HOUSING-FINANCE

MANUAL

FOR

DEVELOPING COUNTRIES

A Methodology for Designing Housing–Finance Institutions

United Nations Centre for Human Settlements (Habitat)
Nairobi 1991

HS/258/91E
ISBN 92-1-131 186-1

FOREWORD

The shortage of finance for housing has long been recognized as one of the obstacles to the provision of housing for low-income households. Currently, for every house built using funds from formal financial institutions, another three to five are built with personal savings and funds from other informal sources. Most households are unable or unwilling to use formal financial institutions which have not been designed to cater for their situations and do not meet their needs. Consequently, much of the funding that goes into housing does not enter the formal financial system. With appropriate housing-finance institutions, households could be encouraged to save for housing, increasing the resources for housing finance. Unfortunately, many who are involved with housing do not fully appreciate housing-finance mechanisms, and many in financial institutions need to know more than they do about housing. It is in response to this need that the United Nations Centre for Human Settlements (Habitat) has been providing training and institutional support to member countries, and has commissioned this Housing-finance Manual.

This Manual provides the necessary instruction for devising housing- finance strategies appropriate to the needs of developing countries. The Manual can also be used to provide the basis for a course of training in housing finance, for the evaluation of housing-finance policies and proposals, and for the preparation of briefs or terms of reference for such evaluations. The Manual has been developed by J Babar Khan Mumtaz and Ronaldo Ramirez of the Development Planning Unit (DPU), University College London, in collaboration with Alan Knight and the staff of the United Nations Centre for Human Settlements (Habitat). The Manual has been tested in training courses at DPU, with participants from Africa, Asia and Latin America.

Arcot Ramachandran
Under-Secretary –General
Executive Director

HOUSING-FINANCE MANUAL FOR DEVELOPING COUNTRIES

This Manual provides the necessary instruction for devising housing- finance strategies appropriate to the needs of developing countries. The Manual can also be used to provide the basis for a course of training in housing finance, for the evaluation of housing-finance policies and proposals, and for the preparation of briefs or terms of reference for such evaluations. It is aimed at those, with some familiarity with either housing or finance, who need to develop a housing-finance strategy or to evaluate or commission one, but who have little or no previous experience or expertise in this field.

The Manual introduces a seven-stage approach for developing a housing-finance strategy. Each stage is presented as a series of Tasks for those unfamiliar with the action required. For clarification, there are Notes that provide an introduction to the salient aspects, and a set of Readings has been included to provide further background information. Sources are cited, and "Rules-of- Thumb" provided for situations where actual information is not readily available.

As a training tool, the Manual can be used for individual or group training, with or without the help of an instructor. Depending on the time available and the depth required, training based on the Manual could range from one to six weeks. If an instructor is available, the Readings can be supplemented or replaced by lectures or other material more appropriate to the particular situation.

If the Manual is being used for group training purposes, please read the Appendix: NOTE FOR RESOURCE PERSONS first.

CONTENTS

		Page
Introduction		4
Stage 1	Demand assessment	11
Stage 2	Appraisal of existing sources of finance	22
Stage 3	Appraisal of potential sources of finance	32
Stage 4	Preliminary strategy formulation	36
Stage 5	Impact of proposed housing-finance strategy	40
Stage 6	Review of proposals	48
Stage 7	Action programme formulation	51
Readings		60
Glossary		61
Appendix: Note for resource persons		66

INTRODUCTION

Housing finance is the provision of finance or capital for housing. There are three ways of interpreting this: housing finance can be taken to mean the capital required for the construction of housing or housing projects, the resources required to acquire or access housing by households, or the credit supplied by (housing) finance institutions.

The first of these interpretations is really **project finance**, except that it happens to be for housing projects. The third interpretation could best be termed financial institutions, focusing on those that supply or deal with housing. In this Manual, we shall not be dealing directly with either of these sorts of housing finance except insofar as they influence and interact with housing finance in the sense of capital for access to housing.

To purchase housing, households might have to layout as much as four times their annual income, and, therefore, few are in a position to buy a house from their own current resources. One obvious solution is to accumulate or save small amounts of capital and defer house purchase until the required total is reached. Even assuming that 20 per cent of current income could be devoted to such savings, this procedure might imply a wait of 20 years or more, provided that costs do not inflate more than the interest accrued on savings in the meantime.

Individual saving, therefore, is not a very attractive proposition. A way to overcome this is not only to use one's own savings but also to borrow the savings of others, to acquire the capital to purchase a house now, and to repay the borrowed amount back over time. For this, a group of prospective house-purchasers could get together and pool savings. Provided .not all the members wanted to borrow from the pool at the same time, we could have a workable system, and the larger the pool, the more workable it would be. This is, of course, the basis of mutual savings-and-loans associations that exist in many forms in many countries for a variety of purposes, not just housing.

However, to get a sizeable operation going, an association of savers alone will not suffice, and other savers must be attracted who do not have house-purchase in view. Such savers need not only be other households but may include institutions as well. Over time, a number of specialized institutions have emerged that can play the intermediary role necessary to run such an operation, bringing savers and borrowers together. Often, governments provide incentives for savers to invest their money with such institutions, which makes them attractive.

A large part of housing finance in the developed countries consists of transactions of specialized institutions, in the form of building societies or housing banks. However, the impact of these institutions in developing countries has been rather limited. That housing-finance institutions do not work well in developing countries can be mostly attributed to low levels and high disparity of incomes.

Income/housing relationships

Generally speaking, household spending on housing increases as income increases. This relationship can be expressed by the straight line A-A in figure 1. However, there are limits to how much a house can cost. If this "limit" is the point B, there is a corresponding income level B above which the income housing relationship will not hold, but housing costs will tend to stay constant. Similarly, there is a corresponding point C below which price housing is not available. Again, this can be related to an income level C below which housing expenditure will have to remain constant, regardless of falls in income.

These two "limiting" income levels can be termed levels of "affluence" and "poverty", respectively, at least in housing terms. There is another income level, D, below which a household does not have access to credit. For example, if banks operate a lending-limit rule of, say, three times household annual income, and the typical house costs $30,000, incomes below $10,000 per annum will find it hard - perhaps even impossible - to obtain finance.

In terms of housing supply, those above the affluence level will find that not only national but even international sources of finance are available to them. Those above the credit level will, similarly, find no shortage of contractors willing to build for them and financial institutions to lend to them. The problematic groups are those below the credit level: for them, access to finance for house-purchase will not be forthcoming, and it is likely that their access to housing will be limited to the rental market. Those below the poverty line will not readily find suppliers from the private commercial sector, and they are the most likely recipients of subsidized housing provision, if it is available [(1)].

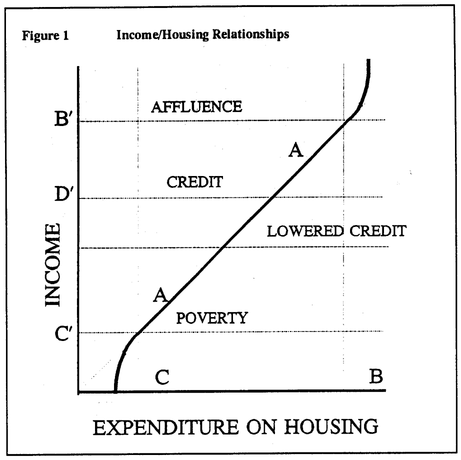


Figure 1 Income/Housing Relationships

[(1)] In the Third World, their only recourse may be to look for solutions in the city's illegal settlements.

Governments intervene directly and indirectly to affect the access of various income groups. Building and planning rules and regulations that impose maximum standards are likely to lower the affluence level, while those that set minimum standards will raise poverty levels. Some governments also intervene directly in housing finance, by providing subsidized credit through tax concessions or underwriting of lenders' risks: such measures tend to lower the credit level.

To look at the different impact that changing the credit level has in developed and developing countries, in figure 2, the same income levels used in figure 1 are plotted against income distribution. The income-distribution lines are plotted to show the typical cumulative percentages of households that earn given incomes. The solid curve is typical of developed countries and the broken line plots income distributions typical of developing countries.

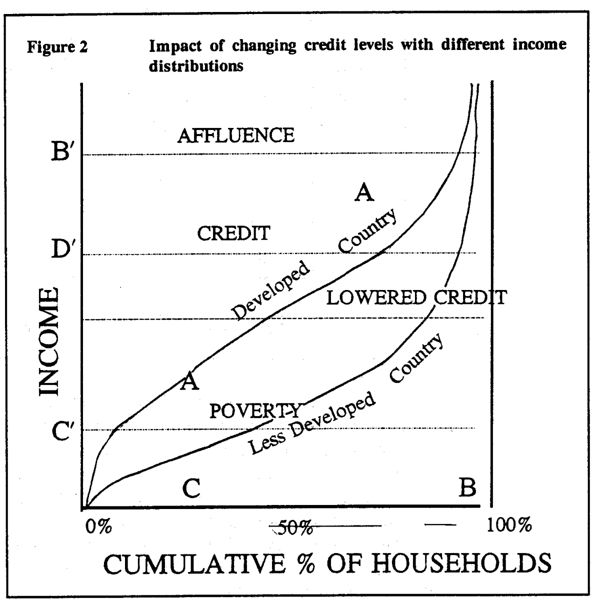


Figure 2. Impact of changing credit levels with different income distributions

By comparing the effects of a change in credit level, it can be seen that the impact on developed-country populations is far greater than on developing-country populations. A change that allows an extra 30 per cent of the former to have acres to credit hardly adds 5 per cent of the latter, which still leaves the majority unable to purchase housing. This explains, to some extent, why housing-finance measures that work for developed countries have little impact in developing countries. By contrast, look at the implications of lowering the poverty level (say through the introduction of "low standards of construction"): while developed countries would gain little (perhaps 3 per cent rising above the poverty level as a result), in the developing countries, a very significant proportion of the population can be affected in terms of housing supply (as much as 40 per cent more being raised above the poverty level).

Another reason why formal institutions modeled on those of developed countries do not work for low-income households in developing countries is that they require formal guarantees in the form of collateral. Whereas, in developed countries, most of the housing finance is required by households to purchase houses (from other households or from developers), in the developing countries, housing finance is required by households to build their houses. In developed countries, the land and the house form security for the lender, and can be mortgaged, and added security can be provided , through life insurance policies. In developing countries many households cannot produce valid title deeds to the land on which they intend to build. In the absence of life insurance policies or other securities, few, if any, institutions will finance land purchase if the only security is the land that is being bought.

Box 1. Sources or housing finance in selected states of Nigeria in 1980 (in percentage)

Source of finance	State								
	Gongola	Kano	Kaduna	Anmbra	Rivers	Bendel	Oyo	Lagos	Total
Building society	0	2	6	0	0	3	6	5	3
Bank loan	0	15	17	13	3	7	2	5	1
Total informal	0	17	23	13	3	10	8	10	4
Loan from employer	1	8	9	4	0	1	1	3	3
Loan from family	1	17	9	14	0	12	12	7	8
Personal efforts	99	58	59	69	97	77	84	79	78
Total informal	100	83	77	87	97	90	92	90	96

Not surprisingly, as boxes 1 and 2 show, only a tiny proportion of households in developing countries purchase their houses with finance provided through formal institutions. In situations where two thirds or more of the population finances housing through means other than formal housing-finance institutions, these other means should be looked at in some detail.

Box 2 Source of finance for new houses in two towns of India in 1981 (in percentage)

Source	City	
	Surat	Villapurna
Personal savings	67	53
Sale of assets	6	14
Provident fund loans	1	0
Employer loans	1	0
Insurance company loans	2	0
Mortgage bank loans	2	0
Commercial bank loans	9	4
Family loans	8	5
Other (informal) loans	5	24

These other means, the so-called informal mechanisms that make up the bulk of housing finance, allow households to purchase housing on a basis other than merely saving before building. Most commonly, households use a combination of means which allow them to:

Build while they save;
Save in building;
Save (earn) by building.

Building while saving, or incremental building, is perhaps the most common of these means, where by a household will construct and occupy a partly built house and improve and extend it over time. Such early occupation obviously allows the household to save on rent as well as provide shelter for a relatively small initial investment. In the short term, however, the household might be "inadequately housed", and the house will most likely be classified as "substandard".

Saving in building and, generally, building at costs that are well below market rates can be achieved by households, partly because through paring of construction and space standards to a minimum and partly through astute purchasing and management, haggling over every input. Additionally, households will use their own labour and that of others on an exchange basis; even professional help might be available at below-market rates from moonlighting or less-than-qualified builders.

Earning by building, through renting out rooms, is standard practice but, again, one which is not recognized by formal institutions as a source of income. One reason is that the formal institutions set up by the public sector usually lend subsidized public money and, therefore, are averse to seeing households profit from it.

There are other ways in which formal institutions tend to discriminate against low-income households and make it difficult, if not impossible, for them to borrow at prevailing terms and conditions. For example, in assessing affordability, most institutions use current levels of income, even though the repayment will be made over the next 20 years or so. Households not only take current income and expenditure into account but also know that they can squeeze expenditure temporarily, if, for example, in the near future, their children also will start earning. Households might also think of house construction as a collective enterprise and not be put off by the fact that it may be years, even generations, before the house is "complete": they see the house not just as shelter for the present generation but as a home for the family. In box 3, some of the terms and conditions of formal institutions are shown, along with an indication of the problems they pose for low-income households.

It is reasonable to assume that if appropriate housing-finance mechanisms were to be devised, a lot more than the current 20 or 30 per cent of households would and could borrow from housing-finance institutions to build houses. Housing finance alone is, of course, not enough. Legislative changes are required that make it feasible for households to build sequentially; land needs to be made available at rates that match demand and at affordable prices, and so on. These other wide concerns are essential components of a housing policy, and a housing-finance strategy should be seen as an integral part of it.

A housing-finance strategy is not a matter of choosing a particular system or establishing an institution. In order to meet varied demands, it has to be composed of a number of linked actions and initiatives by government, public-sector and private-sector institutions and households, each contributing to the provision of improved access to housing finance. A housing-finance strategy should specify which institution or group will undertake each activity; how that activity will be carried out; and which resources will be used.

Box 3 Limitations of conventional financial institutions*

a. High eligibility criteria	**Constraints inherent for low income groups**
- An "adequate" income at a specified minimum, e.g., $6,000	- An income usually below $2,000
- Regular savings at a specified minimal rate	- Intermittent savings, at a very low rate and often not deposited
- Regular employment and place of residence	- Intermittent employment, frequent changes in residence
- Collateral in the form of conventional marketable assets	- Small assets of a form rarely acceptable to conventional institutions
b. Restrictive loan terms	**Needs of lower income groups**
- Minimum loan size is large	- Small but frequent loans
- loans for completed dwellings only	- loans for gradual purchase and/or improvement of dwelling
- High down payments and ratios of down payments to total house price	- Very small down payments
- Maturity of 25 years	- Very short maturities
- Interest at the market rate	- Interest at below-market or subsidized rates
- Regular amortization payments through banking	- Flexible loan schedules, convenient premises and business hours for cash payments
- A total cost of housing finance that frequently amounts to 20-25 per cent of income	- Allocations of only 8-10 per cent of their household income to housing expenses
- loans with terms and conditions that require considerable sophistication to understand and comply with	- loan terms and schedules that are easily understood by people with low level of formal education or literacy.

