QUICK GUIDES FOR POLICY MAKERS

housing the poor in Asian cities

UN-HABITAT

United Nations ESCAP

5

HOUSING FINANCE: Ways to help the poor pay for housing

ISBN: 978-92-113-1944-6
HS/957/08E Housing the Poor in Asian Cities, Quick Guide 5

Cover design by Tom Kerr, ACHR and printed in Nairobi by the United Nations Office at Nairobi

Cover photo by Asian Coalition for Housing Rights

The publication of the Housing the Poor in Asian Cities series was made possible through the financial support of the Dutch Government and the Development Account of the United Nations.

Published by:
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Acknowledgements

This set of seven Quick Guides have been prepared as a result of an expert group meeting on capacity-building for housing the urban poor, organized by UNESCAP in Thailand in July 2005. They were prepared jointly by the Poverty and Development Division of UNESCAP and the Training and Capacity Building Branch (TCBB) of UN-HABITAT, with funding from the Development Account of the United Nations and the Dutch Government under the projects “Housing the Poor in Urban Economies” and “Strengthening National Training Capabilities for Better Local Governance and Urban Development” respectively. An accompanying set of posters highlighting the key messages from each of the Quick Guides and a set of self-administered on-line training modules are also being developed under this collaboration.

The Quick Guides were produced under the overall coordination of Mr. Adnan Aliani, Poverty and Development Division, UNESCAP and Ms. Åsa Jonsson, Training and Capacity Building Branch, UN-HABITAT with vital support and inputs from Mr. Yap Kioe Sheng, Mr. Raf Tuts and Ms. Natalja Wehmer. Internal reviews and contributions were also provided by Ms. Clarissa Augustinus, Mr. Jean-Yves Barcelo, Mr. Selman Erguden, Mr. Solomon Haile, Mr. Jan Meeuwissen, Mr. Rasmus Precht, Ms. Lowie Rosales, and Mr. Xing Zhang.

The Guides were prepared by Mr. Thomas A. Kerr, Asian Coalition for Housing Rights (ACHR) based on documents prepared by Mr. Babar Mumtaz, Mr. Michael Mattingly and Mr. Patrick Wakely, formerly of the Development Planning Unit (DPU), University College of London; Mr. Yap Kioe Sheng, UNESCAP; Mr. Aman Mehta, Sinclair Knight Merz Consulting; Mr. Peter Swan, Asian Coalition for Housing Rights; and Mr. Koen Dewandeler, King Mongkut Institute of Technology, Thailand.

The original documents and other materials can be accessed at: www.housing-the-urban-poor.net.

The above contributions have all shaped the Quick Guide series, which we hope will contribute to the daily work of policy makers in Asia in their quest to improve housing for the urban poor.

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One community dollar equals a thousand development dollars. Why? Because that community dollar represents the commitment of thousands of poor people to their own development. When development comes from people's own savings it is theirs, they own it.

Jockin Arputham, SDI


PHOTO: ACHR

Housing finance: Ways to help the poor pay for housing

QUICK GUIDE FOR POLICYMAKERS NUMBER 5

The objective of this Quick Guide is to introduce some of the key concepts of housing finance and to provide a quick overview of how housing finance works, especially as it relates — or fails to relate — to the urban poor. The guide presents information about both the formal and informal systems of delivering housing finance, and examines the key advantages and drawbacks of both systems when it comes to directing housing finance to the city's poor.

The basic mechanisms of formal and informal housing finance systems may be similar, but by removing many of the barriers that make the formal system inaccessible to the poor, the informal system has in many places become the chief system for delivering what meager housing finance does actually reach the poor. The guide closes with a brief description of some new and unconventional housing finance strategies being tested and expanded in Asia, which are attempting to link formal sources of finance with poor communities and the informal systems by which they live their lives and build their housing.

This guide is not aimed at specialists, but instead aims to help build the capacities of national and local government officials and policy makers who need to quickly enhance their understanding of low-income housing issues.

PHOTO: ACHR

Housing mismatches:

So far, no system in the world has been able to perfectly match the great variety of housing needs with actual housing production. There is almost always either a surplus or a shortage, and many households end up having to live in housing that is not quite what they need, what they want or what they can afford.

Housing conditions and the need for housing finance

Housing comes in all shapes and sizes, including blocks of low, medium or high-rise flats, rental rooms, row-houses and free-standing houses. To accommodate a wide range of housing needs and a growing population over time, a city needs to provide a steady supply of new housing and expand the existing housing supply. Housing which grows too old or too deteriorated to be habitable also needs to be repaired or replaced.

A housing unit can be built by a household itself, or by a carpenter or small contractor that a household hires. Housing can be built by developers for profit or by government agencies. And housing can either be sold or rented, under a variety of rates, arrangements and payment terms.

You don't have to study Asian cities very long to realize how serious their housing problems are, and how many urban households simply cannot afford decent housing of any size or shape. In most countries, large portions of the urban population cannot afford adequate housing, and are having to make do squeezing their households into smaller and smaller housing units, or living far from work on the periphery of town, or building their own houses or renting shacks in slums or squatter settlements. (*See Quick Guide 2 on Low-income housing*)

The shortfall of housing is primarily for low-income housing, where the popualtion is the least able to pay for rising land and housing construction costs and where the market has not been able to provide affordable housing in locations where poor people can access employment and others services.

So, shelter is not affordable to the poor, and this is where housing finance becomes so important. Options to afford housing are needed that can meet the scale required in the context of rapid urbanization. Especially needed are different housing finance mechanisms that can reach the poor. The role of housing finance is also gaining importance as governments are becoming less concerned with direct provision of housing, and acting more in the role of enabler, including working with finance to provide more housing choices for people in cities.

Who produces housing in Asian cities?

1 Owner-built housing: Housing as something people make themselves

The majority of houses in Asian cities are not built by the government or the private sector but by the people who live in them. Owner-built housing is still the most popular form of housing production in the region, among all income groups and across all types and qualities of housing. There are good reasons for this: when people build themselves (or hire their own carpenters, masons or small contractors to build for them), they can control the whole process and build the house which precisely suits their tastes, their needs, their aspirations and their resources. Another advantage of owner-built housing is that it allows households to find creative ways of helping pay for their houses. If they have enough land, households will often build more than one housing unit and sell-off or rent the additional units, as a way of offsetting their house construction costs or generating a long-term income.

In the absence of any effective, large-scale response to housing shortages by the state or the private sector, the urgent housing needs in Asian cities are being addressed by the poor themselves, through the housing they build in informal settlements. More than half the population of many Asian cities is now living in informal settlements. The enormous stock of affordable housing which these slums and squatter settlements provide may be insecure, of poor quality and badly-serviced, but by housing their workforces, it has enabled cities to grow and prosper. There is an urgent need to upgrade these informal settlements into better-serviced and secure neighbourhoods.

There are many lessons to be learned from this people-produced housing delivery system. These include how to understand better the housing needs of the urban poor, and how to help their informal housing supply systems work more efficiently and equitably. *(See Quick Guide 2 on Low-income Housing).*

Housing is a process

For people from all income groups — *but especially for the poor* — housing is not a product, but a process. It's not something that is completed all at one time according to a plan, but is developed in stages, as a household's needs and resources change. Many complain that the sub-standard housing you find in slums, which is often built in this incremental way, is not acceptable. But this kind of housing represents an extremely delicate expression of poor people's gradual capacity to climb out of poverty. Like the houses they build, it's not something that happens all at once. But in cases where housing finance and secure tenure are made available to people, the quality of owner-built housing — even at the bottom-end of the economic ladder — can improve dramatically.


