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Actors of financialization in the German housing system

Marco Copercini

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Abstract

It has been shown that the German housing market, instead of not being financialized, has followed a different trajectory that has led to the current phase of financialization, characterized by the booming housing market (especially in the main urban areas) and the recent entrance in the market of private investors. This literature review shows that, while most of the studies available so far focus on specific cities, companies or practices (such as the acquisition of public housing stocks), a comprehensive analysis of the major private investor typology (listed real estate companies), their investment strategies and their effects is missing.

Keywords: financialization; housing market; private investors; real estate; urban transformation.

Parole chiave: finanziarizzazione; mercato immobiliare; investitori privati; beni immobili; trasformazioni urbanistiche.

1. Introduction

Over the last decades, the increased role finance plays in real estate directly contributes a substantial modification of the housing market, which is a market that represents both a key element for the existential stability of individuals and of the economic dynamics of regions. Housing has the function of being the basic condition for the reproduction of social and working life among individuals (Aalbers 2016; Fields 2017, 592), as without housing working and social life could not be possible the way we experience it.

Financial practices, elements and actors were identified as central elements in the modification of the housing market in almost all countries (Fernandez and Aalbers 2016), including Europe. Since this modification of the housing market, the role of housing in the market has shifted from a focus on its 'use value' (i.e. used as a place to live or for social reproduction) to a focus on its 'exchange value' (i.e. the potential value generated from its trading) (Harvey 2014). Along with this shift in focus from 'use value' to 'exchange value', the interest of financial actors, as well as financial mentality and practices enters the housing market and contributes to its redefinition.

This shift, with the related flows of capital, and the entrance of finance at several levels in the housing sector helps to amplify the socio-economic performances and disparities of regions, shape inequalities as well as determine uneven access to housing (Fields 2017). Additionally, some authors suggest a causal relation between the capital flows from other realms (including financial markets) into residential real estate and the rise in housing prices (Heeg 2013; Kesteloot 2013). From a spatial perspective, these dynamics can lead to an influx of capital flows that tend to concentrate in specific locations though in different amounts, while excluding other locations. Additionally, the concentration of capital flows in specific housing markets and locations can limit or even deny accessibility to these locations for the lower and middle layers of the population. These two aspects combined, especially if this happens in a relatively short period, stimulate a transformation both in the image and in the economic and social functions of the places where the housing sector attracts capitals flows. However, the intensity, actors and effects of this process may change substantially within different contexts.

Within this general picture of financialized housing markets, Germany presents a different trajectory from other European countries, as it is based primarily on a stable housing system and the activity of private investors as actors of financialization (such as listed companies, private equity and hedge funds), who have bought huge amounts of housing stock (including privatized social housing and the subsidized rental market, thereby contributing to a process of the privatization of the welfare state) (Holm 2010; Heeg 2013; Fields and Uffer 2014; Bernt *et al.* 2017; Wijburg and Aalbers 2017).

Set against the rise of financial capitalism and its geographical influence, the relations between housing and financialization are under-researched and under-theorized (Fernandez and Aalbers 2016), even though this gap has been recently identified by researchers of various disciplines, especially economic and financial geography, housing studies, and political economy. This paper aims to present a short literature review on the recent phase of financialization in the German housing market and on the central actors in this process: listed real estate companies.

2. The financialization of housing in Germany

The role of listed companies as financialization actors in the German housing market will be presented from different research strands in the existing literature in order to increase clarity: concept of financialization, structure and peculiarities of the German housing market, the entrance of private investors, and especially listed companies, in the German housing market and the role of these actors in its transformation.

2.1. *Definition of financialization*

Financialization is a basic term used to describe both the penetration, in different ways, of finance into the economy, society or the state and at the same time it describes also an increasingly profitable form of capital accumulation (Arrighi 1994; Sweezy 1995; Fine 2010, 2012; Aalbers 2019).

There are several definitions of financialization (for a history of the concept and its application see Krippner 2004 and Aalbers 2019), also used to describe the penetration of finance in the residential real estate. I report here the most notably diffused in the study of this process on housing:

- financialization is "a pattern of accumulation in which profits accrue primarily through financial channels rather than through trade and commodity production" (Krippner 2005, 174);
- financialization represents "the increasing role of financial motives, financial markets, financial actors and international economies" (Epstein 2004, 3);
- "financialization corresponds to financial neoliberalism which is characterized by domination of the macro economy and economic policy by financial sector interests" (Palley 2013, 1);
- financialization is the process by which something is managed as a fund and is defined as "the increasing dominance of financial actors, markets, practices, measurements and narratives, at various scales,

resulting in a structural transformation of economies, firms (including financial institutions), states and households" (Aalbers 2019, 3).