* From UNDP, *Non-conventional Financing of Housing for Low-income Households* (ST/ESA/83)(New York UNDP, 1982)

APPROACHES TO HOUSING FINANCE

There are a number of ways in which to approach housing finance and to develop appropriate policies and programmes. These can be summarized as follows:

1. *Systemic methodologies*

One way to approach housing finance is to take a systemic look at the housing-production process, in order to identify constraints or inefficiencies. The analysis continues by further identifying those areas and activities where finance is the main constraint. Appropriate strategies can then be devised to overcome the constraints and contribute to efficient and , therefore increased housing production (see box 4).

Box 4. Developing a housing-finance strategy based on a systemic approach
The steps below summarize how a housing-finance strategy could be developed using a systemic approach to housing production.
1. Identify the main housing-production processes of the target groups.
2. For each of these, identify constraints to efficient and/or enlarged operations. Distinguish between different types of constraints, e.g., political, administrative, financial, legal, technical and executive.
3. For each financial constraint, devise strategies to overcome it. Where appropriate, combine strategies to address more than one constraint. Assign roles and resources, and programme the action.

A systemic approach is less likely to identify the needs of households for finance to acquire housing than it is to identify the needs for project finance and the capitalization requirements of firms and organizations operating in housing. The latter can be better addressed through support to business and enterprise methods than through housing-finance strategies.

2. *Supply-based methodologies*

These approach housing finance from the point of view of the suppliers of housing finance and take, as their starting point, a survey and analysis of existing institutions (see Box 5 below). This is the traditional approach adopted by the majority of housing- finance practitioners. Their intention is to examine and understand finance institutions, with a view to removing bottlenecks, improving their operations, making them efficient and enabling them to reach a large number of households.

Box 5. Six main analytical steps in developing a housing-finance strategy*
1. Assess the maturity and competitiveness of the financial markets at large.
2. Assess the relation of the housing-finance system to the rest or financial markets and the vitality of the system.
3. Determine the possibilities of mobilizing additional resources.
4. Develop several "packages" of possible combinations for increasing the volume of finance in the sector.
5. Analyse the impacts or implementing each package.
6. For the recommended course of action, detail the institutional changes needed immediately and over the long term.
* Ray Struyk and Margery Turner, Urban Institute

The advantage of such approaches is that it is easy to pinpoint the initial area for analysis and, since most of the housing-finance supply institutions are similar in their makeup and operations, it is relatively easy to identify areas for improvement. The disadvantage is that, since such institutions supply no more than 20 percent of all housing-finance needs in developing countries and probably none of the needs of low income households, the impact is likely to remain marginal.

3. *Demand-based Methodologies*

These approach the question of housing finance by starting with an examination of the requirements of the target households for housing finance. The demand for housing finance is differentiated according to the subgroups at whom the strategy is being aimed. The search for ways of meeting that demand starts with an analysis of the systems currently used by households in the target groups, and proceeds by devising strategies for removing bottlenecks and inefficiencies before turning to other sources of finance. While relatively new and, therefore, presenting a challenge, these methodologies are likely to have an immediate and significant impact, particularly where the target groups are mainly low-income households. This is the basis of the approach that is used in this Manual.

Box 6. Steps in a demand-driven methodology for housing-finance
1. Assess demand for housing finance *When does who need how much money to build what?*
2. Evaluate existing Housing-finance sources *What have households in similar circumstances been doing?* *What prevents the continued use of these methods?*
3. Evaluate potential sources *Could methods used elsewhere or by other households work here?*
4. Develop a preliminary strategy *Identify the main components*
5. Evaluate impact of proposals *What would the proposals do to the economy, to the housing sector and to households?*
6. Revise strategy *Test/market proposals, check assumptions and modify to anticipate impact*
7. Develop action plan *Detail the legal, administrative, political, financial and technical actions that are required to implement the proposals: allocate resources, identify actors, programme activities*

THE MANUAL

What does this Manual do?

The Manual provides a step by step approach for devising housing-finance strategies appropriate to a particular situation. It also provides the basis for a training framework for analysing housing , finance, and for the preparation of briefs and terms of reference for housing-finance institutions and strategies.

Who is this Manual for?

The Manual is designed to be used by senior and middle-level officials in government, parastatal agencies and private-sector , organizations concerned with housing finance in general and with low-income groups in particular.

How should the Manual be used?

The Manual can be used by individuals or by groups working with or without the assistance of a trainer or resource person.

The Manual provides a step-by-step approach which should be followed. The Task for each step is described, and, for those familiar with a particular step, the input/output requirements (using assumptions when necessary) can probably be met without further data collection or analysis. Where it is not clear what to do or how to do it, follow the instructions and carry out the Task which will guide you through a particular step. Although there are a number of Tasks, it is unlikely that any individual or group will need to go through all of them in order to complete the process. Some of the exercises will be easy and some hard, depending on previous experience and expertise.

Accompanying each Task are Notes which should be read before attempting the Task itself, since they will provide an introduction to some of the ideas and concepts involved. Further detailed information and general background is provided by the Readings. Where there is a resource person, these Readings can be supplemented or replaced by lectures, group discussions or presentations.

What is the working method of the Manual?

The Manual focuses on two things -the process whereby a housing-finance strategy can be developed and the production of a housing- finance strategy. For the latter to be realized, a lot of data will be required, and, to avoid waste of time and effort, it is important that the process be understood.

First, to understand the process, work fairly rapidly through the Manual, taking, perhaps, no more than 10 days to go through the first five stages. During this run-through, do not spend too much time looking for information that is not immediately available, but make reasonable assumptions and estimates or use the rule-of-thumb data provided (see box 7). Having completed the process, repeat it, taking most time over those steps that warrant it. The second run-through will improve the product, since it will give a good idea of what information is crucial and of how to obtain it in the form and quality required.

Box 7. Finding out
The necessity to base conclusions and proposals on "data" often leads to a stalemate when such data are not readily available. The remedy usually suggested is to go about collecting data. This is not merely a daunting prospect, but

might take so long to accomplish that b}' then the data will become obsolete.
Certainly in data-rich environments where data-bases flourish and are constantly being added or added to, the assumption that to obtain information it is merely necessary to locate the right database holds true.
In developing countries, this will probably not be the case. Not only will the right database not exist, but looking for one might take longer than it does to generate the information necessary to take action.
More important than looking for information is the definition of information so that we can recognize it when we see it. Not all data are information: most are obfuscation and tend to get in the way of rather than clarify thought.
In this Manual, the preliminary cycle serves precisely the role of clarifying what information is required and helping define the form it is required in, so that, if necessary, it can be collected for the second cycle.
The main message is to emphasize not how little information, is available but how little is required in order to proceed. The second is to learn to rely on qualitative rather than quantitative data. Better to have in-depth information based on a representative sample than seek to survey a statistically significant number of the population. Above all, it is, important to stress that information can be had not only by reading, but by looking and listening and talking to people.

What are the underlying assumptions and limitations of the Manual?

1. The Manual is designed so that it can be used to develop a housing-finance strategy for **all** income groups, but it is intentionally targeted where the need is greatest, that is, the low-income households.

2. The provision of housing finance (alone) cannot solve all housing problems. There will always be households that cannot afford to borrow the cost of a house on any terms but there is no doubt that improved access to housing finance will lead to improved access to housing.

3. Rental accommodation plays a vital role in housing provision, both for those whose incomes are too low to consider purchase and for those who do not want to own a house, at least not where they are currently living. The provision of rental accommodation is, therefore, seen as an essential and necessary component of housing strategies. However, the calculations and considerations relating to the economics of rents, rates of return etc. are not considered in the Manual.

4. Subsidies, for all the good they do to those who receive them, are difficult to target and, certainly, difficult to sustain either across the whole of the target population or over long periods of time. They should be used with caution and only where there is a clear and defined source of subsidies that can be both targeted and maintained, as, for example, in the use of oil revenues in Indonesia's Kampung Improvement Programme.

5. International, bilateral and multilateral loans for housing are discussed in the Manual but, in general, they can only make a modest contribution and, since housing generates no foreign currency with which to repay such loans, they must be repaid by foreign exchange generated in another sector of the economy. Therefore, at least in the long term, it is assumed that **all** the funds needed for financing housing must be generated locally from domestic resources.

6. In some countries, the provision of housing is considered to be a social obligation, and the ability of the occupier to pay the economic cost is not taken into consideration. In other countries, market forces are unrestrained, and ability to pay is the primary consideration. In most countries, however, there exists a market economy that is qualified in various ways and to varying degrees, and there are economic levers that can be manipulated to produce changes in, for example, interest rates and the allocation of credit. It is this fairly wide range of conditions that have been assumed in the preparation of the Manual.

   The format used in this Manual to describe the tasks required to develop a housing-finance strategy is described below.

FORMAT

Each Task in the seven stages in the process of developing a housing-finance strategy is laid out in the format shown below:

Task

Gives Number and Title of Task.

Objectives

Describes overall objective of the Task.

Issues
Indicates the issues that need to be dealt with during this Task. They should form the basis of discussion sessions.

Definitions
These are of the main terms introduced in this Task. These also appear in the Glossary.

Method
This describes sequentially the activities that need to be carried out to complete this Task. Most of these Tasks rely on judgement which should be arrived at after discussions (if there is a group) or after reading the Notes.

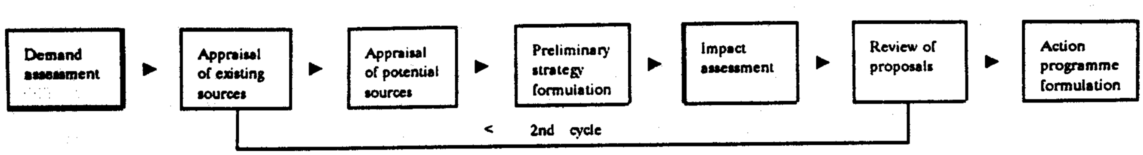
Information
This lists the most likely sources or types of sources, where necessary information might be found.

Rule-of- Thumb
It is recognized that it might not always be possible to obtain the information asked for, either because it does not exist or because there is not the time to acquire it. In such cases the rule-of-thumb values will, at least, allow work to be done for progression to the next Task. In every case where these values and/or assumptions are used, a note must be made of them, in order that they may be confirmed or corrected during the second cycle.

Examples
These are examples, often only partly shown, of how the Task can be executed, and are intended to provide a frame of reference and a guide as to how to carry it out. Actual examples will have more detail than is shown, and will be backed up and accompanied by extensive notes, documents and, of course, discussions.

Notes
These are brief introductions to some of the subject matter and are intended to provide the minimum background necessary for the execution of the Task, particularly where there is no resource person.

STAGE 1: DEMAND ASSESSMENT



The assessment of demand for housing finance is based on how much money households are able and willing to borrow over a given period of time. The conventional calculation is based on costs, a fixed percentage of income and eligibility criteria.

Thus, for example, if it is assumed that, typically:
- The housing cost is $10,000
- The housing loan is to be for 80 per cent of that figure ($8000)
- Loans are available at 8 per cent and repayable over 20 years
- Households can afford to devote 20 per cent of their income to loan repayment;

the loan can be afforded by households with an annual income of $4000 or more.

This group then becomes the target group and can be investigated to identify those who are likely to be willing to borrow for housing on these terms. The total demand for housing finance can then be arrived at by multiplying the number of (above $4000 per annum income) willing households by the average loan amount ($8000). If the potential borrowers are from different income levels with different housing costs etc., the total demand will be the aggregate of the demands of the different categories.

However, this method estimates the demand for housing finance supplied under a particular set of conditions. If the loan conditions were changed or the house or its price were different, the number of households able to borrow and willing to borrow would obviously change. While it is possible to assess variation in demand under different conditions of supply, this method will, nevertheless, always give a supply-determined total. This approach, which uses existing housing-finance supply criteria to determine eligibility, inevitably excludes the majority of households and virtually all of those at low-income levels from participation.

The other approach is based on the assumption that most households have a demand for housing finance, however modest. The starting point of this demand-based approach is to identify what the demand is of the households that are the target of the strategy. This requires an estimate of the number of households willing to finance housing and then, using the ability to pay of these households, a calculation of the demand for housing finance. The task in developing a housing-finance strategy is to identify and generate the supply of housing finance to meet this demand.

This second approach underpins the processes used in this Manual.

Task 1.1 DEFINE TARGET GROUPS

Objectives
To define for whom the housing-finance strategy is intended.

Issues
Should the housing-finance strategy be developed for a particular (target) group or should it be accessible to and aimed at all households?

What criteria and processes should be used to define Target Households (see Notes: TARGET GROUPS)?

Definitions
HOUSING FINANCE: This is the capital made available to a household [(2)] to improve or acquire a house [(3)]. Acquiring a house might mean building a house or buying one that has been built by someone else. The house might be bought from any of a number of sources, including the builder, another household or, even, a landlord, and the seller may be an individual or institution. The amount of housing finance required will depend primarily on the gap between the cost of acquisition and the amount already available to the purchaser. However, demand can only become effective, if the household is able **and** willing to borrow the amount. Its ability to borrow will depend on the terms of the loan as well as its own financial circumstances; its willingness is likely to depend upon its view regarding the value of the house or improvements.

Generally speaking, the amount of capital made available represents the difference between the cost of the house and the currently available resources of the household, and it is made available in the form of a loan to be repaid over a period of time with interest. From the point of view of the household, it is different from other forms of finance, in that the amount is likely to be large in relation to current income (between two and four times annual income). For the lender, housing finance is also different in that recovery poses particular problems.

These and other aspects of housing finance are further discussed throughout the Manual.

TARGET HOUSEHOLDS, GROUPS: These are those households or groups who are intended to be the primary beneficiaries of the housing-finance proposals of the housing-finance strategy. Unless these are clearly identified, both qualitatively and quantitatively, it will be difficult to ascertain whether the objectives of the proposals are or are not being met. In a demand-based approach, it is the demand of the target group that has to be met, and, therefore, it is particularly important to be clear as to who constitute this group.

LOW INCOME: This is a relative term to distinguish between those with (for example) high, middle or low incomes. In atypical developing country (see Introduction), 5 per cent of the population makes up the high-income group, 20-25 per cent makes up the middle-income group and 70-75 percent makes up the low-income group. While the term “low-income groups” covers those with the lowest incomes and no incomes, all low-income households are not necessarily below the Poverty Level, nor do they all have the same needs nor express the same demand.

POVERTY LEVEL: A level of income that cannot afford a basic minimum of goods and services, as defined in a particular context. Most countries have an officially recognized (if not set) poverty-level income.