PHOTO: CODI

2 Government-built housing: Housing as something the state supplies

In various countries and at various times, governments have tried to act as the main producers of housing, usually in the form of subsidized apartments in low, medium and high-rise blocks, and in large housing colonies at the periphery of cities. It was thought that this kind of mass-produced public housing could be produced cheaper and faster by governments, through economies of scale. But most government-built housing is not cheap at all, nor is it mass-produced enough to be able to meet more than a tiny fraction of actual needs. Many governments have now adopted a more realistic *enabling* approach towards housing, and are attempting to increase the supply of housing by shifting from a focus on constructing housing to supporting the housing production of others, such as the private sector, cooperative societies, or individual households themselves, with help from various regulatory and financial tools.


PHOTO: ACHR

3 Government-built social housing: Housing as a form of subsidized welfare

For those who cannot afford to own or rent acceptable housing through the formal sector, social housing that is rented at subsidized rates has long been a housing policy option. Governments are often a key producer of social housing, but are not the only one to supply social housing: there are also social housing projects developed by cooperatives, charities, housing associations, employers and universities.

Subsidizing the housing of a city's poor population can help these households to survive. But social housing also indirectly subsidizes private-sector employers, since it allows them to continue paying below-survival wages to their workers, while still keeping their production costs low and profits high. If only a small percentage of households in Asian cities were in need of adequate housing, social housing might be a practical solution. But the reality is that a great majority of urban poor households can't afford formal sector housing of any sort, and their housing needs are far too big for governments to be able to meet in this way.


PHOTO: BASPANA - KAZAKHSTAN

4 Private sector housing: Housing as a commodity people buy or rent

In almost all Asian cities, private sector developers are becoming major housing producers in three ways:

- **As suppliers** of components of housing such as land, finance, building materials and labour.
- **As contractors** which build houses for individuals or government agencies.
- **As producers and sellers** of houses as commercial, speculative products.

PHOTO: ACHR

In many Asian cities, a lot of the housing being produced by the private-sector is built "to order" for individual clients, but speculative housing by developers is a growing industry. Many developers also sell not-yet-built housing units in a project to people who sign up to make lump-sum payments at intervals, as a strategy for financing the construction in stages. While this reduces the developer's risk, it shows how hard it can be to obtain finance for a housing project.

5 Private sector rental housing: Housing as a flexible option

In most Asian cities, rental housing plays an important role in urban housing, particularly for those who cannot afford a house, who may not be ready to settle down in one place, or for whom a permanent house may be a lower priority to saving or sending money home to the village.

In most Asian cities, there are viable, vibrant rental housing markets for all income groups. At the bottom end, there is an enormous informal market of rental rooms and land plots in slums and on private land. These small rooms or subdivided units may offer crowded, sub-standard living conditions, but they are cheap and available and represent an important survival option for many poor and migrant households. *(See Quick Guide 7 on Rental Housing).*

PHOTO: ACHR

4 ways to reduce housing costs

The cost of housing represents a huge expense for most households, compared to what they earn. Reducing the cost of producing housing, therefore, is one way of reducing the financial burden on people's shoulders. The main components of housing are land, the housing itself and infrastructure services. There are many ways of providing these different components, or reducing their costs — altogether or separately. *(See Quick Guide 3 on Land).*

1 Mass producing housing units on a large scale

There are many variables in any housing construction process, and the amount of cost-saving in a mass-produced housing process will depend on the current costs of land, labour, materials and equipment. Most mass-produced housing falls into two categories:

- **High or mid-rise blocks of apartments**, where land costs are brought down by building more units on a small piece of land, and by standardizing the housing units and reducing construction costs through economies of scale. But while building a 12-story block of apartments might be the obvious way of bringing down per-unit land and construction costs, a high-rise building may also have higher social and economic costs, which make them work less well for the poor. High rise apartment buildings may be suitable housing for middle class and upper income households, who use their houses for living purposes only, but problematic for the poor, who use their housing for both economic activities and shelter.

- **Detached or semi-detached houses**, where costs are reduced mainly by building the same standard unit many times and making use of economies of scale.

2 Self-building by people

Supporting people to build their own housing is one of the best ways of reducing costs, making housing affordable to low-income households and creating a vibrant housing stock in our cities. Self-building allows households to build flexibly and incrementally, as and when they have a need or have the funds. Self-building remains the chief means for poor households to bring down the costs of their housing.

Don't take the term self built too literally, though

Many urban poor households are too busy earning their living to build their own houses, or they don't have the skills to build a good house. So thriving markets of small informal contractors, masons, carpenters, plumbers, electricians and materials suppliers tend to blossom in every city to serve this low-end of the housing sector.

Even if they aren't doing the work themselves, the house-owners manage the process and are in control of all aspects of their housing production, and often contribute their labour. And ultimately, the costs of self-built houses will match the house-owner's available resources.

3 Introducing more practical, more realistic and more flexible building standards

Many argue that one of the reasons why housing in our cities is unaffordable to so many is because housing and building standards are too high: roads are too wide, plots are too big, setbacks eat up too much space, engineering standards are too conservative and service levels are too high. If all these well-intended regulations were actually followed, housing of a very high standard might result, but it would be too expensive for most people in the city to afford.

Many of the urban housing standards in Asia are based on those in developed countries. Most of these standards have been written for housing that is produced by private-sector developers and is aimed at middle-income households. It is reasonable to expect that where private-sector developers build large-scale, high-rise housing for well-off households, housing and building standards need to be high. But when poor households build their own houses over time, these affluent building standards don't make a lot of sense.

What happens in most cases is that people don't follow the rules — whether they are rich or poor. In cities like Bangkok, Mumbai, Manila or Jakarta, you will be hard-pressed to find a single building which follows all the rules — from the richest person's mansion right down to the shacks in a slum.

One way to reduce housing costs is to introduce more appropriate and more flexible building standards, which better match the needs and realities of poor. And one of the best ways to do this is to make room for poor communities to be involved in framing their own local building standards through practice — and then negotiating with their governments to get these standards recognized.

Another way is to replace the conventional system of strict building inspection and control mechanisms with a system of facilitation and support. It is important to remember that the purpose of building standards is not to punish households but to improve their housing and make it more safe and effective.

PHOTO: UNESCAP

4 Introducing standardized building components and appropriate technologies

Another way to reduce building costs is to introduce and help popularize the production and use of standardized building components such as pre-cast beams, columns, piles, roof tiles, ceiling panels, door frames and septic tanks in the construction industry, so that a household can purchase them off the shelf and assemble them on the site. These components are mass-produced, and enjoy similar economies of scale as mass-produced housing. This kind of mass-production of simple building components can also be set up on a smaller scale, within poor communities themselves, by local entrepreneurs, with a little bit of training and technical assistance.

