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Reverse Mortgage – Focus on the Cracovian Real Estate Market**

1. Introduction

A property, as the investing object not only allows the satisfaction from the housing conditions, but also makes a perfect source of manifold advantages, such as the protection of capital from theft, its protection from inflation, or acquiring incomes from renting.

The present article represents an innovative for the Polish market possibility of logging the property income – the reversed mortgage. This product is much different from the credits available on the market; this is a mortgage credit but the way, in which is has been carried out is different from the existing credits. Its specifics results from the interest in the consumers' segment, which has been neglected so far – as a source of additional income beside a classical pension. It is worth to mark, that elderly people invest on market rarely; they also cannot depend on traditional form of long-term credits. Present pension system is not able to assure similar incomes level to these achieved during professional activity, therefore reversed mortgage can fill in the gap, placing the property in a new light, as a potential pension fund.

This instrument involves loading the land property, building or apartment, with the mortgage credit the value of which is paid by the bank at once or in monthly payments by the time definite in contract, what causes the growth of the debt with time. Unlike to a standard mortgage, the borrower is the owner of the property, and the borrower's age favorably influences the height of the received payment – the shorter period of paying, the higher value. This property has to be free from other credit burdens, and it is supposed to be kept on a suitable standard, as the borrower's duties include carrying out suitable repairs, paying taxes, etc.

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Properties situated in large cities, in prestige locations will stand up in the first order as the objects of interest. Cracov is particularly attractive in this regard, especially districts such as Stare Miasto, Kazimierz or Podgórze. Cracov is the most often shown as the city in which Poles would settle the most willingly (according to analysis [4]).

2. Adaptation for Needs of the Real Estate Market in Poland

This mechanism has been worked out in the United States and is successfully applied in many countries of Western Europe and also in India and Russia. In Poland its introduction is predicted for 2010. It comes from the lack of suitable legal acts which would regulate possible procedure of the taxation of earnings received in this way, as well as indispensable bank instruments. It is predicted that this service will be successfully received in Poland, because of aging society – according to prognoses by GUS, in 2050 the amount of people older than 65 years will exceed the half of the population.

The first conducted by ZBP testing results present, that this product interests 8% customers of banks. First companies, such as PZU, BRE, MultiBank, BZ WBK, Credit Bank, MBank or Xelion Financial Advisers prepare the preliminary estimations of payments. When the owner of flat is 70 years old and the value of his property is 350 thousands zlotys, then until the end of his life he can receive 1.0–1.5 thousand zlotys monthly payment, and after his death the property will be passed to the insurance company or the bank, if his heirs fail to pay the debt.

Such a form of logging income can interest young people as well and make up a solution for those who prefer to purchase a real estate instead of getting involved their earnings in pension funds. Such an apartment would bring double income – from renting and from the reversed mortgage, after reaching a definite age (in USA it is 62). The open question refers to the taxation of this income, in the countries where reversed mortgage was introduced the authorities did not put any taxation on this kind of income.

The analysis of European markets shows that interest of such credit will be higher from a traditional mortgage credit by about 1%. The real value of credit with percentages is counted at the moment of the borrower's death together, and the duty of repayment rests on heirs. Because the value of property the most probably will increase (even by several tens per cent), if the value of credit is the part of the property value, the heir, even if they have her to sell it, to pay off the credit, will not remain without maintenance.

The advantage of reversed mortgage, based on data from USA:

- financial support for indigent persons possessing the real estate;
- there is no definite minimum of earnings indispensable to get the credit;
- the capitalization the interest and the vindication of credit at the moment of the owner's death or property sale;
- the income is tax-free;
- lack of fear about the prolongation of the credit period.

The disadvantages of reversed mortgage, based on data from USA:

- the heirs inherit the debts, which have to be paid in most cases by selling the property;
- high cost of paying the credit, considerably higher than in a classic mortgage credit, unprofitable below 5 years of crediting;
- though the duty of appropriate maintenance of the estate belongs to the owner, there are no financial consequences if he does not obey this rule;
- it is possible that the offered property will be rejected by the bank, or the bank will enforce on chosen houses additional conditions (e.g. year of building);
- the credit increases the income, which practically excludes obtaining additional social services, such as allowances or reimbursements;
- despite the fact that the state assures independent consultation while signing the contract, the cases of abuses occur.