Method

The following steps should be followed:

(a) The target group should be defined in broad terms: e.g., low- income households or civil servants. If there are terms of reference, they will probably define the target households. If not, the target households should be defined on the basis of existing housing policies or strategies.

(b) Definitions should be clarified and made unambiguous, using parameters that set the limits of the target group. In defining target households, some or all of the following parameters could be used:

Income: will the housing-finance strategy cover all income groups or be limited to a particular range (e.g., only for middle –income households)?

Occupation: will the housing-finance strategy cover all occupation groups or be limited to a particular range (e.g., only for government or public-sector employees, or only for those in wage-employment)?

Location: will the strategy cover households in all locations or be limited to particular areas (e.g., only in one Province, or only in rural areas)?

Other: will the strategy exclude or, on the contrary, focus on households with particular age, sex, socio-cultural, ethnic or other characteristics (e.g., not for those over 55 years old, or female-headed households)?

(b) Once it has been decided which of the above parameters will be used to define the target households, make sure that each of them use terms that are unambiguous. Wherever possible, quantifiable rather than qualitative terms. For example, some of the parameters might only have been given in such terms as "low income": these will have to be translated into monetary figures (i.e., households with monthly earnings between $x and $y).

Information

If there are terms of reference given (or to be written as part of the exercise), they should be the first source of information. In order to arrive at unambiguous definitions, national plans, policy documents or census and other surveys should be consulted. If there is a "client" he/she might be able to help clarify the definitions and should, in any case, be consulted for approval of the definitions that are intended to be used.

Rule-of- Thumb
The bulk of target households should be formed by those in the low-income groups, on the basis that these households are the least likely to be served by existing housing-finance mechanisms. However, lowest-income groups should not be part of the target group, as housing finance is not likely to be their immediate priority. If no precise definition exists for these categories, use between the 30th and 40th percentile income as the upper limit for your target group, and between the 80th and the 90th percentile income as the lower income limits. If the level and distribution of income is not defined, use half of GNP *per capita* times the average household size as the lower limit for defining low-income households, and that figure should be doubled for the upper limit.

Examples

The example in the box below summarizes Task 1.1

Example Task 1.1 Definition of target groups

In setting objectives for housing finance, a recent review of the country's shelter sector by an international agency suggested that "Housing finance should be provided equitably to the broadest segment of low-income groups possible. Any subsidies should be targeted to the lowest income group".

The same review also went on to identify the need for establishing a "rural land and shelter development programme which would make limited amounts of credit available to rural households to finance priority shelter related needs such as land acquisition, on-plot sanitation, roofing materials etc, with flexible loan amounts and repayment periods."

For the time being, therefore, urban low-income groups are not the subject of any existing or proposed housing-finance strategy, so it was decided to make them the target of this exercise.

Nationally, by urban is meant all those settlements that have been given the status of Metropolitan Corporation, Municipal Corporation, Municipal Committee, Town Committee or Cantonment. In general, these have populations in excess of 50,000 and make up some 30 per cent of the total population of the country of 100 million. In 1981, the census enumerated the urban population to be almost 24 million, composed of some 3.5 million households (i.e., an average size of almost seven), growing at about 4 per cent (Le" adding some 140,000 new households) annually.

On the basis of the best information available, the distribution of incomes amongst urban households is as follows:

Percent pop:		10	20	30	40	50	60	70	80	90
Income (up to Rs)	1100	1450	1650	1950	2300	2750	3300	3650	6000	

While the strategy will not exclude those from other income groups, it will be targeted at poor households. It will also not attempt to reach the poorest 10 percent who are likely to have priorities other than housing, such as employment and improved earnings.

Therefore, the following was agreed upon:

Target Group Urban low-income households
Income Range Rs.1100 to Rs.2300 (Rs.20/ 1 US $)
Location All urban areas of the country
Occupation Open to both public-sector and private-sector employees and the self-employed. Particular efforts should be made to accommodate those not on salaried or "regular" employment.
Other No other restriction or qualification will apply

Notes

TARGET GROUP

A sound strategy for housing finance has to define what the demand is. Unless the target group is clearly specified, it will be difficult to know what its demands are, and it will not be possible to evaluate whether the strategy is being successful in meeting them. It can be argued that a strategy can be designed without first specifying a target group. If it works well in efficiently providing housing finance, it can even be said to be successful: this is, indeed, often the case. However, an efficient strategy might not fully meet the demand for housing finance or might meet demand only partly. For example, while the accounting records of the majority of building societies and housing-finance companies might show whether they are working efficiently, very little of what they do has any impact on the majority of households. While this might be satisfactory or, even, desirable for a private-sector company concerned with profits at a minimal risk, this is not so, if the institution is founded on public-sector funds which are thus being used for the benefit of a minority. Where there is a subsidy involved in the operations, the inequity is the greater.

To ensure that any strategy being developed will benefit those for whom it is intended, we must be clear as to who that group is, through the definition of a target group.

In establishing a target group, a balance has to be kept between those who can be benefited and those that need to be assisted. If the strategy is directed only at those who can benefit, it is unlikely to make much of an impact on the financing of housing for low-income households. On the other hand, if the target groups are unrealistic, the strategy will not only be difficult to implement, but might become counter-productive.

For instance, a government might declare its intention to lend to those most in need. While this was not actually the case with Sri Lanka's Million Houses Programme, the officials implementing the loans programme initially made it so. In their zeal to help those in the greatest need, loans were given to those who were poorest and had little probability of returning them. The rate of defaults was high, and yet the Government could hardly prosecute such households. Much of the ensuing training of the officials working on the Million Houses Programme was focused on the need to differentiate between loans and grants, and the need to define target groups accordingly.

In this Manual, it is suggested that ability and willingness to repay a loan must be a necessary condition for a housing-finance operation to be viable. However, it is not suggested that affordability be used in the conventionally restrictive sense. In the Introduction, an indication was given of the means whereby households finance housing. Every effort should be made to include these means in order to extend the possibility of house-building to low-income groups.

Housing-finance strategies targeted for low-income households should be aimed at reaching as far down the income ladder as possible. In practical terms, this will mean trying to reach all those above the poverty line, not necessarily expecting that housing finance will allow all of them to fulfil their expectations instantly, but expecting that it will enable the poorest amongst the target group to embark on a process that will provide housing within a few years. Where the poverty level or the income distribution is not known, the rule-of-thumb suggested above should be used (the half-GNP figure will need to be multiplied by the average household size to get household income).

The income distribution in most developing countries will prevent some 10 to 20 per cent of the poorest households from being part of the target group. This does not mean that they should not be included in a housing strategy -but they should not be considered as a priority target for a **housing-finance** strategy. Other forms of assistance and policy (e.g., income generation) will be appropriate.

(2) As pointed out in the Introduction, the Manual will focus its treatment of housing finance on households, though much will also apply to others, both individuals and institution, acquiring or providing housing or housing finance to acquire or improve a house.

(3) Finance might also be required to meet urgent, short-term needs, such as might arise when there is a gap between the time when payment is due and long-term housing finance becomes available. Such "bridging loans" are likely to be at high interest rates.

Task 1.2 ESTIMATE HOUSEHOLDS' DEMAND FOR HOUSING FINANCE

Objectives

To estimate the demand for housing finance of the target households defined in Task 1.1. This should express how much financing is required, when and for what.

Issues

Can households express willingness to pay in the absence of an actual product?

Can households really measure their ability to pay in the abstract, now and for the future?

How accurate are surveys in establishing incomes? Can market surveys predict market behaviour?

How should the identification of building and building-material costs be done?

What should be used to calculate the cost of housing? Should it be money actually spent, or should market prices be attributed to all materials and labour, and the costs thus imputed be used?

Definitions

NEED: This is a requirement or necessity. A need for a product exists whenever the required item is not available or is in short supply. HOUSING NEED is a quantification of those households to whom housing is not available. However, "housing" has to be qualified using standards of acceptability, "availability" by conditions of supply, and "households" by demography and social change. Consequently, the measurement of housing need becomes complex and more dependent upon definition than on computation. Housing need is only marginally useful for formulating or establishing housing-finance strategies.

DEMAND: This means the desire of would-be purchasers or users for a particular good or service. Demand is distinguished from need in that the willingness to acquire must be backed up by an ability to acquire. Demand is, therefore, related to the product's price and varies inversely to it. The demand for a product will be determined also by its desirability or value to the buyer, which may be a function of its attractiveness or of the degree of desperation and need of the buyer. **HOUSING DEMAND** is, therefore, an estimation of the number of households that would be willing and able to acquire a particular housing package.

EFFECTIVE, POTENTIAL and PENT-UP DEMAND: Effective demand is that which is actually backed up by a real ability and willingness to purchase a product that is offered. Potential demand is one that might exist in the future or is currently latent, either because the product does not exist or because there are other conditions that prevent buyers from putting their preferences into action. Pent-up demand is a special case of potential demand; it is current but remains unexpressed largely because of socio-political constraints rather than purely material considerations.

TYPICAL: This is something which exhibits the characteristics most common to its class and is an exemplar for its category.

PRICE: This is the money charged for a product and is usually equal to the seller's costs plus profits or losses.

COSTS: These are the expenditures incurred in producing a product, such as a house, and do not necessarily equal price or value.

VALUE: This is the worth of a house as the finished product and it might be different to different purchasers or users. For example, the user value (i.e., the worth of the house to the user of the house) might be more than the formal market value and both might be more than the sum of all the inputs that have gone into producing the house, including the imputed costs for labour and allowance for "profit". Typical user values include location (proximity to employment, schools or to other family members), size, rental value and comfort.

IMPUTED COSTS: When actual costs are not known, because materials or services are not paid for or are paid for at special or concessionary rates, costs are assumed or imputed.

IMPROVEMENT: This includes any and all additions and alterations to an existing house that increase its space, comfort, utility or life. These could range from building additional rooms, to replacing or renewing the roof, to obtaining a water connection or, indeed, to completely rebuilding the whole house.

Method

In order for demand to be calculated, an estimate needs to be made of the number or percentage of households in the target group that would be willing and able to borrow money for housing, and of what these amounts would be. Unless a recent study has been carried out that gives this information or a housing-demand analysis has been carried out, it will be necessary to develop estimates. This will require a survey along the lines indicated in the section on INFORMATION.

For the first cycle, however, the following method can be used to derive a set of crude working figures. This methodology will give an idea of what should be done with the survey results in the second cycle.

1. A crude estimate should be made of the number of households (per year) that would be willing to borrow for housing.

   At one extreme, it can be assumed that this number will be equal to the number of new households formed annually, on the basis that every household would be willing to borrow, if loans were available on the right terms. In the absence of accurate figures, this figure can be derived by applying the annual rate of population growth, through net, natural and migratory increases, to the target group and dividing that figure by the average household size.

   In reality, the demand figure is likely to be lower than the total of households, since not all the increased population will form new households or will want to borrow for housing. Some of the increase will be assimilated by existing households, while others could be housed in units created by subdividing existing houses. This kind of phenomenon is likely to show up in census figures as static or increasing household sizes, despite reductions in family size, as increased overcrowding, or as a reduction in the number of rooms per household. Also, some households will prefer to rent and, therefore, not want to borrow for housing.

   The allowances that should be made, to take these considerations into account, depends on the extent to which they occur amongst the target group. For example, even though there is considerable renting taking place at the moment, it could be that this is a function of a lack of housing finance rather than an expression of lack of demand. Alternatively, it may be that the need for rental housing is being met through new construction, and, therefore, the housing-finance strategy must take that into consideration.

   At the other extreme, it may be argued that the number of households that are willing to borrow for housing is the same as the households that currently build houses, and their annual number should be equated with the total number of new houses built each year (including the "informal" sector).

Additionally, there will be demand for housing finance from existing households, to improve their housing. Again, at one extreme, it can be assumed that this will be equal to the annual obsolescence rate of the existing housing stock of the target group, not necessarily in the form of new, replacement housing but as an indication of the value of improvement and repair work. In reality, the actual amount spent is likely to be far less than this figure, as is evidenced by the steadily decaying state of the housing stock in most developing countries.

2. Crude estimates should be made of the amount of housing finance required by each householder:

This figure will range between the amount that a household needs to borrow to finance housing and the amount that a household will be able to borrow, given the financial status of the household and the terms on which loans are available. The amount that is needed will be equal to the cost of the house or housing improvements, less the amount the household already possesses in cash or in kind. The cost of a typical house or improvement, less the likely savings of a typical household can be used. Where the housing needs of the target households cover a wide range of housing, the target households should be divided into subgroups, with an indication of the number of households in each subgroup and the amounts that they will need to borrow. It should be kept in mind that the mechanisms that will allow the household to afford such an amount will have to be devised. Such mechanisms, which might include borrowing sequentially or subletting, will have to be developed as part of the housing-finance strategy.

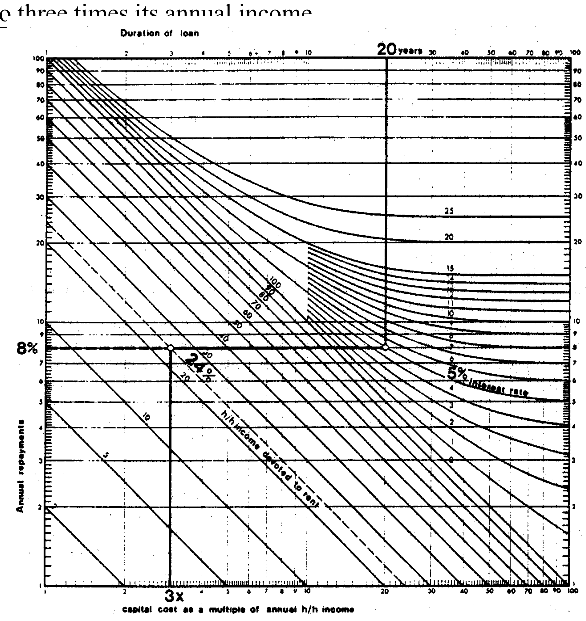
What households can borrow is generally arrived at by using a formula which calculates the capital sum that a regular payment could repay at a given rate of interest, over a fixed time period. (4) This relationship is shown in box 8 which is used to calculate what households can borrow. The amount that a household can repay regularly is expressed as a percentage of income, allowing the capital to be expressed as a multiple of annual income.

(4) The formula is $PMT = C\{i/1-(1+I)^{-n}\}$ where C = capital borrowed; i = annual rate of interest; n = time period of loan in years; and PMT = annual repayment amount.

Box 8 Ability to borrow

The amount of money a person can borrow is determined by a mathematical formula which uses rate of interest and duration of loan to calculate the annual repayment (expressed as a per cent of the capital borrowed). If the amount that a borrower is willing and able to devote annually to repaying the loan is expressed as a percentage of his annual income, it is possible to express the capital sum as a multiple of the borrowers' annual income. There are various programmes and tables that allow the value of any of these variables to be read off, if the others are known.