3 concepts to understand about affordability

1 The ability to pay for housing

Even after using all kinds of cost-reducing measures, housing will still be expensive. And that means people who want to build or buy a house will have to borrow money. How much money a household can borrow (and therefore what kind of housing they can purchase or build) depends on their ability to repay a loan. Affordability is a key to getting housing to low-income groups in cities. Making housing more affordable often means improving people's access to additional resources (like loans), so they can afford housing they couldn't otherwise pay for. Housing professionals have three ways to determine how much a household is able to pay:

- **By using a percentage of their monthly income**. This is based on average payments made by other households in similar circumstances. This method of determining ability to pay is the easiest and most frequently used. The rule-of- thumb for low-income households is to use a figure between 20% and 40% of monthly household income — usually 30%. However, spending 40% of the monthly income on housing is very high for poor households who may also have to spend half their income on food as well as other costs such as transport and school fees.
- **By subtracting expenditure (including current rental or housing expenses) from monthly income, to determine ability to pay.** This method may be more accurate, since it takes into account a household's income and expenditure, and therefore better reflects their economic realities. But in practice, such individual measurements of ability to pay are seldom made. Instead, averages across the group are used to determine how much households can pay, and these averages tend to be higher than many can actually afford to pay.
- **By letting the household decide.** This method is the best, because it allows both the *ability* and *willingness* to pay to be taken into account, and that depends on the decision of each household. Finding out what households *will* actually pay, rather than what they are *able* to pay is a less abstract and more powerful way of understanding factors (like house design, location or timing) that a poor household considers when it decides to borrow for housing.


PHOTO: PACSI

2 A household's monthly income

Household income is a crucial factor in determining affordability. In a situation where most household bread-winners are employed in regular jobs in the formal sector, determining current and even future incomes is easier. But in most Asian countries, the informal, irregular incomes of urban poor households can be quite difficult to assess. For housing finance purposes, more important than a household's total income is the amount left over after monthly expenditures, since that is what will be used to make repayments and will therefore determine how much a household can borrow.

In many poor households, there is more than one income-earner and more than one source of income. And many of these incomes may come from informal sector jobs and small businesses. Plus, it is in the nature of informal sector employment (and of poverty in general) that incomes fluctuate and crises come up which can make a household's available resources highly unstable. All these things make it difficult for formal finance institutions to determine a household's total income.

Poor people know best what they can afford

To simplify things, most financial institutions bypass the complicated realities of poverty and instead use rules-of-thumb (such as a percentage of average monthly income) to determine how much a household can afford to repay a loan. But the most successful housing finance programmes, with the best repayment rates, are usually those in which poor households — and well-organized poor communities — are the ones who determine how much they can afford to borrow and how much they can afford to repay, not banks or external lending institutions.

PHOTO: ACHR

3 Housing need vs. housing demand

Need is the term economists use to describe the condition of lacking something — like affordable housing. *Demand* is the term which describes the number of those things that would be bought, if they were available on the market. So *need* is useful for planning purposes, but *demand* is what housing producers are interested in knowing.

Differences between need and demand can create some strange situations in cities. During times of acute housing shortages, when housing *needs* are very high, there may be a lot of empty housing all over the place, but because their cost is too high, there may not be much *demand* for them. So when you're planning for housing in a city, it's important to look carefully at the figures which describe housing *needs*, and then try to estimate the likely *demands* for the different kinds and prices of housing to be produced, so *needs* can be met.

It's not always easy to figure out demand, since it depends on the price and availability of various kinds of housing. Demand is not something absolute or static, and can sometimes get blown-up. When there isn't a lot of housing available, for example, people may decide to stay with their extended families, but if housing becomes easily available, they may decide to move out. But when it comes to housing for the poor, demand is best determined by the poor themselves.

Why is housing finance so important?

Housing is a fundamental human need and right

1

Housing provides shelter for people to live in and space to carry on the various activities of their lives. Housing also provides a fixed point which allows people to get access to basic services like water supply, electricity, sanitation, house registration and citizen identification. Adequate housing is a human right and the access to housing, and terms under which they occupy that housing, are important parts of a household's social status and important aspects of their well-being.

Housing is expensive

2

In some countries, a decent house can cost up to ten times a household's yearly income. Even under the most favourable conditions, housing will cost a minimum of three times a household's yearly income. Because the cost of housing is so high, compared to what people earn, only the richest households will usually have the cash in hand to buy their houses outright, without any loans or financing.

It makes sense to borrow to buy the housing we live in

3

It is possible for households to save money to purchase housing at some time in the future, or to gradually set aside materials to build one later on. But the high cost of housing means they will have to save for a long time. Depending on their income, most households can afford to spend only about a third of their income on housing, although many now are spending up to 50 percent. If a household did save a third of its income to buy a housing unit in the future, on average, it would take 15 to 20 years to save enough to buy that housing unit. They would also need a place to stay during that long period. That would probably mean paying rent — on top of the money they were already putting into their housing saving. For most households, 15 to 20 years is just too long to wait. The obvious alternative is to reverse the process: borrow the money to buy housing at the beginning, when housing is most needed, and then take the 15 to 20 years to pay back the loan. That way, a household can live in the unit they are paying for.

But to do that means finding a willing lender

4

Before the days of banking and credit institutions, such loans would come from better-off family members or patrons. Family loans, of course, don't require much paperwork, and lenders tend to take a lenient view of late payments or defaults. But many have no access to such options since poor people often have poor relatives. Such informal family loan systems cannot finance the housing needs of large numbers of households.

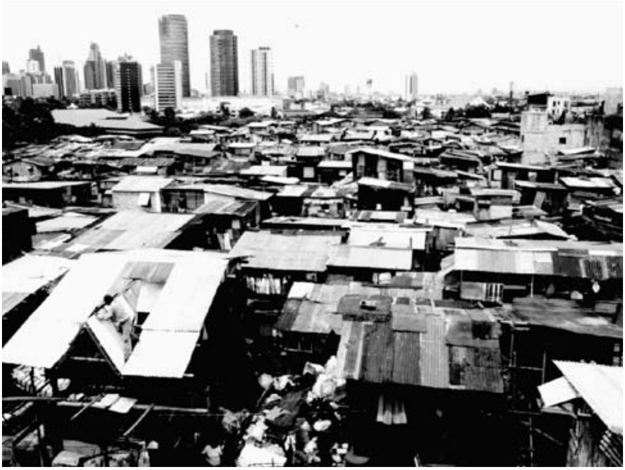

PHOTO: ICSI - PHILIPPINES

What about the poor?

Where formal systems for providing finance for land and housing have developed, access has been limited mainly to those with formal employment, with regular salaries, bank accounts and co-signing friends — all the things that are necessary to apply for formal sector housing loans, and all the things that most urban poor can't provide.

First came banking, and then the more specialized field of housing finance . . .

What is needed are institutions that collect the savings of people who do not need to spend all the money they earn, and make it available as loans to people who want to make a major expenditure like purchasing a house. That is why banks came into being. However, banks lend money for all sorts of purposes, often for shorter periods and with higher profits than housing. Over the years, a new breed of specialised finance institutions have developed, whose main business is to lend money for housing — so far, mostly to non-poor households.

Housing finance is the term for the whole process by which households get loans to buy a house, including all the rules and procedures that go with that process. Housing finance covers the process of giving and recovering loans, not only to individual households, but also to housing developers, based on funds raised by the lender from the wider financial markets.

