procesai pereinamosios ekonomikos šalyse susidaro dėl įvairių priežasčių, kurios būdingos nekilnojamojo turto rinkos procesams, tačiau nėra įvairiosios šalių ekonomikų analizės. Šios priežastys gali būti panaudotos kaip lentelė, atskirti nekilnojamojo turto rinkos formavimui pereinamosios ekonomikos šalyse: 

1 hipotezė: būsto kainų augimą auginimo perienamosios ekonomikos šalyje stipriausiai veikia specifiniai ekonominiai veiksnių, kurie būdingi tik nekilnojamojo turto rinkoms. 
2 hipotezė: yra priklausomybė tarp būsto kainų kitimo ir neracionalaus vartotojų elgesio. 
3 hipotezė: yra priklausomybė tarp būsto kainų kitimo ir mokėtinių politikos įtakos. 
4 hipotezė: yra priklausomybė tarp būsto kainų kitimo ir mokėtinių politikos įtakos.