The nomogram below uses the intersection of lines of given value to provide values for the dependent variable. As an illustration, the nomogram shows that for a loan of 20 years, at 5 per cent interest, the annual repayment would have to be 8 per cent of the capital borrowed. If a household devotes 24 per cent of its annual income to repayments, it can borrow a capital sum equal to three times its annual income.



The regular payment figure is based upon the amount households currently spend on rent or other housing-related payments, and has been found to range between 10 and 40 per cent of income. The figure used should be an amount that is affordable by the household, in that it should leave enough income to cater for the household's expenditures on food and other necessities (see box 9). For the low income households, this figure is likely to be between 20 and 35 per cent of their income. These rule-of-thumb figures should be checked against the real situation amongst the target group as soon as practicable, since real figures vary considerably between households and the variations have significant implications for housing finance. Again, if the incomes and ability to pay of the target households cover a large range, they should be broken down into subgroups, with an indication of the number of households in each subgroup.

Box 9. Ability to pay

The ability to pay of a household is one of the critical elements in calculating what a household can borrow and, therefore, of most housing-finance strategies, and yet it is the most difficult to be precise about. Conventional methods assume that a household could devote upto 25 per cent of its income to housing repayments, and a figure of 20-25 per cent has been thought adequate for making calculations. However, the first difficulty arises from not being able to define "household income". Households are not only reluctant to divulge such information, they might actually not know what it is, particularly as, for many low-income earners, it comes from a variety' of sources and is irregular. Research shows that income surveys are misleading and that more reliable estimates can be got from surveys of household expenditure. This has led to treating "housing" as a residual (akin to savings) and has suggested that households can not afford to devote more than 10 per cent of their income to housing. indeed, many studies show that households appeared to be regularly spending more than 100 per cent of their supposed income on items such as food and other essentials (thus further discrediting income figures), accordingly, leaving no possibility for making housing repayments. Recently therefore, it has been suggested that, while the 20-25 per cent figure is acceptable in general, it is too high for the lowest-income households, and that the figure for percentage of income that households can afford should be taken as 10 per cent (see box 3).

However, figures from 16 cities in eight countries show that the proportion of income devoted to rent decreases with income. Studies of rents paid by low-income households show that payment can be as much as 40 per cent of their incomes and that this might be higher still in some of the "informal" renting housing which provides few amenities and little space of low quality construction. On that basis, it could be argued that, in developing proposals for housing, it would be safe to assume figures of 30-35 per cent of income being devoted to housing repayments, if in return, households got not only good housing but also security, including the possibility of eventual ownership.

The ability to pay of a household is of course further complicated, if time is taken into consideration. Most repayment schemes assume static incomes, whereas, in reality, most households expect their incomes to increase over time, not only because of an increase in their earnings through promotions etc. but also because they expect one or more or more of their children to start earning and contributing to the household's ability to pay. Moreover, household has a target, it will undertake a number of saving and income-enhancing activities that it was not previously doing, in order to meet the target.

Obviously, what a household could do and whether it will do so cannot be decided by anyone but the household itself. Furthermore, nobody but the household can take the risk of not succeeding in that effort and, thus, facing possible hardships in order to meet repayment commitments. This means that only the household can really determine what its ability to pay will be (though it can be ensured that it both understands what it is committing itself to and that it has plausible plans for achieving its intentions), and, to do that, the household needs a real rather than abstract objective. This means carrying out market research, rather than household surveys to estimate a household's ability to pay.

1. Malpezzi S., and Mayo S., *Housing Demand in Developing Countries,* World Bank Staff Working Paper No 733, (Washington D.C., 1985).

3. The estimates should be tabulated to arrive at a crude estimate of the total annual demand for housing finance: For each subgroup or target group, the number of households and typical amount of financing should be indicated. The two figures should be multiplied to arrive at total financing. If subgroups are used, all the subtotals should be added to arrive at the total housing finance for the target group.

Information

For the first cycle, if a recent survey has not been carried out, housing demand will have to be based on what information can be obtained from the census and various other sources regarding household sizes and numbers. The information sources regarding typical costs and prices include published construction cost/price index, surveys, builders, contractors, architects, advertisements and real estate agents.

For the second cycle, in order to have accurate assessment the numbers of willing households, and the amounts they are willing to borrow, a survey is required. The sorts of questions that should be asked by the survey are indicated in the example to this task. These questions should be combined with the questions that need to be asked in Stage 2, and undertaken as one survey.

Example

The examples below give illustrations of assessments of demand.

Example		**Task 1.2 Estimate of demand: first cycle**	
On the basis of discussion amongst the team members, the following figures were arrived at, using currently available information.			
1.	Estimate of number of households:		
	a.	New urban households formed annually (from Task 1.1)	140,000
		In target group: 40 per cent	56,000
		Of these, presumed absorbed into existing units: 20 per cent	11,200
		Net households looking for housing	44,800
30%		Of these, presumed to prefer renting or to use employer provided housing etc.,	
	b.	Existing urban housing units	4,000,000
		In target group: 40 per cent	1,600,000
		Of these, presumed wanting to modify/improve their houses: 2 per cent	32,000
	c.	Total number of households, a + b	63,360
2.	Estimate of finance required:		
	a.	Typical cost of new house	Rs. 120,000
		Typical cost of modification/improvement	Rs. 40,000
		Typical financing requirement (percentage)	50%
		Typical house-purchase loan	Rs. 60,000
		Typical improvement loan	Rs. 20,000
	b.	Ability to borrow 15 per cent over 20 years:	
		Lowest income in target group (at 30% devoted to repayment)	Rs. 23,760
		Highest income in target group (at 20% devoted to repayment)	Rs. 33,120
		Average income in target group (at 25% devoted to repayment)	Rs. 27,720
	c.	Average house-purchase loan, say	Rs. 45,000
		Average improvement loan. say	Rs. 17,000
3.	Estimate of total finance demand:		
	a.	For new houses = 31,360 x Rs.45,000	Rs. 1,400,000,000
	b.	For improvements = 32,000 x Rs.17,000	Rs. 544,000,000
	c.	Total demand for housing finance	Rs. 2 billion

Example	**Task 1.2 Estimate of demand: second cycle**

Based on the findings from the survey, the following households' demand for housing finance:

1. There are three distinct groups of households that are willing to borrow for housing:
   - those that want to build/acquire new housing and have land,
   - those that want new housing and do not have land,
   - those that want to add to or modify existing houses.

2. Most households have access to funds for a down-payment (of Rs. 3000-5000, through existing savings in cash or in kind, one-off gifts from relatives) and those that do not, would be willing and able to save towards a deposit.

3. Most households would prefer to restrict their repayment period to between 5 and 10 years, and a monthly repayment of Rs. 100-500.

4. Most households are willing to build in stages and accept the temporary hardships that it would entail. Except for those in the lowest income group, few want to sublet as a means of increasing their ability to replay a loan.

Notes
Survey questions

Shown in the box on page 33-34 are questions that could form basis of a questionnaire for use in a survey to derive an estimate of housing demand. IT IS NOT A QUESTIONNAIRE AND IS NOT LAID OUT AS SUCH. There are three sets of questions, the first dealing with establishing pent-up demand for housing or housing improvements, the second with establishing the amount of finance that might be required and the third with households' willingness and ability to borrow.

It is assumed that the pent-up demand of renters will be different from owners; therefore, these have been distinguished in the first part. Questions are also asked to establish whether new housing options are likely to change household composition and the average size and number of households. In the other two parts, the questions relating to costs and, particularly, income and expenditures have to be handled with care, to elicit replies that are as accurate as possible.

The purpose is not so much to get statistically valid replies as to derive a sense of what the demand is for housing finance for a specific target group. How the survey is conducted and by whom are important. If at all possible, the interviews should be done by the strategy developers rather than by hired interviewers. That way, the strategy designers will get the best feel for the situation.

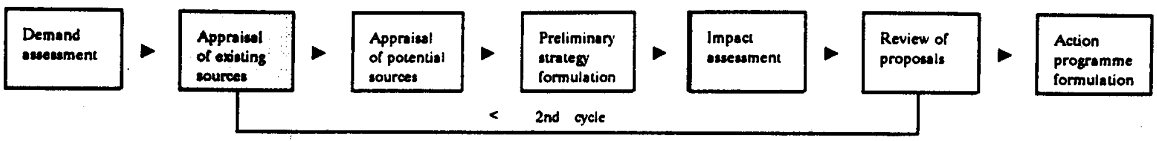
The questions listed here and their reply categories are intended as a guide. The list of questions is given to show the sort of questions that will need to be asked in a survey. The questions will have to be modified to suit particular situations, and the way the analysis will be undertaken will also determine the form in which the questionnaire is laid out. For example, if the questionnaire is to be administered by interviewers who are not part of the strategy-generating team, it will have to be prefaced by instructions on how to ask questions and how to enter responses; terminology and definitions will have to be made clear and unambiguous. To make it easy to get responses, on-contentious questions might have to be introduced at the beginning; the ordering and sequence of questions might have to be altered to keep open-ended questions together with probing questions and to separate them from close-ended questions. If the questionnaires are going to be processed using a computer, the software and programming might determine the format and require coding of responses.

The list of questions presented here should make the logic of the questionnaire easy to understand, and a similar list could also be used for the first cycle or as a pilot, before designing the questionnaire itself. A preliminary analysis can be carried out by summing the responses in the relevant rows. Some simple correlations can also be done this way. Using this method, 200-300 interviews can be processed in a day by two or three people.

Example Task 1.2 Demand estimate questions	
1. Who lives here?	Number of people Their relationships
2. How long have you lived here?	Years Previous location (name)
3. Why do you live here?	Reasons
4. Under what terms is this house occupied by you.	Owned by household Rented (from?)

	Rent-free (from?)
5. Do you consider your present housing to be satisfactory, both where you live and whom you live with (household composition)?	Yes (go to 23) No
6. Do you think improvements/additions would make your housing satisfactory?	Yes (go to 7) No, Why (go to 8)
7. What would you suggest as changes?	Improvements (go 10) Additions (go to 10) Household composition
8. Do you think a new/different house would provide satisfactory housing?	Yes (go to 9) No, Why (if also No to question 6, go to 23)
9. Describe such satisfactory housing.	Location (name/type) What sort Tenure
10. Are you considering making such changes/moves?	Yes, When (go to 12) No (go to 11)
11. Why not?	Financial constraints Other reasons (list)
12. How much do you think it will cost?	Amount (estimate or actual)
13. How much of this do you have?	In cash In other forms(detail)
14. How much more could you get?	Source Amount
15. If the remainder were to be made available as a loan, would you borrow it?	Yes (go to 17) No (go to 16)
16. Why would you not borrow?	Explain (go to 20)
17. How would you repay such a loan?	From current income (go to 18) From sale of assets (go to 20) From new/extra income (go to 20)
18. Do you currently save such an amount regularly?	Yes If not, why not
19. How do you expect to be able to do so in the future?	Explain
20. Would you be willing to build/improve in stages	Yes, Which No, Why not
21. Would you be willing to let part of your house	Yes, to anyone Yes, but only to (name) No, because (reasons)
22. Would your household be willing to contribute labour to building your house	Yes, What and when No
23. What do you estimate your household's monthly expenditure is on	Food Housing, rent Housing, other Transport Education Entertainment Clothing Other Saving
24. If you wanted to, which of these expenditures could you reduce	Indicate which By how much
25. What do you estimate your household's monthly income to be	Income of household head Incomes of Others (specify)
26. Is this income?	Regular Assured
27. Do you have any savings in cash or in kind (jewelry, building materials)	Regular Total Non-monetary
28. Have you borrowed money in the past	For what purpose From what source At what rate, terms Is there any amount left unpaid

Stage 2: APPRAISAL OF EXISTING SOURCES OF FINANCE



Among low-income households, there are many who find the means to construct houses. It seems logical to see if the mechanisms used by these households can be extended to others in similar circumstances. As has been pointed out in the Introduction, the majority of low-income households do not use formal sources of finance for their house-building but resort to a number of other methods. Very little is known about these methods and how they work.

The task, therefore is first to find out what methods are currently being used and then to evaluate them to see if they can be incorporated in the housing-finance strategy.

Finding out about anything to do with money is complicated and tends to create a feeling of unease and mistrust among the respondents, particularly if their transactions are not quite straightforward and legal. Therefore, tact has to be used, and their confidence gained, in order to draw out the details.

Task 2.1 SURVEY CURRENTLY USED SOURCES OF FINANCING FOR HOUSE- BUILDING

Objectives
To identify the methods and sources currently used by the target groups for obtaining finance for building.

Issues
What are the problems of obtaining information and identifying, measuring and evaluating existing sources? This is even more critical for the “informal” systems which provide 80 per cent or more of the finance for housing (see Notes: FINDING OUT HOW HOUSEHOLDS FINANCE CONSTRUCTION and WAYS OF FINANCING HOUSE-BUILDING).

Definitions
FORMAL: This means any system that is legally instituted, registered and recognized by the public authorities. Its operations are usually subject to scrutiny, and reporting is required by applicable legislation. The formal "sector" consists of all the known and “visible” entities and enterprises, as opposed to the informal "sector" which is largely "invisible" because it is not subject to regulation and does not appear in official statistics.

INFORMAL: This means any system where the rules and regulations defining its operations have not been formally constituted but are based on custom and practice. As a result, it is also likely to be unofficial and unrecorded and, probably, not subject to legal codes. Informal has also been described as being the opposite of formal or its dual. In practice, the two are not isolated but are likely to exhibit a high degree of interaction and, probably, form a continuum.

COLLATERAL: This is a form of security afforded to the lender by the borrower, by pledging property as a guarantee for the repayment of money. Ideally, the value of the property so pledged should not be less than the amount borrowed, and the property, must be possessable and capable of being liquidated for cash by the lender.

TERMS: This refers to the rate of interest at which money is lent and the period over which it must be repaid. These may be fixed or varied during the loan period. Variable interest rates may nevertheless be "fixed" by relating them uniquely to another interest rate which may itself vary, such as the "base" rate set by the Central Bank. The period may also vary, for example, in order to keep the monthly payment amount small or constant.

CONDITIONS: This refers to all other requirements set by the lender and might relate, for example, to such things as down payments, possession of legal title, secure employment and nationality.

DOWNPAYMENT: This refers to the money that has to be paid as the first installment of a series of payments in a repayment scheme. , The down payment is seen as an additional security for the lender/seller, as proof of the buyer's/borrower's financial capacity and as proof of intention to go ahead with the transaction. Most housing-finance schemes do not lend for the whole amount of the property to be acquired, the difference being met by the borrower in the form of a down payment which is usually larger than the subsequent payments (often between 10 and 20 per cent of the total cost).

Method

A chart should be drawn up with five columns, based on the one used in the Example to this Task. Columns should be labeled: Source; Terms; Conditions; Typical Loan Amount; and Capacity, respectively. The Terms column may be further subdivided into three columns headed Interest; Period; Collateral and Down payment, as in the example to this Task.