PHOTO: ACHR


PHOTO: ACHR

It has to make a profit:

Banks and formal lending institutions are businesses. They loan in order to turn a profit on the money they lend — for all purposes. In order to ensure their profits, cover their costs and attract others to invest the money they need to lend for housing, it is essential that loans get paid back.

Understanding how formal housing finance systems work

Most households will need to borrow money in order to get decent housing. There are banks and lending institutions that specialize in providing loans for housing. But housing finance requires a bit of specialized understanding, because:

- **All housing units are different**.
- **Housing loans are big**, because of the high cost of housing and as compared to the monthly incomes of the borrowers.
- **The repayment period is long** for housing loans — usually much longer than other kinds of consumer and business loans.

Banks and housing finance institutions need to take all these factors into account when they give out loans. And they have to be careful because the bottom line is that they have to get their money back, as the loans are eventually repaid.

Loans have to be recovered, because the money loaned by a bank is not the bank's property, but consists of other people's savings — savings they may not need right now, but will want at some point in the future. A bank acts as a kind of broker to link savings with credit needs. A bank can only give out loans if people are prepared to deposit their savings in that bank.

Housing finance in poor countries

In poorer countries, formal housing finance is often underdeveloped, because:

- There are many poor people who do not save in banks or cannot afford to save, and so there isn't a lot of money available from formal sources to lend.
- Many people don't trust banks and keep their money safe by stowing it under, for example, mattresses or buying gold instead.
- Banks prefer to lend the money they have to a business for a short period, rather than for housing over many years.
- The economic and political situation is often unstable and that increases the risk that a borrower may not be able to pay back a loan.

Where does the money for housing loans come from?

Having the funds in place to make housing loans to large numbers of households requires the presence of an effective and accessible housing finance market, which is responsive to the needs of the majority. And this requires a better understanding of how to attract funds to the housing finance sector and how to manage those funds effectively and efficiently.

Lending money over a long period of time is a lot riskier for a lender because the chances are greater that a borrower might default on the loan, that property values may drop so much that they no longer match the value of the loan collateral or that inflation makes the loan worthless. Long term loans also tie up relatively large amounts of lending capital for long periods of time.

Attracting funds from various sources to finance housing is no easy matter. To attract funds, it is important to know the motivations and objectives of the people that save and the institutions that invest and to make sure that there are mechanisms in place to satisfy those objectives in a secure manner.

Buying and selling housing loans

One way for formal housing finance institutions to attract lending capital is through the development of **secondary mortgage markets**. In secondary markets housing finance institutions can sell their housing loans often at some sort of discount to long-term investors such as pension funds or insurance companies.

1 **The incentive for the housing finance institutions** is that they can use the money they get by selling off these packages of housing loans to finance a new set of housing loans. Plus, by allowing them to share the risk of lending with other investors, the housing finance institution is able to reduce the cost of lending, which means lower interest rates for the borrowers.

2 **The incentive for the long-term investors** who buy up these loans is that they can get a regular, predictable income from the loan repayments. The amount of discount offered by the housing finance institutions when they sell these loans to long-term investors depends on the overall risk of the loan going into default. In more mature financial markets, such transactions are closely regulated to ensure transparent allocation of risks for both the investors and for the housing finance institutions. Secondary mortgage markets are still new to Asia, though, and exist only in more mature financial markets such as in Japan, Korea, Thailand, Malaysia and Singapore.

PHOTO: LUMANTI

How else do housing finance institutions attract funds for lending?

Besides borrowing from capital markets (especially through secondary mortgage markets), there are a number of other strategies which formal sector finance institutions use to attract funds for housing. It is important to remember, though, that most of these strategies still fail to meet the needs of those poor who do not have regular incomes. What are some of these strategies?

1 Housing finance from banks' guarantee funds

One of the advantages of housing finance for investors is that it is less risky to invest in housing finance than something more volatile, like currency markets or start-up companies. In many countries, governments make good use of this lower-risk to persuade commercial banks to use part of the reserves they are required to maintain for housing loans.

2 Housing finance from compulsory savings schemes

Funds can also be channelled towards housing through the creation of compulsory or contractual savings, where a percentage is deducted from the salary checks of workers and put into a special bank account dedicated especially for housing. The pool of money in these special housing savings accounts is then available for housing loans to the member workers.

3 Housing finance from specific taxes or government lotteries

Another strategy is for governments to declare a certain tax (for example a luxury tax on imports) or run a national lottery in order to generate funds for housing finance.

PHOTO: CODI

Doing things by the book:

Whatever the technique being used to attract funds for housing finance, it is important to have in place proper controls and regulations, and institutions that are well and effectively managed. These institutions need not necessarily be governmental, but transparency and efficiency are a must to assure potential lenders that loans will be repaid.

PHOTO: CODI

Housing finance funds which are driven by community organizations of the poor, or at least managed jointly with them, are now proliferating and maturing in many Asian countries, and presenting a significant new finance delivery mechanism that really does reach the poor.

CONCEPTS & APPROACHES

Managing housing finance funds

Managing funds for housing finance effectively is the best way of ensuring that more funds will be made available for more loans in the pipeline. Effective management is also the best way of ensuring those funds continue to be repaid, so that they can revolve in new loans, and increase the impact a certain amount of limited lending capital can make on the housing supply in cities. Besides transparency and openness, management costs should be kept to a minimum and clearly accounted for.

Housing finance funds can be managed by a number of different actors, or combination of actors. We now have many examples of strong housing finance institutions being run not only by banks, but by national federations of poor communities, cooperatives, municipal and national governments, NGOs, non-profit institutions — and increasingly by collaborative institutions which bring together several of these stakeholders.

Many options

These finance institutions can be set up as private or non-profit organisations, NGOs or cooperative organizations working for their saving and borrowing members. They can also be set up as specialist housing finance institutions or be located as a special "window" within an already-established finance institution.

Each of these institutional set-ups have their advantages and disadvantages, but the most effective tend to be those which are tailor-made to suit the particular circumstances and political and regulatory environment of their local context. The important consideration is whether the set-up can effectively and efficiently manage the financial tasks required of it.

Understanding loan conditions

The conditions that come with a housing loan are important elements which determine who can and can't get that loan. A loan's *conditions* include all those restrictions which determine who is eligible to take that loan and who isn't — things like a person's monthly income, history of past savings, available assets and household members willing to guarantee the loan.

The terms and conditions of a loan are usually set in ways that reduce the lender's risk, protect its own business interests and guard against not being repaid. And of course, reducing the lender's risk means limiting the pool of eligible borrowers.

Finally, the least risky loans for the lenders are those with the stiffest conditions for the borrowers, which exclude many and include only those with the best credentials and the ones with better-paid and more secure long-term jobs in the formal sector.

Why can't most poor people borrow money from banks?

- **A regular income:** Perhaps the greatest obstacle for poor borrowers is the condition that they prove that they have a regular monthly income, which most poor households working in informal sector, self-employed or casual labour jobs do not.
- **Collateral:** Another obstacle is the need to have legal title to the property they want to buy, which most of the urban poor don't have.
- **High downpayments:** To reduce the lender's risk, many housing loans come with the condition that a certain part of the total housing cost is borne by the borrower. Poor households often do not have the means to raise such "downpayments".
- **Small loans:** Given their low income, the poor often require small, incremental loans which can be easily paid back. Processing such small loans is not cost effective for banks.

