

German bauparkassen help finance nine million homes

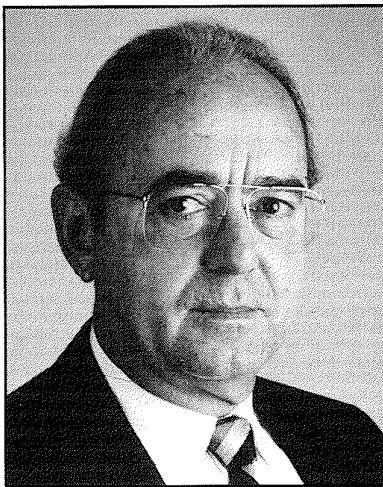
Germany's savings and loan system has been highly successful and, says Dr Otto Schäfer, could be used in developing countries

SINCE the war, Germany's bauparkassen have helped to finance more than nine million homes in the Federal Republic. During this period, they have paid out to their customers in excess of DM700 billion for the construction of new housing and the acquisition of formerly occupied housing units, as well as for modernisation and restoration work, the conversion and extension of existing housing units, and the acquisition of building land.

Today, the bauparkassen administer 24.6 million contracts representing a total contract amount of DM851 billion. At the end of 1986, the combined total assets of all 30 German bauparkassen amounted to more than DM158 billion.

Table 1
Amount paid out by the German Bauparkassen for housing construction

| Year | Amount paid out in billion DM |
|------|-------------------------------|
| 1955 | 1.6 |
| 1960 | 4.1 |
| 1965 | 9.0 |
| 1970 | 19.2 |
| 1975 | 29.9 |
| 1980 | 48.1 |
| 1985 | 44.4 |



At present, 16 million West Germans have one or more savings and loan contracts with a bauparkasse. In fact, every third person over the age of 18 is a saver with a bauparkasse.

In 1986 alone, 2.7 million contracts representing a total contract sum of DM82.4 billion were concluded, and building loans to the amount of DM41.5 billion were paid out to savers. The German bauparkassen thus represent by far the largest group of institutions involved in the financing of housing construction in the Federal Republic of Germany (see table 2). Three out of four newly

constructed housing units in individual houses are today financed partly by a bauparkasse.

A self-contained financing system

The bauparkassen's dominant position is due primarily to the particular character of the German savings and loan system for construction.

In contrast to almost all other countries, and in particular to the Anglo-Saxon countries, the German bauparkasse method of operation is

Table 2
Financing of housing construction by institutional investors¹ in 1985

| Financing institutions | Total amount paid out for housing construction | |
|--|--|--------|
| | million DM | % |
| Bauparkassen in total | 44,406 | 41.3 |
| Private bauparkassen | (29,942) | (27.8) |
| Bauparkassen incorporated under public law | (14,464) | (13.5) |
| Mortgage banks | 28,390 | 26.4 |
| Savings banks | 29,218 | 27.2 |
| Life insurance companies | 5,506 | 5.1 |
| Funds of the institutional investors | 107,520 | 100.0 |

¹Funds of the banks and public sector not ascertainable.

based on a self-contained financing system. Based on the amalgamation of savers to form a self-help community, this system is independent of the capital market and its interest rate fluctuations. The savers with a *bausparkasse* undertake a contractual obligation to make regular savings contributions to joint funds, from which they receive the amount subscribed for under the contract according to a system of priorities (allotment).

The amount covered by a contract with a *bausparkasse* is made up of the savings accumulated by a saver in the *bausparkasse* (40% to 50% of the amount covered by the contract) and the contractual building loan, i.e. the difference between the amount covered by the contract and the savings actually accumulated by the saver in the funds of the *bausparkasse*.

This type of savings and loan system is characterised by the identity of saver and borrower. The saver remains a creditor of the *bausparkasse* until he has been paid the savings he has accumulated in the funds of the *bausparkasse*, but once the building loan has been allotted to him, the saver then turns into a debtor of the *bausparkasse*.

On conclusion of the contract, the *bausparkasse* saver acquires a legal claim to a saver's building loan. The low interest rate of this loan is fixed over the entire life of the loan and is virtually unrivalled by other competitors: it may be 4.5%, 5%, 6% or 6.5%, depending on the tariff. It is totally independent of capital market developments, and interest rate escalation clauses and/or variable interest rates do not exist in the savings and loan system for construction.

Thus, anyone considering a building project has a clear basis for calculations right from the beginning. During the saving period, the savings accumulated by the saver are credited with an interest rate which is fixed at 2.5%, 3%, 4% or 4.5%, depending on the interest rate which will be charged during the loan

period.

The *bausparkasse* saver can make use of the loan — which is granted exclusively for housing purposes — as soon as he is eligible for allotment, i.e. once the following conditions have been fulfilled: the minimum savings period, the minimum savings balance of 40% or 50% of the amount subscribed for under a contract, and the qualification figure, which depends on the overall funds available.