A list of all the main sources of financing house-building activities, whether formal or informal, should be made in the first column, under "Source." By "main" is meant those sources that are used by a large proportion of households or make a large impact on the total financing picture.

Against each source should be indicated the typical terms (column 2) and conditions (column 3) that apply. In column 4, the typical amount lent by the source should be indicated, either as a percentage of total value or as monetary figure or both. In the last column, an assessment of the capacity of this source should be given, either as number of loans, share of total requirement or total amount of money it could provide annually.

Information

Unless a survey has been done recently, it will be necessary to undertake a survey that catalogues how households in the target group finance their house-building (see Notes: FINDING OUT HOW HOUSEHOLDS FINANCE CONSTRUCTION).

Where it is not possible to carry out a survey (even of the modest size indicated in the Notes), personal experience will have to be relied upon, supplemented by casual interviews with colleagues, neighbours etc.

Rule-of-Thumb

There are no "rules-of-thumb", but see Notes: WAYS OF FINANCING HOUSE-BUILDING.

Example

See Example on next page which summarizes the information produced for Task 2.1 in the first cycle. The second-cycle survey results are shown in the example following the Notes: FINDING OUT HOW HOUSEHOLDS FINANCE CONSTRUCTION.

Notes

FINDING OUT HOW HOUSEHOLDS FINANCE CONSTRUCTION

Unless a survey has recently been done, it will be necessary to undertake one that catalogues how households in the target group finance their house-building. Such a survey should seek to identify all the main ways of financing house-building activities, whether formal or informal. Where time and resources permit, the survey should interview households that are building or have recently finished building houses. It is not necessary that the survey cover a (statistically) significant percentage of such households but, rather, that enough are contacted to ensure that the whole range of categories of households (Task 1.2) is covered: the number of households surveyed may be as few as 50 (as long as there are at least five households from each sub-group of your target group). It should be possible to undertake such a survey if about eight work-days are available, plus another day or two to analyse the results.

Example Task 2.1 Survey currently used sources of financing for house building							
Source of finance	Interest	Period (Years)	Terms Collateral	Down payment	Conditions	Amount of Typical Loan (in Rupees)	Assessment of Capacity
Relatives	0, nominal	Inf - 10	social	none	reciprocal social obligations	10 - 20,000	Most households should be able to call upon some amount through this source, and could account for 30 per cent or total requirement
Employers	0, nominal	5 -10	none; pension	not applicable	must be a 'permanent', full-time employee of some years standing with at least 10 more years of service before retirement	20 - 30,000	Though widely available to those in regular service, it is still discretionary. There is no reason to suppose why all those who 'qualify' (20 -30 per cent of target group) should not be able to utilize this source
Material suppliers	0, 10	Up to 1	Personal surety	20 – 50 per cent	Must purchase all or most materials from one source	5 - 10,000	This is more in the form or short-term credit to ease cash-flow problems of house-builders, and most material suppliers will extend such credit
Committees	0 to 20+	1 to 2	Social	not applicable	must be a member of a (work-related) group	3 - 5000	A form of ROSCA generally available only to those in regular employment, though it could be extended to others, especially through/to women
HBFC	10 - 15	15 to 20	Land (title)	100 per cent of loan	loan amount cannot exceed 50 per cent of building cost; title deeds of land must be produced	up to 250,000	Despite cumbersome bureaucratic procedures, this source should be available to all those who can meet its terms and conditions
Banks	15 - 20	5 - 10	land + guarantor	not applicable	must be credit-worthy; either through own record with that bank or through guarantors	no limit	With the right connections, short-term loans are generally available to those who can provide collateral
Money lenders	20 - 200+	up to 3	Personal surety	not applicable	must have a fixed place or residence and be known to neighbours	no limit	A useful and easily available source of short-term finance but with crippling rates or interest

Survey Questions

The list of questions shown overleaf incorporates the questions and reply categories of Task 1.2. The Notes introducing the survey questions in Task 1.2 should be read first. It is assumed that only one survey will be carried out to find out about both demand and currently used sources. The questions relating to demand come from Task 1.2, and the additional questions shown here (questions 5 to 11) relate to the sources of finance used by the target households.

EXAMPLE Task 2.1: Questionnaire	
Questions	**Reply categories**
1. Who lives here	Number of people Their relationships
2. How long have you lived here	Years Previous location (name)
3. Why do you live here	Reasons (location, building)
4. Under what terms is this house occupied by your household	Owned by your household Rented (from?) Rent-free (from?)
5. Under what terms is this land occupied by your household	Owned by you (as part of the house) Rented (from?) Rent-free (from?)
6. When was this house built, and how much did it cost	Date (guess/actual?) Cost (guess actual?)
7. In building the house who made decisions or was responsible for the various aspects	Designing Financing, paid for it Construction For each, indicate (household, contractor, previous user, institution)
8. What was originally constructed	Draw/describe
9. What additions have been made, when, by whom and at what cost	Describe/draw

10. For anything paid for by you, what was the source of the funds	List, for each source (prior savings, current income, sale of assets, loans, other) Amount, how obtained
11. What are the details of each loan	List for each loan: amount, rate of interest, period, conditions, current status of loan
12. Do you consider your housing to be satisfactory now, both where you live and whom you live with (household composition)	Yes (go to 30) No (go to 13)
13. Do you think. improvements/additions would make your housing satisfactory	Yes (go to 14) No, Why (go to 15)
14. What would you suggest as changes	Improvements (go to 17) Additions (go to 17) Household composition (go to 17)
15. Do you think. a new/different house would provide satisfactory housing	Yes (go to 16) No, Why (if also No to 13, go to 30)
16. Describe such satisfactory housing	Where located What sort Tenure
17. Are you considering making such changes/moves?	Yes, When (got to 19) No (go to 18)
18. Why not? What are the constraints?	Financial Others(list)
19. How much do you think it will cost	Amount (estimate/actual)
20. How much of this do you have	In cash In other forms (detail)
21. How much more could you get	Source/amount
22. If the remainder were to be made available as a loan, would you borrow it	Yes (go to 24) No (go to 23)
23. Why would you not borrow	Explain (go to 27)
24. How would you repay a loan	From current income (max monthly amount, go to 27) From sale of assets (list max amounts, go to 27) From new/extra income (list max amounts, go to 27)
25. Do you currently save such an amount regularly	Yes If not, why not
26. How do you expect you will do so in the future	Explain
27. Would you be willing to build/improve in stages	Yes, Which No, Why not
28. Would you be willing to let part of your house	Yes to any one Yes, but only to (indicate who) No, because (reasons)
29. Would your household be willing to contribute labour to building your house	Yes, What and when No
30. What do you estimate your household's monthly expenditure is on	Food Housing, rent Housing, other Transport Education Entertainment Clothing Other Saving
31. What do you estimate your household's monthly income to be	Income of household head Incomes of others (specify)
32. Is this income	Regular Assured
33. Do you have any savings in cash or in kind (jewelry, building materials)	Regular Total Non-monetary
34. Have you borrowed money in the past	For what purpose From what source At what rate, terms Is there any amount left unpaid

On the pages 45-48, the list of questions from the questionnaire is shown, with a summary of the responses filled in. These responses can be analysed, including cross-tabulation where appropriate, to give an indication of the methods currently used to finance house- building by the target group as well as the demand for different types of housing and housing finance.

<table>
<tr><th colspan="3">Example Task 2.1 Second cycle survey</th></tr>
<tr><td>1. Who lives here</td><td>Number of people
Their relationships</td><td>Ranged from I to 15+, Average 7.2. Less than 10 per cent fewer than 2 persons. The majority were nuclear families with one to five close relatives (daughter-in-law, parent or sibling or household head)</td></tr>
<tr><td>2. How long have you lived here</td><td>Years
Previous location (name)</td><td>Approximately 1/3 born in the same locality, 1/3 another locality in the same city, and 1/3 have migrated to the city between 5 and 25 years ago</td></tr>
<tr><td>3. Why do you live here</td><td>Reasons (location, building)</td><td>The majority (87 per cent) said because they had been able to find the land there (most had also applied/sought land elsewhere but had been unsuccessful), many also cited presence or relatives or kinsmen</td></tr>
<tr><td>4. Under what terms is this house occupied by your household</td><td>Owned by your household
Rented (from?)
Rent-free (from?)</td><td>68 per cent owned their housing units
22 per cent rented their houses (2/3 from private landlords)
10 per cent lived rent-free (the majority being housed as part or their employment)</td></tr>
<tr><td>5. Under what terms is this land occupied by your household</td><td>Owned by you (as part of thc house)
Rented (from?)
Rent-free (from?)</td><td>As above</td></tr>
<tr><td>6. When was this house built, and how much did it cost</td><td>Date (guess/actual?)
Cost (guess/actual?)</td><td>19 per cent less than 5 years ago, 21 per cent 5 to 10 years, 40 per cent 11 to 40 years and 20 per cent pre-1947
Most households put a value of about Rs.70,000 on a two-room house, but actual costs of construction varied from Rs.20,000 to Rs.l55,000 (without a close correlation in terms or quality or square footage)</td></tr>
<tr><td>7. In building the house who made decisions or was responsible for the various aspects</td><td>Designing
Financing, paid for it
Construction
For each, indicate (household, contractor, previous user, institution)</td><td>The majority (78 per cent) said the head of household, and another 28% said head with builder/contractor
Almost all said the head of household
Most felt no construction decisions had been made ("We built the way everybody builds") but admitted that contractors had suggested/influenced choice or materials ("We used what we could find")
(Note: All or the above exclude 'Don't know' answers in calculating percentages)</td></tr>
<tr><td>8. What was originally constructed</td><td>Draw/describe</td><td>3/4 of the houses (73 per cent) had been built as one-room or two-room, single storey units, with front and back yards. The rest were with more rooms; very few (3 per cent) had more than five rooms.</td></tr>
<tr><td>9. What additions have been made, when and by whom and at what cost</td><td>Describe, draw</td><td>About 67 per cent had made substantial changes to original design: mostly by cost adding rooms or enclosing verandahs</td></tr>
<tr><td>10. For anything paid for by you, what was the source of the funds</td><td>List, for each source(prior savings, current income, sale or assets, loans, other)
Amount, how obtained</td><td>Over 90% used all of the following: prior savings (including inheritance), current income, sale or assets (mostly land and jewelry), loans (mostly from relatives and from pension funds). 12% borrowed money from the House Building Finance Corporation (none exclusively).</td></tr>
<tr><td>11. What are the details of each loan</td><td>List for each loan: amount, rate of interest, period, conditions, current status of loan</td><td><table>
<tr><td>Loan Source:</td><td>Relatives</td><td>Employers</td><td>HBFC</td><td>Banks</td><td>Inform al</td></tr>
<tr><td>Interest:</td><td>None</td><td>0-10%</td><td>15%</td><td>8- 15%</td><td>20-120%</td></tr>
<tr><td>Condition</td><td>None</td><td>long service</td><td>Various</td><td>Employee</td><td>Short Term</td></tr>
<tr><td>Current Status:</td><td>67% paid off</td><td>45% paid off</td><td>8% paid off</td><td>25% paid off</td><td>90% paid off</td></tr>
</table></td></tr>
<tr><td>12. Do you consider your housing to be satisfactory now, both</td><td>Yes
No</td><td>68 per cent
32 per cent</td></tr>
</table>

where you live and who you live with (household composition)		
13. Do you think improvements/ additions would make your housing satisfactory	Yes No, why	85 per cent (of No respondents to Q.12) 15 per cent (of No respondents to Q.12). Mainly because of location or tenure
14. What would you suggest as changes	Improvements Additions Household composition	Over 90 per cent suggested improved services, mainly water supply and drainage Over 90 per cent suggested additional rooms or space About 15 per cent would prefer to have existing household split into two or more
15. Do you think a new/different house would provide satisfactory housing	Yes No, why	100 per cent (of No respondents to Q.13) Some expressed difficulty/expense of obtaining such a house
16. Describe such satisfactory housing	Where located What sort Tenure	Closer to work (mostly central area) Self-contained (mostly from those who share facilities) Owner-occupied
17. Are you considering making such changes/moves	Yes, When No	Under 5 per cent, most said as soon as possible
18. Why not? What are the constraints?	Financial Others(list)	Over 90 per cent Main reason cited was impossibility of finding such a house
19. How much do you think it will cost	Amount (estimate/actual)	Estimates ranged from Rs.70,000 to Rs.150,000
20. How much of this do you have	In cash In other forms (detail)	Most said between Rs.3000 and Rs.15,000 Main form was jewelry, the other was loans to relatives
21. How much more could you get	Source/amount	Estimates ranged from Rs.5,000 to Rs.50,000, mainly from relatives or employers
22. If the remainder were to be made available as a loan, would you borrow it	Yes No	Most Very few
23. Why would you not borrow	Explain	Worried about repayments/defaults
24. How would you repay a loan	From current income (max monthly amount) From sale of assets (list max amounts) From new/extra income (list max amounts)	All said they could repay between Rs.100 to Rs.500 Most felt able to raise between Rs.5000 to Rs.50,000 Almost half the respondents felt they could earn an extra 10 to 50 per cent income
25. Do you currently save such an amount regularly	Yes If not, why not	10 per cent Main response related to lack of incentive, difficulty of access to institutions, insecurity
26. How do you expect you will do so in the future	Explain	Most said that in the past, when they had to, they had managed somehow
27. Would you be willing to build/improve in stages	Yes, Which No, Why not	Majority, one or two room/s at a time Some felt that they could make an effort only once
28. Would you be willing to let part of your house	Yes to anyone Yes, but only to (indicate who) No, because (reasons)	Most of the low-income groups Prefer not to rent to relations Mostly those with high incomes, worried about lack of privacy
29. Would your household be willing to contribute labour to building your house	Yes, What and when No	Majority said they would contribute manual labour, outside working hours Only those who felt they were too old/inform declined
30. What do you estimate	Food	45-60 per cent

your household's monthly expenditure is on	Housing, rent Housing, other Transport Education Entertainment Clothing Other Saving	15-20 per cent 10-10per cent 5-10 per cent 5-10 per cent 5-10 per cent 5- 10 per cent 10-20 per cent 0-5 per cent
31. What do you estimate your household's monthly income to be	Income of household head Incomes of others (specify)	Rs.1000 to Rs.2500 Rs.1000 to Rs.2000 (mostly earnings of eldest son)
32. Is this income	Regular Assured	85 per cent 75 per cent
33. Do you have any savings in cash or in kind (jewelry, building materials)	Regular Total Non-monetary	60 per cent made some savings regularly Amount ranged from Rs.1000 to Rs.20,000 Amount estimated from Rs.5000 to Rs.50,000
34. Have you borrowed money in the past	For what purpose From what source At what rate, terms Are there debts outstanding	Is there any amount left unpaid. All had borrowed, mostly for short term requirements, weddings, illnesses Mostly from relatives Usually without interest, over undefined periods Almost 20% had debts outstanding; many were unsure about their indebtedness situation

Notes
Ways of financing house building

For the overwhelming majority of households, finance for house-building comes from a variety of sources, and each household puts together the best combination it can (see example on p.51). The package is likely to combine a range of sources, both formal and informal. The higher the income level, the greater the contribution of formal sources is likely to be. However, it must be kept in mind that, overall, formal sources of housing finance provide, perhaps, between 20 and 30 per cent of the total housing finance: the rest comes from informal sources.