The transformation of the urban landscape and also the residential real estate, it has been therefore argued, is now assessed on financial criteria (Harvey 2006; Brenner 2009; Torrance 2009), as investments made by financial actors are basically driven by the extraction of profit, while the social effects are merely a spin off effect of their investment strategies (Hebb and Sharma 2014). This raises therefore fundamental political, economic and societal issues.

Even if all four presented definitions of financialization can be applied to the study of this process in residential real estate, the one proposed by Aalbers is more actor centred, covering the majority of dynamics and actor features, allowing therefore a brighter approach to the process of financialization. In particular, the fact that this definition considers also financial actors, practices and narratives, makes it the most suitable for understanding the role of listed companies and their investment strategies, as well as their effects on cities and regions.

2.2. *German housing market*

The housing market in Germany is characterized historically and institutionally by a path-dependent development of stability, which can contain the price fluctuations and the effects of financialization processes in the housing sector more than in other European countries (Kofner 2014; Kohl 2014, 2016; Voigtländer 2014). However, particularly since the global financial crisis of 2008, there are signs that the financialization and flow of private capital in Germany are contributing to a modification of the housing sector, even if on different paths than what has been observed for other European and American markets (Hesse und Prekwinkel 2009; Fields and Uffer 2014; Bernt *et al.* 2017). Additionally, both private and municipal housing companies divested their real estate portfolios in order to pay-off municipal debt or to raise shareholder value (Kirchner 2007; Voigtländer 2010). This lead to a great amount of transactions, as between 1999 and 2011 around 1.4 million housing units (almost 3.5% of the entire German housing stock) were sold off (BBSR 2011). These sales took place in both part of Germany, as well as in both economically strong and weak regions (Wijburg *et al.* 2017).

In the literature, several elements have been identified, which have helped to make the German housing system and its recent modification peculiar. Firstly, house prices, since the early 2000s, have undergone an increase, not only in owner-occupied housing units, but also in rents, even though in international comparison Germany as a whole has remained a market with low prices even after the 2000s. The above-average rise in prices within the housing sector, compared with the price developments of the previous decades, reflects a regionally differentiated development, as it has been seen especially in the main urban areas (Kholodilin und Michelsen 2015; Botzem and Dobusch 2017), even though not all urban regions are characterized by positive economic performance. Secondly, in Germany, there has been almost no increment in the construction of new buildings for housing, while the mortgage-GDP ratio in the last 15 years, in contrast with the majority of other European countries, has remained almost stable (Aalbers 2016).

Thirdly, the differences of the German housing market are found not only at the national level (between Germany and other countries), but also at the subnational level, as the situation in Eastern Germany is surely the area that has changed the most, from the abandon of urban and rural areas after reunification and the selective repopulation of the cities (Kabisch *et al.* 2010). It has led to the polarization of growth in Easter Germany, where in declining regions some cities, and especially their centres, represents islands of growth (Herfert 2007). Additionally, forms of financialization have been observed also in housing market of shrinking cities of East Germany as the result of policy changes (Bernt *et al.* 2017). These changes in the spatial distribution of people and their economic activities have greatly impacted regional urban development, as well as the management of the housing stock, which become overabundant in some regions and scarce in others (Glock and Häußermann 2004). Thus, it becomes clear how the economic and social spatial dynamics are interrelated with the housing sector.

Finally, even though between 2001 and 2010 the housing market relaxed, in the last years, and especially after 2013, the federal authorities started to issue stricter regulations regarding housing rents, which effected especially the markets of the main cities (Kholodilin 2015). Contemporary, the privatization of almost all the sold communal and state-owned housing stock, which took place before 2008, has led to a reduction in social housing (Helbrecht und Geilenkeuser 2012; Heeg 2013). The related privatization of welfare state and effects of financialization of housing through private investors (Bernt *et al.* 2017; Kitzmann 2017a) lead to the modification of the housing market, especially in the main urban areas, and to undermine its stability, as the German housing market stability is mainly related to the provision of good-quality affordable rental apartments by public authorities (Voigtländer 2014).

2.3. *Entrance in the German market of financialized actors*

The main factor of change in the German housing market is represented by the entrance of listed companies, private equity and hedge funds, which have overtaken, among other real estate projects also almost all the sold state-owned housing stock (BBSR 2017) (often used for social housing purposes or, more generally, offered at accessible prices) and therefore changed a cornerstone in the housing market, which may influence the rest of the market in Germany and lead to the restructuration of the spatial distribution of people on low incomes. The entrance in the market of private investors and the formation of listed companies that took place in the last decade was favoured by institutional changes (Becker and Breidenbach 2006; Bernt *et al.* 2017).