3. Cracovian Secondary Real Estate Market

The 2008 year brought a slight correction of the prices of flats on secondary market, the largest reductions of prices were in not very attractive districts, such as Nowa Huta, 5–10%, however in more prestige districts the correction was rather symbolic. In February 2008 the average sell price of a of square metre in a two-room flat in popular standard in Cracow was 7400 zlotys, and at the end of 2008 it is predicted to be at the level 7 800 zlotys [5]. Assuming the average price of a square metre about 7.5 thousand zlotys, and the average gross salary 3139 zlotys (in the enterprise sector in the first quarter of 2008, GUS) it can be calculated, that 2.4 monthly gross salaries are needed to buy one square metre, which makes Cracow the most valuable city in Poland. In further places are Wrocław, Warsaw, and the smallest relation between the value of square metre to average salary (1.00) was observed in Katowice. It is also noticeable that the prices of flats show differences within the city, which can create attractive enclaves of higher standard as well as

cheap, often untidy regions. The distribution of selling prices in Cracow as well as their proportional part in market are presented in figure 1.

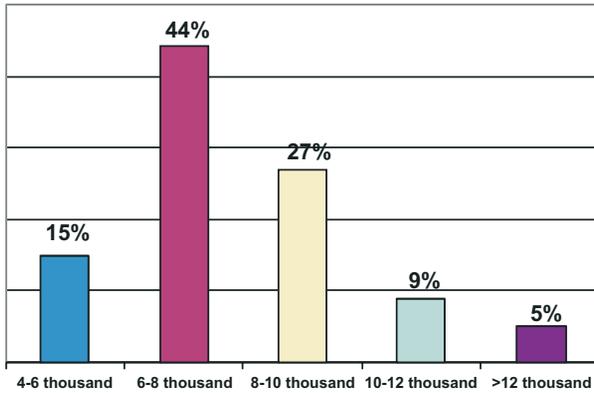


Fig. 1. The structure of offers of flat sales according to prices in July 2008 (in zloty/m²) [4]

Average selling prices in Cracow depending on the district are presented in table 1. It is worth to mark, that particularly valuable housing properties are in pre-war tenements, situated in the centre of the city and market prices of one square metre can even exceed 10 thousand zlotys/m².

Table 1. Selling prices of estates in the Cracovian secondary market, the state in July 2008

Region/district (year of building)	Price [zloty/m ²]
Krowdrza (2002)	8 500
Krowdrza/ Nowa Wieś (pre-war)	9 300
Nowa Huta (1959)	4 900
Dębniki (1995)	8 300
Prądnik Czerwony (1997)	8 400
Podgórze (1990)	7 700
Stare Miasto (pre-war)	8 900

Authors' own source

4. Conclusions

The product presented in the article has been tested in many countries, starting from USA, through India and ending with Australia. It has been very popular in these countries. This is a favourably assessed form of property protection, alternative to classic pension; therefore its implication on Cracovian market of prop-

erty should not encounter obstacles. The owners of flats in attractive locations who purchased them for small payment from PGM will be the best recipients of this offer. PGM administrated the predominant number of old tenements in 1990s, so now the owners of such flats will gain most. This offer will be also interesting for younger generations, who will look at the real estate as the future protection from temporary fluctuations of prices. In long-term analyses, regardless fluctuations, they can expect their growth of about 10–15% annually, exceeding deposit accounts considerably. In the majority of properties in Cracow the growth of prices can be expected. The exceptions are flats in panel buildings, which, overestimated in 2007; in 2008 lost much of their value. The lack of legal settlements is at present the only obstacle in introducing this product. From side of banks the full approval for introducing the reverse mortgage into Polish market is visible. This can be proved by the interviews with the President of ZBP Krzysztof Pietraszkiewicz, as well as scientific conference dealing with this problem: *The Polish version of Reverse Mortgage*, which took place on 13th June 2008. The former Polish Minister Andrzej Aumiler, in 2006 tried to persuade the authorities of cities to introduce an instrument similar to reversed mortgage, however he did not succeed. The instrument was supposed to be based on signing contracts between the city authorities and pensioners. Based on them the pensioners were supposed to be paid 300–600 zlotys monthly and after their death their property rights would be passed to the community. Legal acts that would allow introducing this new product are necessary and expected in the closest future. The interest of both the consumers, banks and insurance companies predicts the success this undertaking, and the City Cracow, as one of five largest Polish cities can become a place of the pilot programme in the reversed mortgage.

References

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- [6] GUS data.