The most likely informal sources of funds for initial construction are shown below:

(a) The biggest single source of funds is savings out of current income. Occasional surpluses, particularly when incomes are variable, are used to purchase building materials, and the progress of construction will depend on these margins. A study of a low- income area in Bangkok shows the time taken to complete houses built in this way to vary between 4 and 12 years.

(b) The second most quoted source is loans from friends and relatives, mainly from members of the extended family. The terms of such loans are imprecise, and interest seems not to be charged, although it has been reported that "social obligations" are incurred. There is clearly a limit to such a process. An extended family of, for example, 20 people may be able to subscribe to two or three loans but it will not be able to go much beyond this and house the majority of its members.

(c) The next and somewhat similar source is loans from employers and from colleagues at work. A difference in this case is that interest is likely to be charged and the loan may be related to continuing employment.

(d) There is the selling (or pledging at a pawnshop) of assets that have been previously accumulated such as jewelry or personal possessions. There can also be the sale of land or livestock.

(e) There is some recourse to moneylenders, but very high interest rates, short repayment periods and robust methods of collection limit the use of this source to situations of urgent need.

(f) There are the informal savings groups, sometimes known as rotating savings and credit associations (ROSCAs), that are described in box 10. Although they raise small amounts for short periods they are of interest in that they resemble, in some ways, the early associations that became building Societies. Whereas the sums raised by ROSCAs are rarely likely to be enough for the recipient to construct a house, they are very frequently cited as the source of funds where construction is incremental or where most of the construction is through self-help or without recourse to actual money.

Box10. Rotating savings and credit associations*

Rotating savings and credit associations (ROSCAs) are a popular form of informal finance. They have various aliases: *tanda* in Mexico, *pasanaku* in Bolivia, *san* in the Dominican Republic, *syndicate* in Belize, *gamaiyah* in Egypt, *isusu* in Nigeria, *susu* in Ghana, *tontine* in Niger, *hagbad* in Somalia, *xitique* in Mozambique, *arisan* in Indonesia, *paluwagan* in the Philippines, *chit fund* in India and Sri Lanka, *committees* in Pakistan, *pia huey* in Thailand, *hue* in China, *kye* in Korea, and *ko* in Japan.

ROSCAs intermediate in the most basic way. A small number of individuals, typically 6 to 40, form a group and select a leader who periodically collects a given amount (a share) from each member. The money collected (the fund) is then given in rotation to each member of the group. In some countries, such as India and Cameroon, ROSCAs have evolved into formal banks.

Three types of ROSCA are found in many countries. In common ROSCAs, the leader receives no special consideration (other than possibly getting the first fund). Commission ROSCAs pay their leaders, who in return may assume liability for defaults. Promotional ROSCAs are used by merchants to sell goods, especially consumer durables.

Loans are interest free in most common ROSCAs; the amount received is equal to the total paid in by the member. More sophisticated ROSCAs may allocate funds on the basis of discount bids, a practice common in China, India, Thailand and some parts of West Africa. The winner is the person willing to accept the largest reduction in share payment from other participants in return for receiving the next fund. All participants in a commission ROSCA, except the leader, pay for the right to participate and receive less than they contribute.

Recent research in Bolivia showed that one third to one half of all adults living in urban areas often participated in ROSCAs and that their ROSCA payments amounted, on average, to about one sixth of their salaries. These associations were even found among employees of formal financial intermediaries. Despite hyperinflation and poor loan recovery by formal lenders, Bolivians reported few problems in their ROSCA. Studies show that a relatively high proportion of those with steady incomes in Cameroon, India and Sri Lanka often participated in ROSCAs. These associations have also been reported amongst employees of the central banks of Belize. Bolivia, the Dominican Republic, and the Philippines.

The popularity of ROSCAs among low- and middle-income groups shows that people like to save, even under trying circumstances. The Bolivian research showed that more than 90 per cent of the people interviewed joined ROSCAs primarily because they wanted to save more and felt that membership forced them to do so.

* From: *The World Development Report 1989*, Washington, D.C. The World Bank, 1989

In raising relatively large sums in this way from a variety of sources, people in developing countries are showing great resourcefulness and enterprise. The advantages of these methods are that there are few forms to fill in, and procedures are simple to follow and there are few or no eligibility criteria. However, there are also many disadvantages. The amounts are small and from a number of different sources. The loan terms might not be recorded, so that conditions of repayment and interest charges are uncertain. It seems, at least, probable that the overall conditions to the borrower are less favourable than would be those of a single loan from a formal institution on stated terms and at a market rate of interest.

Example Task 2.1 Second-cycle survey

<u>Mr. Abdul</u>
There are five persons in Mr. Abdul's household - his wife and two children, and his mother - and their income averages just over Rs.2000 per month. They moved here some seven years ago from rental accommodation near the city. The land for the house was given to Abdul's wife by her parents as part of her dowry about 15 years ago. At that time the land was outside the Metropolitan Area, and was unserviced. In any case, the Abduls were unable to afford any construction, and the plot lay vacant. Later, when the Metropolitan area was extended, and electricity became available nearby, Abdul took a 12-year interest-free loan from his employer and built his two rooms, kitchen and bathroom. The loan equaled about 60 per cent of the cost; the rest came from the sale of his wife's jewelry (30 per cent) and borrowings from relatives (10percent). Money had to be paid to a draughtsman to draw an official plan and submit it for building and planning permission, though the house as built does not follow those plans. Abdul would like to extend the house when his family's needs increase, but is unable to do anything until he has finished paying off his present loan.

<u>Mr. Bakr</u>
Mr. Bakr is one of a household of 10, including his parents who are the actual owners of the house. When Bakr and

his brother got married, they were each given part of the plot on which to build their own “house”. The Bakrs now have two rooms of their own, but share living space with their parents. Both the brothers contribute to a kitty for food and utility bills and other common expenses. When the parents die, the brothers will divide the original buildings between them.

Bakr and his brother are motor mechanics; repairing cars and motor cycles in the garage of their father’s house and using the street in front. Their monthly incomes vary between Rs.1500 and Rs.2000, and after contributions to the common expenses, Bakr is left with Rs.500-600 for his wife and three children. The two elder children go to the local government school, while the youngest stays at home.

Bakr built his rooms in four stages over a period of five or six years, corresponding to the times when business was particularly good: the foundations were laid and left for two years, then the walls were built over the next two years, and the roof completed. Over the next two years, the floors were finished off, and one of the doors and windows fixed. The services have only been completed this year. The whole operation was done by calling in masons and other skills as needed. Since the "extension" is Illegal, no design was prepared or submitted to the local authorities.

Mr. Colpetty

Mr. Colpetty is a retired government clerk, living with his wife and four children. The eldest son is working in the Gulf as a driver, and has been the main factor in the Colpettys' building their house. Previously, they lived with other members of the Colpetty family, but, when their son secured the Gulf job, they sold their interest in the joint family house and used it to buy the land. With the title deed and accumulated savings, the Colpettys were able to obtain an HBFC loan of Rs.70,000 which is being serviced by part of their son’s remittances. The remainder is being deposited in a bank to build up the capital for him to build an extension on the roof for himself when he gets married.

The house was designed by an architect acquaintance of Mr. Colpetty, and the original designs allowed for the extension. Both the original three-roomed house and the extension are legal and have been approved.

Mr. Dawood

Mr. Dawood works as foreman in one of the factories in the nearby industrial estate and was lucky enough to obtain a plot of land in the first housing scheme he applied to. The down payment was secured by the sale of his wife's jewelry. That and his own savings also helped secure a loan from HBFC for the construction of the two-room house. Since the HBFC loan was paid out in stages, he has had to finance the construction of each stage through his work-based “committee” and, for the roof, even had to resort to short-term borrowing from the local moneylender to see him through the pouring of the concrete slab.

His income of Rs.2500 per month has to support his wife and four children as well as his mother and an unmarried sister. However, the sister makes some contribution to the household expenses by taking in piecework and generally helping around the house. Dawood is worried that, without a father, he has the responsibility of getting his sister married off, and he does not want to take on any further financial commitments until he has fulfilled that obligation, for which he may have to take a loan from his employers or, perhaps, a committee. However, as his eldest son is now 16, he expects him to start working within a year or so, and so bring in extra income. His first priority is to replace the existing kitchen, which is a temporary structure, with a proper building and, then. To add another room. He expects to get technical help from his cousin who works as a draughtsman with the local authority and who helped him get the original design passed and approved (in fact, it appears that this cousin may also have had a hand in Mr. Bakr's "luck" in the plot ballot).

On the other hand, by borrowing from a number of sources, the household might be able to playoff one lender against another or spread defaults around. With a single lending source, in the event of a default and subsequent foreclosure, the borrower stands to lose everything. Thus, the fear of signing away not just the house built from the loans but also their own land on which the house stands might deter borrowers from taking on a formal loan. Of course, informal mechanisms are often used simply because, for many would-be borrowers, there is no alternative.

Once the initial house or, more often, part of a house has been constructed, it will be added to incrementally over time, using many if not all of the above means of finance. However, this time around the initial construction will probably generate the main funding.

This happens in three ways:

(a) There are savings in rent which can be substantial in areas of housing shortage. On the other hand, they can be offset to some extent by increased transport costs, if the household has had to move away from employment in order to acquire land, and there may be high charges for services.

(b) Income can be generated either by letting out some or, even, - all of the recently-built accommodation or by using it to carry out income-earning activities, ranging from the opening of a shop to small-scale assembly and manufacturing operations.

(c) The achievement of the first stage of the construction acts as an incentive to the household to efforts in saving and income generation and also signals initiative and credit worthiness to friends, family and employer, making it easy to access those sources.

Task 2.2 EVALUATE EXISTING METHODS OF FINANCING FOR HOUSE-BUILDING

Objectives
To identify those of the currently used ways of financing house- building that could be incorporated in the Strategy.

Issues
What criteria should be used for incorporation of existing methods into the proposed strategy?

Definitions
CRITERIA - this means the items of a set of conditions that need to be satisfied, such as:

LEGALITY - refers to whether the method is legal or recognized as a bona fide way of obtaining finance.

ACCEPTABILITY - refers to whether the method is (or could be made) acceptable to most people in the target group.

ACCESSIBILITY - refers to whether the target-group population can and is able to use the particular method.

ELASTICITY - refers to whether the method is capable of coping with increased scale of operations that would be implied if it were incorporated in the Strategy.

Method
The purpose of this task is not to evaluate the currently used methods in terms of their efficiency or effectiveness in recovering loans, and degree or levels of defaults. The intention is to evaluate the methods to see if they should be included as a component of the proposed housing-finance strategy.

The following steps should be followed:

(a) Establish criteria for inclusion and incorporation. These are likely to include: legality, acceptability, accessibility and elasticity.

(b) For each of these criteria, the performance terms and levels that would meet the needs of the target group should be indicated. For example, under "acceptability", if the target group were Muslims who were unwilling to pay interest on savings or borrowings, a method that could not be converted into a risk-sharing operation, would likely be unacceptable.

(c) Columns should be added to the chart developed in the previous Task to provide a column for each criterion plus another column for Recommendation. The rows of the original chart should be extended on this new chart so that it can be filled in for each of the previously identified sources of housing finance.

(d) Each of the sources should be taken in turn, and their performance evaluated against the criteria established in the step (a) above. This evaluation should be used to indicate on the chart whether each source meets each of the incorporation criteria. This need only be done by a tick or cross or a brief note on the chart. Separate notes should be kept, summarizing the evaluation discussions.

(e) In the Recommendation column, reasons should be given if any method which meets half or more of the criteria is not to be incorporated in the strategy (see Rule-of-Thumb). The fact that a method is recommended at this stage does not mean that it will be included in the eventual strategy without modification, nor that it may not be left out later.

(f) If none of the current methods used meets even half the criteria, those that meet the most criteria should be chosen and the procedure in step (e) followed.

Information
From previous Task.

Rule-of-Thumb
If a method is being widely used, it should be possible to incorporate it in the strategy, provided the willingness is there to do so. Existing methods might not work for everyone in the target group, but if they provide a useful source of finance, they should be part of the strategy. A method or source should not be rejected simply because there are reasons why some households in the target group cannot use it, as that would deprive those who could.

Examples
An example of how this step was carried out for a typical case is shown in the box opposite.

Example Task 2.2: Evaluation or existing methods: summary chart

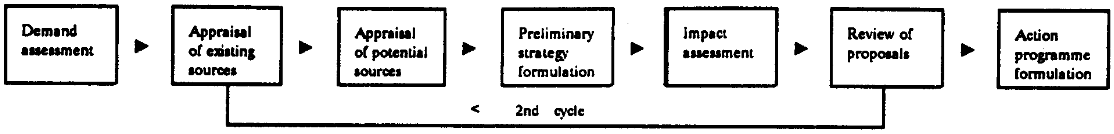
Summary chart

Source [Task 21]	**Legal**	**Acceptable**	**Accessible**	**Capable**	**Recommendation**
Relatives	yes	yes	yes	no	incorporate
Employers	yes	yes	limited	yes	incorporate
Material supplier	yes	yes	yes	no	incorporate
Committees	no	yes	limited	no	incorporate
HBFC	yes	yes	limited	yes	incorporate
Banks	yes	Limited	limited	yes	incorporate
Money lenders	no	no	no	no	leave out
Notes (The notes were used to record a summary of the discussions and decisions regarding each of the above sources, and shown below are extracts from the full set)					

Relatives
In the current social set-up, informal borrowing from relatives will continue to play an important and acceptable role. Even the poorest households will have access to some relatives who will be able to advance some money: the poorer the household, the less this amount will be, but the poorer the household, the more likely it is that the amount will be crucial. Most of this money will be interest-free (though not necessarily without obligations) and available at short notice. These amounts are particularly critical for those who have to make sudden or short-notice payments, such as to buy land, pay deposits etc. It is not thought that the amounts involved would ever be sufficient to meet all the needs of any household, and they would have to be supplemented by other sources.

Banks
Banks are not accessible to most of the households in the target group, and even those that can use them do so for short-term bridging finance. Even for these households, the procedures for obtaining a loan are very complicated, and are generally used as a last resort. Moreover, because of their restricted opening hours and locations and the fact that any money deposited with them is subject to being taxed, most households do not find them an acceptable source for funds. With some simplification of procedures, banks could be incorporated but would play a very limited role.

Stage 3: APPRAISAL OF POTENTIAL SOURCES OF FINANCE



Objectives
To identify those suppliers and ways of providing housing finance that are not currently used to meet demands of the target group, and to evaluate them for their relevance to housing-finance strategy.