The contractual amount subscribed for initially, which is equal to the savings at the time of allotment plus the amount of loan entitlement, is then paid out to the saver according to this time-savings system. After it has been allotted, the loan is repaid by the saver within a stipulated period.

The German *bausparkassen* offer a great variety of savings contract tariffs which differ by their interest rates as well as their savings and/or repayment rates, enabling every saver to choose a method of financing tailored to suit his own individual circumstances. The maturity of the loans varies between around 6½ and 18 years, depending on the tariff.

Comprehensive range of financing methods offered

Financing possibilities are also available to those customers who are not entitled to a loan under a savings and loan contract with a *bausparkasse* but who need the money because, for example, they have spontaneously decided to buy, restore or modernise a house or apartment.

Credit institutions offer financing facilities to such customers who require immediate access to capital. They offer to make available the funds required to accumulate the necessary amount of savings or to prefinance a savings and loan contract with a *bausparkasse* which has not yet been allotted. Such loans are currently offered at a relatively low interest rate of 6% to 7%. Moreover, they are free from redemption and are repaid out of a *bausparkasse's* savings funds once the savings and loan contract for construction has been allotted.

One of the characteristic features of the German system is that it combines various elements regarding the available methods and financing institutions, while the customer is at the same time only involved in one single, very simple procedure and will normally receive an "all-in-one" offer. Such a package comprises, for

→ 32



Apartments in Kehl, West Germany.

← 31

instance, a share of up to 45% of the "appropriate costs" of a house in the form of a fixed-interest rate loan, which is refinanced via the capital market through the issue of mortgage bonds. A further share of 25% to 30% is financed by the *bausparkasse*, and a third share of about 10% is offered by a bank as an additional loan at a variable rate of interest. The remaining funds are provided by the saver's own capital (savings accumulated by him in the funds of a *bausparkasse*). 100% loans are unusual in Germany.

All the larger groups of credit institutions — particularly savings banks, co-operative banks and commercial banks — offer such "all-in-one" packages, which include savings and loan contracts with a *bausparkasse*. In fact, a bank, a *bausparkasse*, a mortgage bank, and an insurance company are often united in one group of such institutions or have concluded an agreement for regular co-operation.

The advantage which this system of combined suppliers has for the customer is that he will only have to compile the required documents once. He has to submit only one application for a loan, and this will need to be examined only once. The customer creates only one mortgage (the very flexible "charge on land") and he often only has one contact-partner for the entire correspondence and transactions. This partner will also pay out the actual loan and undertake collection transactions at a later date. The advantage this system offers to the borrower is its flexibility and the broad choice the borrower has between:

- various methods of financing, ranging from methods based on long-term fixed interest rates to those based on variable interest rates;
- early debt clearance or loans free from redemption;
- insurance against possible risks by including insurance schemes;
- the possibility of taking advantage of all tax concessions granted for

taking out life insurance contracts as well as savings and loan contracts for construction; plus, of course, readily-available help to overcome any difficulties which arise.

State incentives

The State encourages the accumulation of capital by granting house-building bonuses or tax advantages. The *bausparkasse* saver can choose which type of incentive he prefers. He may receive a bonus of 14% (plus 2% for each child) of the savings accumulated annually up to savings of DM800 (single persons) and DM1,600 (married couples), provided that his income is below a certain level (DM24,000 for single persons, and DM48,000 for married couples).

If he meets these requirements, the saver may alternatively be able to deduct his savings instalments from his taxable income as special providence scheme expenditures. Moreover, the State encourages contractual saving activities with a *bausparkasse* under the Equity Participation Law by granting a savings bonus to workers.

Advantages of the German system

The decisive advantages of the German contractual savings and loan system for construction are to be found in the consistency of the system. This means that:

Financing through a contractual savings and loan system with a *bausparkasse* is independent of capital market developments.

The interest for the building loan is fixed right from the beginning at a low rate which hardly any competitor can match.

The builder or buyer consequently does not undertake any risks regarding interest rate fluctuations.

The financial burden is clearly calculable from the outset.

In contrast to many other coun-

tries, where high interest rates have at times brought housing construction activities to a standstill, the low interest rate on loans granted by a *bausparkasse* in the Federal Republic has helped to keep the financial burden at a justifiable level for the builder or buyer, respectively, even at times when interest rates are extremely high.

The relatively high continuity of payments made by the *bausparkassen* results in continuous development in the field of housing construction. Thus in 1981, for instance, more than 220,000 housing units were completed in owner-occupied houses or condominiums despite high capital market interest rates, which sometimes exceeded 13%.

Bausparkasse savers contribute an average of around 40% of the cost of financing their houses from their own capital funds. This relatively high share of capital funds is mainly the result of the system of accumulating savings under a savings and loan contract. The share of capital funds they can invest is significantly higher than that of persons who do not save with a *bausparkasse* and constitutes — together with the building loans granted at a fixed low rate of interest — certain insurance against risk for the saver, which should not be underestimated.