1 Understanding loan repayment periods

A loan's *repayment term* refers to the period of time during which the loan has to be repaid. This period is usually fixed at the beginning, as part of the loan contract. While loans for business purposes tend to be short term, housing loans are necessarily long-term. To make the monthly repayments affordable to households of all income groups, the repayment term has to be stretched over a long period — usually 15 to 30 years. In theory, these long repayment terms should get easier for a household to repay a loan over time, since their monthly repayments remain the same, while most are expected to enjoy a gradual increase in their incomes. But with the cost of housing in cities rising fast, and with fluctuating interest rates that are seldom low, these 15-30 year housing loans can become very expensive and a great burden on households of all income groups.


PHOTO: LUMANTI

2 Understanding interest rates

It's important to remember that for banks and lending institutions, loans are business. They are not lending money to people out of the goodness of their hearts — they expect to earn a profit on the money they loan out. In the business of loans, that profit comes in the form of yearly interest a borrower has to pay on top of the repayment of the original loan amount.

Interest is a kind of rent people pay to use someone else's savings money. Interest also has to cover a bank's administrative costs, profits and risks they absorb when somebody doesn't repay their loan. The interest charged on a loan is an important part of whether it is affordable to potential borrowers. For poor borrowers, high interest rates can make the loan too expensive and therefore inaccessible. Higher interest rates encourage people to save but discourage people from borrowing. But sometimes higher interest rates are a necessary trade-off, because without them, the banks won't be profitable and won't be able to attract money for giving more loans.

Governments sometimes try to force housing finance institutions to keep interest rates low, so that loans will be affordable for low-income borrowers. But when this happens on a large scale, it can actually backfire and encourage investors to take their money out of the bank and look elsewhere for more profitable places to invest.

How are interest rates calculated? The interest rates charged on loans vary a lot, depending on local market rates, degrees of risk for the borrower, length of the loan repayment term and the regulatory conditions in each country. The basic interest rates in a country's economy are usually set by the government or are set to follow the prevailing finance market rates. But this is just a kind of reference point.

Interest rates often change during the course of a loan's repayment. There was a time when interest rates remained fairly stable over a long period of time, but increasingly, interest rates change dramatically during the 15 to 20-year period over which a typical housing loan is repaid. As a result, many formal housing loans these days are made with the understanding that the interest the borrower will have to pay will change (or "float") over time, according to the fluctuations in the prevailing market interest rates.

3 Understanding collateral

Besides charging interest rates that are high enough to ensure a good profit, lenders try to protect their investment by taking steps to reduce the risk of not being repaid. A common technique lenders use to safeguard against non-repayment is to require that borrowers deposit something of value with the lender, which is kept for security against non-repayment, and returned only when the loan is fully repaid. This is called *collateral* or *loan security*, and can take the form of gold jewellery, a land title deed or other valuable items. The use of property as loan security has now become common in housing finance around the world and is called a "mortgage". The requirement of property as collateral has made housing loans inaccessible to the majority of urban poor households, who live on properties with uncertain tenure. *(See Quick Guide 3 on Land).*

Conventional housing finance strategies

Housing finance is one part of the much larger financial sector where money is loaned and repaid to fuel the development of cities and national economies. These financial markets include all the buyers and sellers and borrowers, as well as all the transactions that take place between them. Similarly, the housing finance market includes the producers of housing, the consumers of housing, the institutions that loan money for housing and all the transactions which take place between them.

Conventional housing finance strategies are based on a separation between housing production and housing finance. The housing is produced, as large or small public or private-sector projects. In conventional housing finance, the objective is to provide loans to people to enable them to buy these ready-made housing units, as and when it suits them, most often using mortgage-financed loans.

For this kind of finance system to work, there must be several lending institutions capable of handling mortgage finance, and these institutions must have enough capital to lend for housing. When such lending institutions are being started by government, some public funds will usually have to be provided as start-up lending capital. It is also important that procedures for raising additional funds for lending are spelled out clearly, and that all the rules about who can borrow and under what terms are clear and transparent. Most conventional lending institutions will be governed by some kind of board, and managed by a separate management structure with a full staff trained to operate all aspects of the institutions.

These financial institutions must also be embedded in a regulatory environment which provides a legal basis for making loans, borrowing, repaying and repossessing housing assets or accessing insurance in the event of loan defaults. The lending process is also dependent on a land management system which clearly identifies land ownership and land title of individual plots.

Risk and lending to the poor

Because banks work with other's people's money, they try to keep risks at a minimum. As we've seen, one way of reducing risk is to require that borrowers put up some kind of *guarantee* or *collateral*. In the case of a housing loan, the guarantee is usually property: land or housing. Then, if the borrower can't repay the loan, the bank can take possession of the property and sell it to recover the un-repaid money. But the collateral requirement creates an unfair situation where those who have property can easily borrow to buy more property, while those without property cannot borrow or buy anything.

- **Housing loans tie up capital for a long time:** Although the risks associated with housing loans may be low, many believe there is a shortage of funds for housing loans to low-income households because they tie up small amounts of capital for long periods of time, earn a low interest rate and are therefore less attractive to lenders than other kinds of shorter-term, higher-yielding lending.
- **Loans to the poor are small, risky and a headache to manage:** Housing finance institutions are reluctant to finance low-income housing because it is more risky, with greater numbers of defaults, greater potential troubles, greater administrative expenses and headaches recovering repayments on so many tiny individual loans.

PHOTO: URC - KARACHI

Most formal lending institutions expect that poor people should adjust themselves to accommodate their formal systems. But after decades of expecting, this is not happening. The poor can't follow these regulations and can't squeeze their uncertain lives into these strict criteria. Yet, these institutions don't seem able to look at the equation the other way around: that it should be their job to adjust their system to address the realities of the people they are seeking to help.

Why aren't formal housing finance systems reaching the poor?

When it comes to getting housing finance to reach the poor, the conventional systems for managing housing finance and the formal finance institutions that lend for housing have an extremely low record. The sad fact is that the formal housing systems, as they exist today in most Asian countries, have been unable to reach the majority of the urban populations.

Even where these conventional finance systems have been supplemented with a variety of direct and indirect subsidies on housing costs, interest rates and repayments, these extra measures have not been enough to overcome the problems that are inherent in conventional finance mechanisms. As a result, they continue to serve only a select and fortunate few, leaving the majority of potential borrowers outside the scope of their financial services.

Clash between formal finance systems and informal lives

It is important to understand that the way formal banks and lending institutions operate is miles away from the realities of how poor people live, work, survive and manage their money in informal communities. Because incomes are low and irregular, in rare cases where poor households can access formal loans, they can only afford to borrow very small amounts, or a series of small loans over time.

For banks, the administrative costs of lending a small amount of a hundred dollars to a poor household is almost the same as lending a million dollars to a rich businessperson. And of course their profits will be almost nothing on the hundred-dollar loan, but very large on the million dollar loan. So it's no surprise that most banks would prefer to focus their lending on the million-dollar clients rather than the hundred-dollar ones.

PHOTO: UNESCAP

Not many options for the poor:

In the absence of accessible formal housing loans, the poor are more or less on their own, or left to supplement their resources with loans from the informal sector, where accessibility might be greater, but there is a big price to be paid in high interest rates.