Issues
Should *all* suppliers be surveyed, or can a preliminary selection help identify key potential suppliers? (See Notes: SUPPLIERS OF HOUSING FINANCE.)

Should the survey be limited to those suppliers that exist in the country, or should those from elsewhere also be included?

Definitions
POTENTIAL SOURCES: These include all those that are not currently being used by the target groups. They include those that exist locally but are not used by them, those that do not exist locally, those sources that are not currently used for housing finance and, also, those that need to be created.

Method
A chart, similar to that in the Example for this Task, should be used to identify and list all the suppliers of finance. Then, the steps below should be followed:

(a) For each of the suppliers, information should be collected on their source of funds, lending criteria, lending terms, past performance, assets, liabilities, location and quality of service. Brief notes on these should be entered in the respective columns. Not too much time should be spent collecting this information or clarifying details at this stage.

(b) Against each of the suppliers identified should be indicated whether their relative potential to meet the demands of the target households is high or low. [The criteria developed for Task 2.2 to evaluate existing sources (e.g., accessibility and acceptability) should be kept in mind.] The Notes: SUPPLIERS OF HOUSING & FINANCE can help make this assessment. Where the potential differs for the different target subgroups, this should also be indicated.

Information
Listings of potential formal financing suppliers are given in directories of various kinds, including business directories, such as the Yellow Pages of the telephone directory. Most of these institutions publish annual reports that will provide most of the information required, It is a good idea to ask each institution listed if they know or are aware of other institutions.

Potential informal financing suppliers are difficult to identify. In addition to the participants' own knowledge, there might be surveys or studies by financing, research and academic institutions that identify such suppliers.

Rule-of- Thumb
See Notes: SUPPLIERS OF HOUSING FINANCE.

Example
The example shown in the box on the opposite page has been extracted from an exercise and shows only some of the suppliers that were actually evaluated.

Notes
SUPPLIERS OF HOUSING FINANCE

There are a number of ways that the various suppliers of housing finance can be classified, for example, how they are owned and controlled (whether publicly, privately or mutually) and how they obtain their funds. Box 11 on the next page uses a classification based on the flow of funds to analyse a housing-finance system [5].

[5] This model has been taken from Mark Boleat's *National Housing Finance Systems.* London, Croom Helm, 1985

In the Notes below, a classification based on the nature of the suppliers of housing finance has been used to categorize them into:
- Specialist housing-finance institutions
- Other finance institutions
- International financing suppliers
- Informal financing suppliers

Example Task 3.1 Potential Suppliers of Housing Finance			
Summary Table			
Supplier	**Cooperative Bank**	**Building Societies**	**Savings and Loans Associations**
CURRENT STATUS	No housing-specific Cooperatives	The few that exist serve only upper-income groups	None exist in the country
SOURCE OF FUNDS	Treasury	Individual and institutional savers	Individual and institutional savers
LENDING CRITERIA	Lends only to properly constituted cooperatives which can be for any purpose recognized by the Co-operatives Act	Borrowers must be members for at least one	Borrowers must be members
LENDING TERMS	8 per cent over 10 years	10-15 per cent over15 to 20 years	10-15 per cent over 5 to 10 years
PAST PERFORMANCE	Recoveries have been generally good, particularly for loans given for income-generating activities	Mixed record of recoveries; best where societies work-based	With governmental, oversight, recoveries have been good
ASSETS	??	??	??
LIABILITIES	??	??	??
LOCATION	Head office in capital, branches in every District Headquarters	Operate in the capital and the largest city only	Potentially community based
QUALITY OF SERVICE	Mediocre; the Bank does little to promote itself or its services	Varies; well-run societies offer a good service to their members, others do little for them	Likely to be a function of the interest each community takes in them
POTENTIAL	Could easily be extended to include Housing Finance Cooperative Banks	On the basis of past record, unlikely to reach far enough down the income range for majority of target group members	Could be a way of formalizing some or the aspects or committees (ROSCAs)
NOTES [These are selected extracts from the Notes made during discussions and investigations of the potential sources]			

Specialist housing-finance institutions
These can be one of three types:

1. *Governmental or parastatal housing banks, authorities, corporations etc*. which have a large proportion of their funds from governmental allocations or through forced taxation/payroll levies on all or some individuals or organizations, but might also allow individual or institutional deposits. They may also borrow on the capital markets as well as being supported by external/international funding. Such institutions might provide financing for housing either in the form of funds against security or through the provision of sites and/or buildings on a hire-purchase or mortgage type repayment system. Their advantages are is that they provide long-term lending specifically for housing, often with built-in subsidies, and a very low rate of foreclosures or evictions of defaulters. They tend to exclude low-income groups from borrowing, though not from deposit-taking.

2. *As above, but established by the private sector.* Their main source of funds is likely to be deposits and bonds and/or debentures, though they might have governmental and/or external/international funding as well. They generally operate in the same way as the pub1ic-sector institutions, with similar advantages, though perhaps lower or no subsidies. Branch managers are likely to be able to exercise discretion and to take collaterals and defaults seriously.

Box 11. Types of finance systems

To work effectively, any housing-finance system has to raise money from those who do not intend to borrow and lend it over long periods of time. There are just four routes by which this can be achieved, two of which can only be partly successful and which do not make full use of the intermediation process:

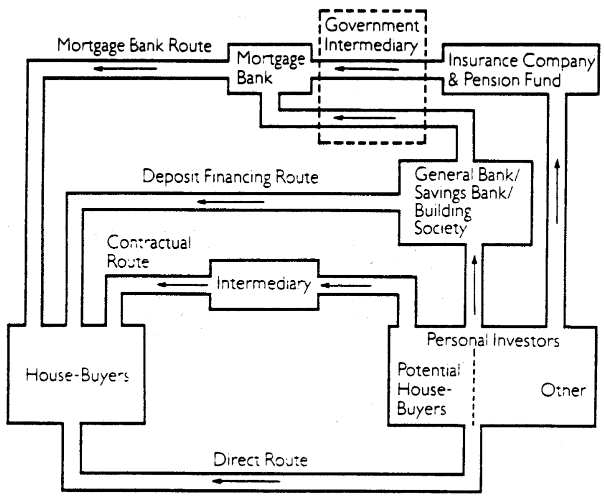
(a) The direct route, by which those who need funds to acquire a house obtain those funds directly from individuals with surplus financial assets, either because of a personal relationship or because of a business relationship, for example, a vendor may supply funds to a purchaser.

(b) A contractual route by which part but not all of the funds which a house-buyer requires is raised from the savings of other potential home-buyers or from other contractual savings schemes.

(c) The deposit financing route. by which short-term savings or individuals are channeled into long-term loans by intermediaries, usually retail banks, either general purpose or specialized in the provision of housing finance.

(d) The mortgage bank route, by which institutions making mortgage loans fund these by bond issues which are purchased by institutional investors and, to a much lesser extent, by individuals.

The four systems are illustrated below.



3. *Mutually owned organizations, societies and associations, such as building societies, savings & loans associations and housing co-operatives* which exist primarily as a means for their members to accumulate and access housing finance. Most of their funds therefore come from members' deposits, but they might also take other deposits as well as raise funds through the sale of bonds and debentures. Their advantage is that they can provide long-term lending specifically for housing. To be successful, however, they must have access to funds other than those of members seeking housing finance. The successful ones tend to cater for middle- income rather than low-income households.

Other finance institutions
These can be one of four types:

1. *Commercial banks* which are like the housing banks, except that their business is not dedicated to housing. They will typically provide short and medium-term finance, particularly .for bridging and construction finance purposes, including incremental building.

2. In*surance Companies,* whether Public, Private or Mutual, which will also lend for housing from their profits or because they are required to do so by law. It is possible to borrow from them using the policy as a collateral. Their advantage is that they can provide long-term finance. However, they tend to exclude low-income groups.

3. *Provident and pension funds,* particularly in the public sector, lending to individuals against expected future funds, they are most likely to divert some of their funds as (often compulsory) investments to other housing-

finance institutions. While they provide long-term lending, they tend to exclude low-income groups and those without regular employment.

4. *Credit unions and co-operatives* which use their own members' contributions and lend for a variety of purposes that could include long-term lending for housing out of surpluses. They also could include low-income groups and might lend at lower interest rates than commercial organizations.

International and external financing:
This can be by foreign governments and (their) agencies, and international or regional development banks, agencies or institutions. Most of them have the advantage of having capital, particularly foreign exchange, which can be made available on soft ~ terms. They specialize in lending for specific projects, such as for resettlement, infrastructure or seed capital. The availability of foreign exchange at relatively low rates can be an incentive to accept loans which they can use for other purposes, while providing equivalent local currency financing for housing. The main disadvantage is where they have to be repaid in foreign exchange, and generally their lending is short or medium rather than long-term.

Informal suppliers of finance
There are three categories of suppliers:

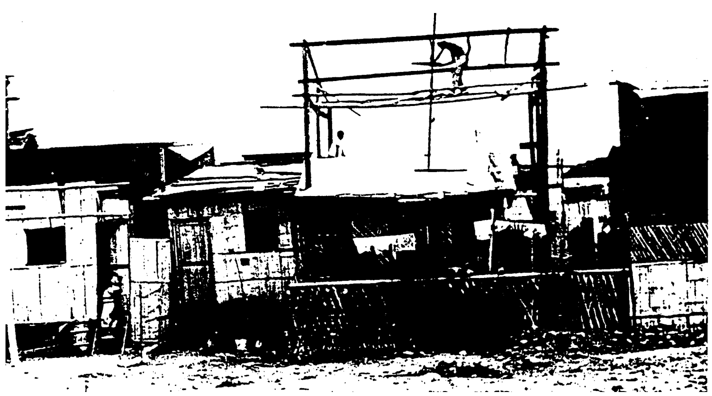
1. *Individual,* who might be the borrower's employer using own resources or acting as an intermediary, perhaps as a guarantor; a moneylender who is usually a lender of last resort, given the exorbitant rates of interest and strict enforcement against defaulters; or patrons who use low-income families as a front to obtain access to housing which they can then use all or part of for subletting. While having the advantage that they provide lending to low- income families that have no other source of finance, their terms are generally harsh. The employee might even find that the house is also lost if employment is terminated.

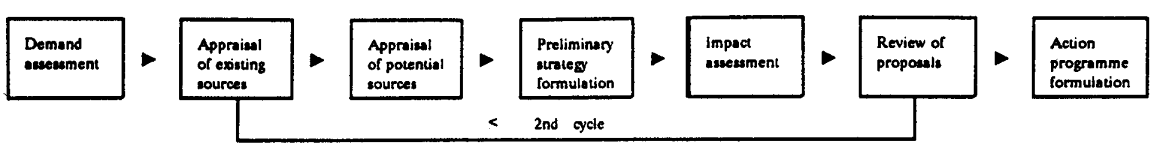
2. *Informal,* usually unregistered societies and groupings which provide rotating credit for their members, usually not enough for housing but useful for incremental building or for short-term bridging purposes. These reach the low-income groups and are based on mutual trust and experience rather than eligibility criteria. The saving and repayment experience gained in this way can be useful for expanding or extending to a formal institution.

3. *National and local voluntary and non-profit organizations* which may undertake to provide housing as a special/specific project. They have limited funding but can reach the low- income groups, often providing innovative solutions.

(See also: Notes for Task 2.1)

Stage 4: PRELIMINARY STRATEGY FORMULATION





By this stage a number of sources for improving the provision of housing finance to the target households will have been analysed, and those that are considered appropriate identified. The purpose of this set of tasks is to bring these together in the form of a package. Before this package can be finalized and detailed, its impact and implications considered, and its implementation programmed, it is useful to set out in outline what the package consists of, so that any obvious conflicts and confusions can be identified and resolved. Much of the work, therefore, consists of bringing together the material of the previous tasks and adding to it the necessary supplementing and supporting activities and actions of households and the government.

Task 4.1 PRELIMINARY STRATEGY PACKAGE

Objectives

To bring together the various existing, modified and proposed sources of financing house-building in the form of a strategy package.

Issues

Should all conflicting or contradictory actions be removed, or will some contradictory actions help increase choice or access?

What is the appropriate level and degree of detail, when outlining the action required?

Apart from selecting appropriate suppliers of housing finance, what can be done by the households themselves. How can governments support them? (See Notes: LOW-INCOME HOUSING FINANCE TECHNIQUES).

Definitions

n.a.

Method

A chart should be drawn based on the Example in the box, with two columns headed STRATEGY and ACTION. The chart should be divided horizontally into three sections, and the following steps taken:

(a) The first section of the chart is headed SUPPLIERS. The outcome of Task 2 and 3 should be used to list all the sources of housing finance to be incorporated in the Strategy. These should be entered in the first column, and the necessary modifying actions (if any) in the second column.

(b) Next, the chart should be checked to see whether there are any instances of a set of actions suggested in column 2 contradicting or conflicting with any others. For every such instance, it needs to be decided whether both should proceed, or whether one should be modified or eliminated.

(c) The middle section, headed HOUSEHOLDS, should be used to list the various activities required of the households, in order to improve their access to housing finance. These will range from making and depositing savings, to joining or establishing cooperatives, to regularizing titles, to embarking on income generating enterprises. See the Notes: WAYS OF FINANCING HOUSEBUILDING (Stage 2) for likely activities. Other suggestions will have come from the surveyor through informal discussions. Yet other activities will have to be undertaken in response to the modifications and actions suggested in the section on SUPPLIERS above.

(d) In the second column should be indicated the actions required to be taken by households and others, including the government, to ensure that the activities required of the Households can actually be undertaken.

(e) In the last section, headed GOVERNMENT, the activities required of the various levels and departments of government should be indicated. Some of these will be repetitions of or in response to the actions indicated in the other two sections, but there will be other activities which the government could undertake in order to facilitate housing finance.

(f) Again, in the second column of this section, the actions needed to perform the activities listed in column one should be indicated.

All the entries should be kept brief. Any details that there might be should be kept in separate notes for use later.

Information
Output from Task 1, 2 and 3, supplemented by the accompanying deliberations and judgements.

Rule-of-Thumb
n.a.

Examples
The figure on the next page gives an extract from an exercise based on the data and results of the example developed in the previous tasks.

Example Task 4.1 Preliminary strategy package

The preliminary strategy package is based on three inter-related sets of actions:

1. The establishment of a savings-for-land scheme (SLS), whereby those that want housing plots can invest at a lower-than-market rate of interest against a guarantee of having. access to land for housing. This scheme will obviously be of most appeal to those who do not currently own land, though even some of those who own building plots may also use this to save small irregular amounts. Savers will be able to withdraw their funds at any time, However, once their savings reach the plot price (currently calculated at Rs.3000 for an 80 sq. m plot), they can then use their savings book to register for a plot of land. The development authority will guarantee to provide a plot within one year of registration.