Consequently, the number of problem cases, i.e., those cases in which the builder or buyer runs into financial difficulties, is far smaller with the *bausparkassen* than with the other credit institutions. As a result, the accumulation of capital funds via contractual savings and loan schemes with a *bausparkasse* is deliberately encouraged by the State in the Federal Republic, even though some restrictions have had to be made in past years within the framework of cutbacks in public expenditure.

A sound method of financing

With the official encouragement of owner-occupied housing in Germany

GERMANY

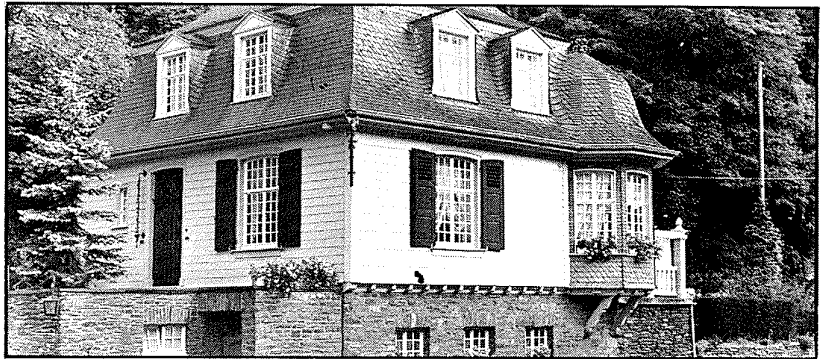
as from 1 January 1987 onwards, the Federal Government has taken a deliberate decision against the possibility of deducting interest on loans, i.e., the encouragement of the use of borrowed capital by granting tax advantages. The advantages are granted independent of the extent of outside financing. The system of the limited deduction of interest on loans which had been introduced to the Federal Republic at times in the past was merely an integrated part of an economic policy programme, which was intended to stimulate housing construction.

The encouragement of contractual saving not only provides the builder or buyer with a much sounder method of financing, but is at the same time considerably cheaper and more effective for the State than the encouragement of debt.

The prerequisite for an adequate basis of capital funds is usually the accumulation of an appropriate amount of savings over a certain period of time. On average, people who build or acquire their own house or condominium in Germany accumulate savings over a period of around seven years. The fact that the average age of buyers currently ranges between 37 and 38 years is not due to the obligatory period of saving required under the building-saving system, because many of the savers with a *bausparkasse* are young people between the age of 18 and 25 years who might very well become the owner of their own house or apartment at the age of 25 to 30 years. Quite frequently, other factors constitute an obstacle:

Since the period of vocational training in the Federal Republic is usually longer than in many other countries, many young people start to earn a reasonable income relatively late in life, and consequently also start their own family late (the average age of marriage is 30 years for men and 27 for women).

The quality requirements for owner-occupied houses or apartments in Germany are probably



Attractive family house near Aachen, West Germany.

among the highest in the world, ranking second after Switzerland. People prefer to save up more money over a longer period of time rather than be forced to compromise in their demands.

As a result of these high quality requirements, housing costs are very high compared to international standards.

In contrast to most other countries, over the coming years a large number of capital assets in Germany will be transmitted by succession for the first time since the end of the war. In future, it will thus be possible to acquire real estate more easily and at an earlier stage.

Over the past four decades, the German contractual savings and loan system has given impressive proof of its efficiency. The system requires efforts from the individual (savings accumulated), while the support granted by the State in the form of premiums or tax reliefs has to be considered as "help for self-help".

As an "integrated contract system", the German savings and loan system is also particularly well suited for the financing of owner-occupied housing in developing countries. This has been confirmed by numerous inquiries and requests for information made recently by these countries. This system might be useful for a developing country if the population is encouraged to acquire owner-occupied housing by saving up a sound amount of own capital funds rather than adopting a system under

which the builder or purchaser of an owner-occupied house or apartment is encouraged to run up high debts without having saved up any money at all. The high rates of inflation prevailing in many developing countries are by no means an obstacle to the process of contractual saving. Ways and means can be found which prevent the saver from having to "run after the prices with his saving instalments".

The experience gained by the German *bausparkassen* has shown that those who are prepared to cut down on their demands regarding consumer goods in order to accumulate a certain amount of savings are also better able to raise the financial instalments for the payment of interest and the redemption of their loans.

DM 1.99 = \$1 at end-1986.

DR OTTO SCHÄFER has been managing director of the Bausparkasse Wüstenrot since 1969. Since 1978 he has, in addition, held the post of managing director of the Wüstenrot Holding GmbH. He is a member of several supervisory boards, and is chairman of the Wüstenrot Lebensversicherungs-AG. He is also editor of the "Comment on German Law concerning the Bausparkassen". Since 1973 Dr Schäfer has been chairman of the Legal Affairs Committee of the European Federation of Building Societies and since May 1986, chairman of the board of the Verband der Privaten Bausparkassen.