How to make housing finance reach the poor better

As already discussed, formal housing finance systems touch only a fraction of the total houses produced in most Asian countries. These formal financial markets have been unable to reach down the income levels in our societies and reach those households in most urgent need of loans for land and housing.

Many argue that to reach this neglected sector that is in such great need of access to loans, there is a need for new kinds of specialist institutions, with more flexible policies and a new working culture that understands poor people's financial realities. Unless the institutions which make loans to poor communities can understand the particular needs of this client group, they will almost certainly face non-repayment problems.

It is important to remember that the high cost of housing and the low wages of the urban poor continue to limit access to housing loans to only those with higher and more regular incomes. In cases where land or housing loans are provided through the formal-sector processes, access is limited to those with formal-sector employment who can provide all the documents to support their application for these entitlements. But most of the poor live and work in the informal sector of the economy.

The poor are credit worthy

The poor can borrow and they can repay their loans. But the systems which manage their borrowing and repaying must involve them centrally in the management. They must also be flexible enough and open enough to allow new strategies for loan repayment which allow poor communities to resolve repayment problems — strategies like making bulk loans to community groups instead of individual loans, and letting the group manage the repayment process collectively.

Understanding how informal finance markets work

There is a burgeoning informal financial market that provides quick and easy access to housing finance for those unable to meet the terms and conditions of formal sector loans. The principles of the informal financial sector are similar to those of the formal sector, but their informality has advantages and disadvantages. Although this informal market meets a large need, it does so at great cost.

Interests rates charged on informal loans from loan-sharks and money lenders are often exorbitant — sometimes as high as 1% per day, or 20% per month — and repayment collection practices when people default can be brutal. Economists would point out that these loans from money-lenders are expensive because competition is so limited and the risks of non-repayment are so high. Since most loans are given without any collateral, defaults and non-repayments are usually punished loudly and violently, to ensure that other clients will be scared enough to repay their loans. With these kinds of interest rates, small loans can mushroom into giant financial burdens in a very short time, putting households into a position of perpetual enslavement to their lenders.

This is a system nobody likes and nobody wants, but because it is the only one available to most poor households, it accounts for up to 80% of all housing finance among Asia's urban poor. It may be violent and exploitative, but the informal loan markets comprise a significant financial sector which needs to be understood.

The option to accept this system and improve it

Some feel that with a little understanding and regulation, these informal lending systems could operate much more effectively, more efficiently and less exploitatively. Many also feel that formal-sector lenders have a lot to learn from the informal lending systems, which have been able to make finance more accessible to the majority of the population, especially the poor.

Most informal markets operate best because lenders know their borrowers and have social links which make it difficult for borrowers to default on loans without losing face. This is not too different from the principles of client relationships, credit history and credit-rating that banks use to determine who gets a loan. The lesson in these informal lending systems is that financial relationships can be based on mutual trust and cooperation, rather than strict documentation of income or willingness to pay.

For all their problems, these informal loan systems show that small, localized operations may be more effective than big centralized ones, allowing for personal knowledge to replace legal requirements and paperwork. But because they are so localized, informal lenders may not have the capacity to serve the scale of need that exists within their area. Plus, when things go wrong with an informal loan, because everything is based on spoken agreements, neither borrower nor lender have much scope to get external help through the legal system.

5 strategies to make sure housing finance reaches the poor


PHOTO: ACHR

Strategy 1: Community-based self-finance

Being largely left out of the formal financial markets and as a response to the exploitation of the informal market, with the help of NGOs and some government organizations, many poor communities are increasingly building and managing their own collective finance mechanisms through community savings and credit activities.

When communities save their money together, and make loans from their collective savings, they are not only building their own financial resource base, but they are developing the collective management skills and financial capacities to manage money as a group. Community members enjoy most of the advantages that informal lenders do, such as closely knowing the situation of the borrower and using social collateral as a mechanism to recover loans. Because they are owned and operated by the poor themselves they are able to eliminate the costs of the formal market and the exploitative elements of the informal market.

Poor communities in cities across Asia — and large, well-organized networks and federations of these communities — have in the past twenty years been building what is now a large, well-organized and well-connected movement of community-managed savings and credit groups.

Besides saving for livelihood, emergencies and housing, these savings groups have also strengthened the communities they operate in, by providing people a simple, regular mechanism for building collective management skills, cooperation and mutual assistance, while they build a community's own financial resource base.

Where poor households have no hope of negotiating for what they need as individuals, or even as a poor community, they are increasingly learning that as large, well-organized networks of poor communities, who come to the bargaining table with their own significant resources, they can negotiate for many things they need, such as land, basic services and access to housing finance. Without the strength of this large scale support, these things would be unreachable.

Strategy 2:
Simplifying the formal sector

While the *formal* housing finance system has the funds and the ability to raise funds from formal financial markets, the *informal* and community-based housing finance systems have the knowledge and experience to successfully reach the poor. It is important for the formal housing finance system to understand and tap this knowledge. One way is for formal sector lenders to adopt more simplified, informal-style practices in their lending programmes to the poor — practices such as:

- **Minimal paperwork.** The poor are often intimidated by bureaucracy and can't afford to take much time from their work. Many poor people may also be illiterate.
- **Minimal collateral requirements.** This requires the lender to know the borrower and have close links with both the borrower and also his or her community, so that social pressure techniques can be used in cases of default. This might suggest locating the loan office right inside the informal settlement, or somewhere close by.
- **Ensuring flexibility in repayment.** Poor households have different abilities to repay. Standardized practices often fail to reach them. Negotiating terms of repayment that are mutually agreeable, on a case-by-case basis, can greatly reduce the instances of default.
- **Incremental housing financing.** Giving a series of small, consecutive housing loans is one way to help poor households build up their credit history and rating: so that after repaying a few smaller loans, they would be eligible for taking a larger loan with a longer repayment term.

Many government and non-government finance institutions have adopted elements of this approach, the most famous being the Grameen Bank in Bangladesh. The downside of this strategy is that the transaction costs of loans for the bank or financing institution are high and therefore interest rates may be higher than commercial banks. To make the loans cheaper, some governments have tried to subsidize these loans. Other groups in India and the Philippines have tried to establish guarantee funds which reduce the perceived risks associated with lending to the poor.

To subsidize or not to subsidize?

Many working in the field of low-income housing believe that the best way to make housing loans affordable to the poor is to subsidize them, so that the poor pay below-market interest rates on the money they borrow. The subsidy can be provided by the lending institution (in the form of reduced profits earned on those loans) or by the government (in the form of direct subsidies to the lenders, to make up the difference in rates). Advocates argue that the poor, with their irregular incomes and low wages, cannot compete in the formal market systems and need some subsidy. Subsidy opponents argue that the poor pay much higher interest in the informal sector anyway and so can afford to pay market rates. Many poor households would be happy to pay market interest rates, they say, if such loans were available to them, rather than pay the high rates charged by informal money lenders. They also argue that given the huge scale of low-income housing needs, government subsidized funds will never be sufficient. Funds would have to be raised in the open market, where it is more difficult to acquire subsidies.