The nature of these new private investors has changed in time and space, as private equity and hedge funds can be considered nowadays almost irrelevant, especially in the main markets (i.e., Berlin and NRW), as they have evolved in listed companies or have been acquired by them, even though private equity and hedge funds are still active in other German regions with lesser relevant markets (Wijburg and Aalbers 2017).

2.4. *The role of listed real estate companies as financialization actors in the housing market*

The role of listed real estate companies in financialization processes is particularly relevant for three reasons. Firstly, the entrance in the market of listed real estate firms has indirectly affected the rest of the rental housing sector in general (Fields and Uffer 2014), as state-funded affordable housing may not offer strategic assets for local governments any longer, as it would lead to the demolition or privatization of public and social housing, reduce supply side subsidies in favour of housing allowances, promote home ownership and deregulate rents (Crump 2002; Turner and Whitehead 2002; Wyly *et al.* 2010). Secondly, these actors basically orient themselves in the housing market, not as traditional housing companies, but more as share profit-oriented (Holm 2010). From this perspective, they are also oriented towards the strategies of handling the properties they manage. Finally, besides private landlords (including private housing companies, private individuals, institutional investors and companies controlled by financial investors), listed companies are the most important suppliers of rental housing in Germany (Kofner 2014).

The entrance of these new actors is part of the unique path of the German housing market towards financialization, described as the succession of three different waves (Wijburg and Aalbers 2017): the first wave (1986-1999) saw the marketization of the mortgage market; in the second wave (1999-2009), the privatization of the public housing sector took place; in the third wave (2009-present), there has been a housing boom in German cities, while listed real estate companies have entered the market to an overwhelming extent. Listed real estate companies, as well as financialized companies in this sector, have showed, also in Germany, differentiated strategies for the extraction of value from the housing units they manage (Fields and Uffer 2014; Bernt *et al.* 2017; Romainville 2017; Wijburg *et al.* 2017).

2.5. *Open issues*

As presented above, the German housing market is changing rapidly and the recent activity of private investors, especially listed companies, has been identified as peculiar of financialization practices. However, previous studies on the German housing market and its financialization, or on the activities of listed companies as financialized actors in the housing market have not tackled the issue comprehensively, as they have mainly focused on the following aspects:

- specific cities, regions or projects regarding financialization (Holm 2010; Uffer 2011; Fields and Uffer 2014; Aalbers 2016; Bernt *et al.* 2017; Kitzmann 2017b; Romainville 2017; Wijburg *et al.* 2017);
- specific housing segments, especially social housing (Holm 2010, 2013) or ownership rates (Uffer 2009; Helbrecht und Geilenkeuser 2012; Heeg 2013; Aalbers 2016);
- specific institutional arrangements of features that constitutes peculiarities or structural elements of the German housing market (Becker and Breidenbach 2006; Herfert 2007; Kabisch *et al.* 2010; Kofner 2014; Voigtländer 2014);
- specific private investors and the conditions that have led to their rise (Holm 2010; Wijburg and Aalbers 2017; Wijburg *et al.* 2017).

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Therefore, a systematic and multi-scalar analysis of listed companies, their strategies, the spatial distribution of their activities and the related effects on the German housing market, as well as an extensive assessment of the impact of these activities at the urban and neighbourhood level is still missing. Despite this gap it emerges clearly from the literature that the housing market in Germany has changed in the last decades under the force of financialization processes and that private real estate investors have played (and are still playing) a crucial role in redefining the German housing market.

3. Conclusions

There are two conclusions to be drawn from this short literature review on the case of the German housing market and the financialization processes that are taking place with its actors: one at the company level and one at the urban-regional level.

Regarding the company internal logic, it can be said that financialization is like a state of mind, mainly oriented at the shareholder value and treating an object as a financial asset (Aalbers 2019) that is then reflected in the investment strategies of companies. This management approach of real estate, especially to housing, represents a different element and brings new actors to the German housing market.

On the other side, the change in mentality from a 'use value to exchange value' (Harvey 2014) will have significant consequences on the economic and social life in cities and regions. In this sense, financialization and the focus on generating rapid revenues can be understood as a state of mind of the investors in the housing market. It stimulates a specific geography of capital flows in the housing and real estate sector. This is reflected in an increased or reduced accessibility to housing in specific cities and regions, which may influence the rest of the market and lead to the restructuration of the spatial distribution of people, especially the ones with low incomes. The increased capital flow and its spatial concentration, as well as the increased prominence of specific actors may also contribute in changing the socio-economic functions of places, therefore influencing the urban and regional transformation.

The introduction of a financial mentality to the management of housing, especially in combination with the spatial concentration of capital flows, can stimulate structural changes in the socio-economic structure of cities and regions. This is well known in the debates on housing and financialization, but is has to be stressed in order to show the impact that these topics have on the (urban) daily life.

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