2. The development of an incremental housing programme (IHP) which will require the urban development authority to acquire government land, using funds accumulated in the SLS, and lay it out in blocks. The only infrastructure to be provided initially will be water mains and graded main roads. Further infrastructure will be provided only as and when demanded by each street, provided that they have by then deposited the requisite amount in their Street Development Fund (SDF). The charge per household to cover all infrastructure (currently Rs.9000) is made up of the cost of providing the different components, and these may be 'bought' gradually by the street.

3. The development of a community-based savings and loans association (CSA) which will lend to its members amounts not exceeding the cost of building one room (currently Rs.15,000). These loans will attract a market rate of interest (currently I5 per cent) and must be repaid within five years. For those at the bottom end of the target group, this would mean devoting under 30 per cent of their income to repayments. Once the first loan has been repaid, the member automatically becomes eligible for a subsequent loan. A three-room house could thus be built within 15 years.

The actions required for these strategies (by the Suppliers) are set out below (similar charts were drawn for action required by Households and by the Government):

A. SUPPLIERS [Land; Finance]

STRATEGY	ACTIONS
SLS	a. allow for “participating institutions” to handle deposits b. advertise/publicize scheme, inspire confidence in savers
IHP	a. institute speedier procedures for acquisition, lay-out b. establish simple procedures for accessing/occupying plots c. establish cadre of resident community'-development officers
CSA	a. establish community savings and loans (under Coop Bank ?)

Notes
LOW-INCOME HOUSING-FINANCE TECHNIQUES

Whatever method is chosen for housing finance, there are a number of policies that can be adopted to ease the difficulties of low-income borrowers.

These are some things that only government can do:

(a) Incremental construction standards could be introduced for houses below a certain size or cost, to allow for the construction of "starter houses", so that households can gain a foothold in the housing market, with units that can be gradually improved and extended.

(b) If one-room houses occupying less than a third of the plot area were exempt from all building controls, households could build a minimum shelter quickly and very cheaply. Two-room houses (whether new or through improvement) would be subject to basic controls, and three rooms and over would be fully subject to building controls. The idea is that, before the house could be enlarged, the existing construction would have to be improved.

(c) Services could also be provided incrementally, reducing up-front costs to households. Costs could be minimized, if, initially, only a basic level of infrastructure was provided sufficient to meet basic demands of health and hygiene. These could be added to as households paid their share of the development costs for upgraded infrastructure. Land and property taxes could be increased gradually, to reflect these improvements.

(d) Similarly, access to land could be simplified if users could "borrow" the capital sum and pay only the interest on the land price while they used it. For example, land could be provided by the government at an "annual rent" equivalent to or only slightly higher than the interest on the purchase price. The household would have the option to purchase the land at any time at its originally agreed price. Thus, households would have unsubsidized access to land cheaply and, yet, could acquire full title, when they required, upon payment of the capital. While it is true that, at that future date, the land might be many times its original price, in effect, the price of the land would already have been "paid" with a loan. At the time of future purchase, it would be the principal that was being repaid.

The government is also, perhaps best placed to provide guarantees to a lending institution, to the extent that it has low-interest or grant funds available. The Government could make these available, to mix with market-rate finance.

A housing-finance institution could consider a package that allows for one or more of the following:

(a) It could make loans to developers for low-cost rental housing, including the construction of single-roomed units in a single compound, sharing facilities. It should allow for the construction of single-storey condominiums for low-income households. At present, such housing is only available through the "informal sector".

(b) It could make loans for repair, extension, improvement and upgrading. These would support the sequential building and improvement processes currently employed by low-income households. Access to finance would mean that they could be built to good standards or the sequence could be speeded up.

(c) It could make sequential loans, when an additional loan is made on repayment of the first. Currently, many lending schemes exclude those who have had previous loans. This is acceptable only if the loans are subsidized and the purpose is to spread the subsidies; however, without subsidies, such a restriction eliminates those who demonstrate their credit-worthiness It also encourages taking loans larger than the borrowers can actually afford, since they know they will not get another chance.

(d) It could issue sequential mortgages (or other security documents) that make such loans possible.

(e) It could make group mortgages, that is, loans to a specified number of people all of whom are responsible for repayment. This both spreads the risks and lowers costs, through the administration of a large single loan rather than a number of small individual ones.

(f) It can make loans to cooperatives or similar community based institutions. Where these exist or can be created, they offer even greater safeguards than group loans but, equally, might require training and technical support to run the institutions.

(g) It can introduce variable-repayment options, by which unequal payments can be made, as funds permit. This is particularly important where the borrowers do not earn regular incomes. Administrative overheads could be minimized, if the payment was in the form of books of saver stamps, using existing Revenue stamps. These could be checked periodically, to equate them with "regular" payments if required.

(h) It could institute a collection service, to make payment easy. If borrowers did not have to go to the institution, but the institution (or its agent) went to the borrower, repayments would increase and become more regular, owing to the added pressure and convenience.

(i) It could finance building contractors or community savings associations, as suppliers of building materials. If materials suppliers could, as a result, buy in bulk, this might help lower costs to households, if some of these savings were passed on to them.

(j) It could issue building materials loans as credits. This could ensure that housing loans were actually used for construction and, if properly : handled, could also reduce costs by reducing paperwork.

(k) It could accept guarantors to support applications. This could be particularly useful, where the borrower could not furnish adequate collateral.

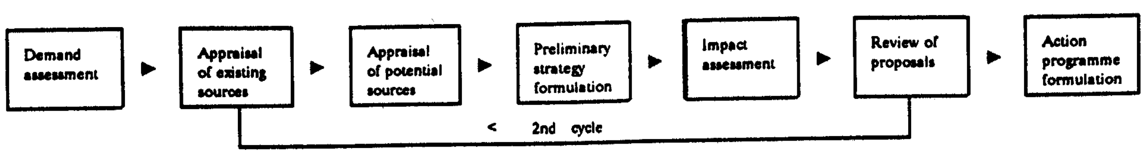
(l) It could make loans to purchase land, using the title as security. Currently, most financial institutions ask for a valid title before lending. This excludes poor households who do not have the capital to buy land.

(m) It could streamline legal procedures. In many cases the difficulty of initiating due processes leads to a reluctance to lend, since there is little chance of enforcing repayment or ensuring possession, in case of default.

(n) It could give low start mortgages on which the amount due increases throughout the repayment period -see box 12 below.

Box 12. The accelerated repayment mortgage
Sometimes known as the "low start" or graduated payment mortgage, this method provides for the monthly repayments to increase at a regular amount throughout the repayment period. This enables the initial repayment to be lower than in a conventional mortgage, and, so, households with lower incomes can become eligible to borrow. The reasoning is that, over a loan period of 20 to 30 years, both incomes and property values (through inflation) are going to increase and that this fact should be taken into account. In the early years, repayments do not cover interest due, so that the amount of the capital increases, and this might put the r lender at risk if the loan is near 100 per cent of value, and recovery had to be made. With rising property values in most places, the risk is probably small.

STAGE 5: IMPACT ASSESSMENT



Stage 5: IMPACT OF PROPOSED HOUSING-FINANCE STRATEGY

The outline housing-finance strategy proposed in Stage 4 will, of course, have an impact on the provision of housing finance for the target group. However, there will be other impacts on the economy and society as a whole. Some of these may be positive and help reinforce what is to be achieved, but some may be negative, and not wanted.

If these positive and negative impacts can be identified in advance, it is easier to initiate appropriate action. Thus, for example, a tendency for arise in the price of building materials can be minimized if not eliminated if action is taken to increase their supply.

Such additional action should, of course, also form part of the strategy and policy proposals, and should therefore be incorporated in the action programme in Stage 7.

Task 5.1 EVALUATE IMPACT ON HOUSEHOLDS

Objectives
To estimate what the impact of the proposed strategy will be on (target) households, and pre-empt negative effects.

Issues
Should the evaluation of the impact be limited to the target households, or should other households also be considered? (See Notes: IMPACT ON HOUSEHOLDS OF INCREASED ACCESS TO HOUSING FINANCE.)

Should only "first-round" effects be considered? If not, how can the impacts be measured?

How accurate is the assessment likely to be?

Definitions
HOUSEHOLD FORMATION: This is the establishment of new households. Members of an existing household may break away and establish their own household, either because of changes in their own, or their household's, circumstances (e.g., reaching a particular age; change in marital status; increase in household size; change in economic/occupation status; death or departure of one or more members), or because of changes in the world around them (e.g., changes in the availability of affordable/suitable housing).

SAVINGS BEHAVIOUR: The ways in which households save, including how and where they save, and the reasons for saving.

PROPENSITY TO SAVE: The likelihood that a population or group will save rather than spend extra income. It is generally assumed that the higher the income level, the more likely it is that additional income will be saved rather than consumed, since a relatively smaller share of the income is spent on absolute essentials which cannot be cut back.

Method
The following steps should be followed:

(a) On a chart based on the example to this task, the three rows should be headed: Household formation; House size/type; and Savings habits. The rows should be labeled Households and houses; Likely impact; and Action recommended.

(b) The matrix should be filled in with reference to the proposals (see Task 4.1) regarding modifications to existing financial institutions and new institutions.

(c) If the housing-finance strategy is implemented and works as intended, it will have an effect on housing and influence households. In particular, it will effect their savings habits (see NOTES below).

Discuss [(6)] the likely impact on household formation; house size/type; and savings habits. The best guide will be to draw upon the experience of previous instances in which easier access to housing has been achieved. The survey done as part of Stages 1 and 2 will also give an indication of the pent-up demand and, therefore, the likely impact of the proposals. Notes should be made summarizing the discussion.

[(6)] During the first cycle, these are more likely to be in the nature of classroom discussions, but in the second cycle, they should include other experts, such as the households, community development officers. NGOs, etc.

(d) The discussions should be used to indicate what is thought likely to happen as the result of each of the proposals. This should be entered briefly in columns two to four (the three 'Impact' columns). Where the impact is likely to be different for the various sub-groups, or limited to some of them, or perhaps is only on non-target households, this should be indicated.

(e) Consider what action, if any, needs to be recommended to minimize the adverse effects and capitalize on the desirable aspects of the proposals. Obviously those proposals that are likely to produce an adverse or undesirable impact will need counteracting, but some proposals might produce an impact which, while not negative, will need to be taken into account. For example, if more households are formed, this could affect the calculations of target numbers. If other households also start saving, then this could increase the number of loans that could be given at anyone time. In these cases too the necessary action needs to be indicated. The recommendations should be listed in the last column.

Information

Indications of the likely impact are most likely to be found in reports of what happened when similar measures were introduced in the past.

Housing and sociological studies may provide information regarding household formation rates. An indication of pent-up demand for household formation may be obtained from census findings of overcrowding or increasing household size.

Housing reports may also provide information on likely changes to house types and sizes. Such information may also be available with housing agencies and professionals dealing with low-income housing.

In the absence of any past experience as a guide, it may be necessary to undertake a small "market research" type of survey of households which are representative of the target groups. Such a survey need not take more than half a day and could be limited to as few as 10 households per group, giving a total of perhaps 50 households.

Rule-of-Thumb

See NOTES below.

Examples

See figure below which shows an example for Task 5.1

Example Task 5.1 Impact on households and houses		
ASPECT	LIKELY IMPACT	ACTION RECOMMENDED
H-Hold Formation	More easily available funds could speed up process of splitting and sub-dividing of households.	Cater for the possibility of increased demand from younger households, first time investors
H-Hold Saving	More households will start savings, particularly with SLS, but also with other institutions	Cater for small irregular investors
Houses	Less overcrowding More likely to look messy with more incremental construction taking place	Permit/legalize subdivision of plots, buildings Develop cadre of building facilitators to replace inspectors

Notes

IMPACT ON HOUSEHOLDS OF INCREASED ACCESS TO HOUSING FINANCE

Given that increased access to housing finance will make housing more easily available to more households, the following impacts can be anticipated:

(a) **Household formation**

To the extent that the proposals allow for more households to have greater access to housing, it will encourage existing households to undertake house construction/acquisition. It will also encourage people to form more, though probably smaller-size, households.

Restrictions on the supply of housing units are likely to reduce the rate of new household formation. Households will tend to grow larger rather than split. For example, instead of setting up their own household, shortage or costs of housing may oblige a newly-married couple to remain with one of the parental households. Similarly, elderly parents may give up their independent household in favour of the more economic option of becoming incorporated into one of their children's.

Increasing the supply of, or access to housing may encourage more adult children to set up their own independent household, even before marriage.

It is not suggested that most housing-finance strategies are likely to have a profound impact on household formation, but rather that it is likely to modify or reinforce existing tendencies.

(b) **Housing types/Sizes**

The proposed housing-finance strategy will make available more funds than are currently available to households and is likely to encourage the construction of larger and more elaborate houses. (Though see Task 5.2 for impact on housing markets).

Obviously, if the financial institutions lay down criteria regarding house size or type, then it is likely that they will be followed. For example, if the terms and conditions do not allow for condominiums or other forms of joint ownership, then bungalow type detached housing is likely to increase. On the other hand, the financial institutions may only lend for housing that meets planning and building codes. However, if these are not easily enforceable, or there is a tradition of flaunting them, such stipulations may have little impact.

(c) **Savings behaviour**

The housing-finance strategy is likely to use savings as a means for households to gain access to housing markets. If this includes assistance for households to accumulate required deposits, or to improve their credit rating, it will encourage more households to save and existing savers to increase their savings.

The general experience has been that, given an incentive to save (e.g., for marriages and housing) even very poor households will save at levels quite above those which may be supposed by their general economic situation. See box 13 below.

Box 13

India's Housing and Urban Development Corporation (HUDCO) carried out a survey of economically weaker section (poor) households, six months before they joined a hire-purchase housing scheme. The same group was interviewed six months after they had moved in, with a view to evaluating the impact of having to make regular monthly repayments. While expenditure on the first two items is predictably reduced, and expenditure on 'rent' is increased, what is surprising is the increase in savings. One explanation may be that it is to allow for the purchase of consumer durables, or more likely, that it is a hedge or safety valve against the time when the household may be unable to earn the amount required to make the repayment. Unfortunately item 2 is a large grouping that does not allow us to pinpoint the real areas of savings.

Expenditure	Percentage of income six months before	Percentage of income six months after
1. Food items	63.8	56.8
2. Education, entertainment, clothing, books, transport	30.4	19.0
3. Rent/monthly repayment	5.8	17.9
4. Savings	zero	6.3

If changes are made in the operations of the savings institutions which make it more convenient for households to save, this will further reinforce the trend for housing-motivated saving efforts.

If the new or modified savings institutions proposed by the strategy offer better or easier opportunities of access to housing than other (existing) institutions, they are likely to divert savings and savers to them. If the *general* economic benefits offered by these institutions are more attractive than those of other institutions, they will also divert savers and savings from groups other than those seeking housing. Such benefits are not limited to rates of interest, but also have to do with security, ease of access and tax benefits.

If such institutions are exclusive to the target group, their impact on other households may be limited. However, the greater the differential in benefits that is available to the target group, as compared to the rest of the population, the more likely it is that ways will be found by those outside the target group to participate (but see also Task 5.3 for impact on financial markets).