Strategy 3: Channelling loans through community savings groups

Another key approach is to use community-based savings and loan schemes as "brokers" for channelling loans to poor communities. Community-based savings and loans schemes provide governments and lending institutions with an established, capable management mechanism within poor communities themselves that is able to manage loan disbursal and repayments as a group, thereby reducing the lending institution's management overheads. A community savings group not only attracts funds for housing finance, but the process of operating a savings and loan process within a poor community develops the collective and individual financial management capacities the poor will need to manage larger housing and land loans later on. Many communities make housing loans from those institutions dependent on having good prior savings, and use peer-pressure systems to ensure repayment and assist default situations collectively.

Women are especially atttracted to savings groups because they provide credit quickly if the household is in crisis, and can provide loan facilities, for example for income-generating activities. Women also often find that their participation transforms their relationship with others, in the family and in the community. Saving groups create a venue for meeting regularly, and for learning from others.

Collective finance
Collective land
Collective management

Communities with a history of collective savings and lending are in a good position to manage housing finance which comes from external sources, especially if that finance is collective, not individual. A fast-growing strategy for channelling housing finance to these communities is to make group loans to the community organization, which then on-lends to its members, and takes responsibility for managing every aspect of the repayment process and making a single group repayment each month to the lender.

In these group loan strategies, the whole community is collectively responsible for repaying the loan, and developing internal systems for ensuring the repayments are made in full each month, even if some members might have repayment problems. Although savings groups may have no legal power to punish late-payers, there are a number of techniques they can work into their loan management systems to accommodate the inevitable repayment problems and to help their neighbours who have problems making repayments. These systems are positive, supportive, realistic and highly social. When communities design and manage them, they will ensure good repayment. One way communities do this is by charging their members an extra margin on top of the lender's interest rate, or making some extra monthly saving compulsory during the repayment period. Both techniques allow a community to build up a reserve to act as a buffer against repayment problems.

Collective loans and collective land in Thailand

Communities are increasingly negotiating secure tenure terms that are not individual but collective, through cooperative ownership or collective leases to the land their settlements occupy. In Thailand, housing and land loans from the **Community Organizations Development Institute (CODI)** are made only in bulk to community cooperatives with active savings groups, and only when the land is collectively owned or leased, at least for the duration of the loan contract. Besides providing a safeguard against speculation and gentrification, this condition of collective tenure increases the social pressure that the community organization can exert on members who default. It also allows the community to set up systems to collectively provide for their own most vulnerable neighbours, such as the elderly. The added benefit of this approach is that it sparks off other collective activities, like community welfare, environmental improvements, community enterprise, youth groups and cultural activities.

PHOTO: CODI

Housing loans from CODI:

Between 1992 and December 2006, CODI has approved a total of US$ 56 million in land and housing loans to 55,504 poor households, in 820 poor and informal communities in 160 cities around Thailand. All of these loans have been channelled through the community savings groups, which manage the repayment collectively.

Collective loans and collective land in Philippines

Another example of group lending is the **Community Mortgage Programme (CMP)**, which channels subsidized loans (from government fiscal budgets) for land and housing to poor communities which have organized themselves into homeowners associations and found affordable land to buy and develop their own housing, on a self-help basis. NGOs, local governments or community federations act as legal “originators” for these community loans. There is no requirement that communities have savings groups, though, and its track record of repayment is mixed.

Source: www.achr.net

PHOTO: ACHR

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PHOTO: USAID FIRE PROJECT

The gap between poor people's survival systems and formal development financing is very wide. On the one side are the poor, starved for resources. On the other side are the development and finance sectors full of resources but unable to get them to the people who most need them.

Strategy 4:
Using intermediate institutions to bridge formal and informal finance

One way to link poor households (in organized communities) with formal sector finance is by creating an intermediary institution of some sort, which can bridge the gap between them in several ways. This intermediary institution could:

1. **Increase the comfort factor.** It could help formal institutions feel more comfortable about lending to poor households by offering some kind of risk mitigation, loan guarantees, bridge financing or even the non-economical reassurance of a trusted intermediary.

2. **Open new markets.** It could help formal finance institutions reach the markets which have so far been unreachable to them.

3. **Tailor loans.** It could help the formal finance institutions to adjust their systems and procedures to make the loans more workable for the poor, so that eventually they could link with poor households directly, without any intermediary.

4. **Promote bulk lending.** It could take bulk wholesale loans from the finance institutions and then lend-on in flexible ways to many different community housing, land and upgrading projects — all with their own loan amounts, repayment terms and interest rates.

5. **Establish revolving funds.** It could use long-term, wholesale loans from the finance institutions to revolve in a variety of shorter-term loans to poor households for many purposes — not only housing. This would give households more flexibility in using finance to support a more comprehensive and more holistic community development process.

6. **Introduce subsidies.** It could introduce some subsidies along the way, in order to make the loans more accessible to the poor households. The subsidy could come in the form of a government or donor-financed interest rate subsidy, for example, which trims the commercial interest rate to a lower rate for on-lending to the households.

4 examples of intermediary finance institutions

This strategy is no longer new, and there are a growing number of these intermediary finance institutions in Asian countries, which involve a wide variety of partnership structures and institutional arrangements. Here are just a few variations on the theme of intermediaries:

1 **Community Development Funds (CDFs)**. These are light, flexible and jointly managed by communities, local authorities and other local actors and are now appearing in several Asian countries and providing much-needed credit for housing, infrastructure and income generation to poor community organizations. CDFs function like banks, but can work in more flexible ways to channel soft loans to the urban poor, who have been unreachable by formal finance. These funds are all different, set up to respond to very different needs, capacities and political contexts in their local areas. Some of these funds have been initiated by the government, and others by NGOs or community federations, with local governments acting as key partners. The lending capital in these funds comes from many sources, including international donors, local and national governments, community savings and private-sector finance institutions. These funds are all closely linked together, and there is a lot of exchange visiting and learning between them. *(See Quick Guide 6 on Community-based Organizations)*. *Source: www.achr.net*

2 **CODI in Thailand:** The Community Organizations Development Institute (CODI) has launched a pilot project to teach formal sector banks how to deal with poor people's cooperatives. Thailand's Government Housing Bank (GHB) has agreed to re-finance US$5.7 million of housing loans that CODI has already made to 10 community cooperatives with good repayment records. As part of this experiment, CODI will deposit half this amount in the GHB, as a guarantee fund. After the loans are transferred, communities will make repayments to GHB, freeing up more CODI funds for other, riskier community housing loans. If the pilot works, the process will be scaled up. *Source: www.codi.or.th*

3 **SPARC in India:** The Society for Promotion of Area Resource Centres (SPARC), a Mumbai-based NGO which supports the housing projects of the National Slum-dwellers Federation in India, has been playing this intermediary role for a large number of large-scale government housing projects and public sector housing loan schemes to poor communities. These projects involve tens of thousands of housing units. *Source: www.achr.net*

4 **CLIFF in India and Philippines:** The Community-Led Infrastructure Financing Facility (CLIFF) is a US$10 million fund set up by the UK charity Homeless International together with DFID and Cities Alliance, which provides capital loans and loan guarantees to urban poor organizations to facilitate urban investment loans from the local finance sector, to finance slum rehabilitation, resettlement and infrastructure projects in partnership with local authorities. CLIFF is being piloted in India and the Philippines. *Source: www.achr.net*

PHOTO: UNESCAP

There's nothing new or innovative about building as cheaply as possible, within ones available means, as a way to avoid the need to borrow or go into debt for housing. The poor have been building their shelter like that all along. But even these old techniques can be improved upon, and when poor communities are organized and supported, they can come up with all sorts of new ways to bring down the cost of their housing projects.

Strategy 5: Cost-reduction strategies

Probably the most immediate and pragmatic way of dealing with the lack of available housing finance is to reduce the need for it. This is not to say that the battle to make housing finance accessible to the poor should be abandoned, but while that effort continues, there are several things communities can do right away to lower the cost of their housing, and therefore to reduce their need for the housing loans that are so hard to get.

1 Reducing housing costs through design

One of the best ways of reducing the cost of housing is to use a variety of design and construction strategies which make the unit construction costs lower and make more efficient use of the land, such as to:

- **Design tight housing layouts** that allow as many households as possible to occupy a limited amount of land.
- **Design housing units of smaller size**, or units which can be expanded upwards later.
- **Use community and household labour** to build the houses, to reduce labour costs.
- **Use alternative, recycled or cost-saving materials** to bring down materials costs (like community-made blocks or building components, recycled doors and windows).
- **Buy materials collectively** to get bulk discounts on bricks, blocks, cement, steel, roofing sheets and sand.
- **Build housing collectively** to make use of "economies of scale" to bring down per-unit costs.

2 Reducing housing costs through internal cross-subsidies

Another strategy that governments, developers and communities have used to finance low-income housing with minimal loans is to cross subsidize the low income housing through profits from the sale of market-rate housing units within the same development.

- **The governments of Malaysia and Philippines**, for example, require that all private sector housing developers dedicate 20 percent of the housing units they develop for sale to the poor at government-determined prices.

- **The State Government of Mahrashtra**, in India, has a scheme which allows un-used building rights from sites where low-income housing is being developed to be sold to developers to use in commercial developments on other sites ("Transfer of Development Rights"). Some poor communities occupying prime inner-city land have built a number of such market-rate units into their slum redevelopment plans, and the money they collectively earned on the rent or sale of these units has subsidized the cost of their own housing. Setting up these cross-subsidy redevelopments is not easy, and often requires bridge-financing and some technical assistance from a partner NGO and either the national or the local government. *(See Quick Guide 3 on Land).*

PHOTO: HOMELESS INTERNATIONAL

3 Reducing housing costs by building incrementally

In the absence of loans to build or buy housing on the formal market, most people living in informal settlements build their houses incrementally, making improvements and investments as resources are available. In this way, the development of housing is a long process, instead of a one-time thing. And because the investments are spread out over time, they are almost automatically linked precisely to a household's fluctuating resources. Some governments and institutions have recognised the effectiveness and appropriateness of incremental housing, and supported the process by providing *core housing*, or even developing sites-and-services schemes, in which only plots are provided and households can build and improve their housing gradually, at their own pace and using their own means. *(See Quick Guide 2 on Low-income Housing)*

PHOTO: ACHR

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8 ways to develop a better set of housing finance strategies

Make housing finance systems that are need-driven, not supply-driven

1

This means designing a programme that meets the realities of the target households, rather than seeing which households are eligible to participate in existing or modified financial schemes.

PHOTO: UNESCAP

Don't restrict finance mechanisms to housing alone

2

It is in the nature of poverty that people's needs are not easily separated into compartments, and survival often depends on a range of factors, including livelihood, housing, land tenure, basic services and health care. When finance mechanisms take a more flexible, more holistic view of people's needs, they can give poor communities a tool to resolve many needs in addition to housing.

PHOTO: UDRC - MONGOLIA

Consider using subsidies as tools to make finance more accessible

3

Many of the housing finance strategies which have been most effective in reaching the poor include some kind of subsidy. Subsidies, especially interest-rate subsidies and loan administration subsidies, can help a lot to make housing finance accessible and affordable to poor households.

PHOTO: USAID FIRE PROJECT

Support community savings as part of housing finance

4

The presence of strong, collective savings and credit groups in poor communities is one of the best ways of preparing people to manage long-term housing loans with efficiency, fairness and transparency — and also the best way to ensure that those loans are repaid.

PHOTO: ACHR

Keep loan sizes and loan purposes flexible

5

Housing loans don't need to be big, one-time things. Smaller, more frequent loans to support incremental housing should also be possible. Some stronger communities may be ready to redevelop their housing all at one go, but others may prefer to do it more gradually, and finance should be available to help both.

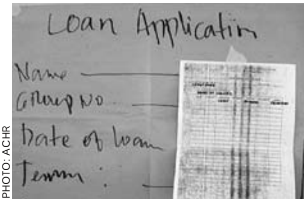

PHOTO: ACHR

Involve people in every stage of planning a housing finance strategy

6

Poor people know what they need better than any government official or finance professional. The first step is learning to listen to them, which is something most governments and finance institutions can improve upon. Making space for poor communities to be involved in planning and managing any housing finance is crucial if the system is going to be effective in reaching them and in facilitating good repayment.


PHOTO: USAID FIRE PROJECT

Minimize rules and procedures and maximize flexibility

7

Simplifying entrenched procedures is not a simple thing to do, given the deep culture of stiff rules and regulations and bureaucracy in most finance institutions and government agencies, and the practices of inspection and intimidation which often comes with finance problems. But to reach the poor and be understandable to them, a housing finance mechanism needs to be simple, easy, flexible and fast to respond to needs, and to provide an atmosphere of facilitation and support for what people are doing.


PHOTO: UN-HABITAT

Explore innovative, community-based ways to provide loan security

8

Requiring individual land titles to get housing loans cuts off a majority of the urban poor from accessing finance. There are many ways poor communities can develop internal systems to secure loans and ensure steady repayment, including group loan management, collective land titles and mandatory savings as part of the loan contract.


PHOTO: ACHR

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An annotated list of key websites: *For an annotated list of websites which offer more information about the key issues discussed in this Quick Guide series, please visit the Housing the Urban Poor website, and follow the links to “Organizations database”.*

www.housing-the-urban-poor.net

RESOURCES

The pressures of rapid urbanization and economic growth in Asia and the Pacific have resulted in growing numbers of evictions of urban poor from their neighbourhoods. In most cases they are relocated to peripheral areas far from centres of employment and economic opportunities. At the same time over 500 million people now live in slums and squatter settlements in Asia and the Pacific region and this figure is rising.

Local governments need policy instruments to protect the housing rights of the urban poor as a critical first step towards attaining the Millennium Development Goal on significant improvement in the lives of slum-dwellers by 2020. The objective of these Quick Guides is to improve the understanding by policy makers at national and local levels on pro-poor housing and urban development within the framework of urban poverty reduction.

The Quick Guides are presented in an easy-to-read format structured to include an overview of trends and conditions, concepts, policies, tools and recommendations in dealing with the following housing-related issues:

(1) **Urbanization:** The role the poor play in urban development (2) **Low-income housing:** Approaches to help the urban poor find adequate accommodation (3) **Land:** A crucial element in housing the urban poor (4) **Eviction:** Alternatives to the whole-scale destruction of urban poor communities (5) **Housing finance:** Ways to help the poor pay for housing (6) **Community-based organizations:** The poor as agents of development (7) **Rental housing:** A much neglected housing option for the poor.

This Quick Guide 5 introduces some of the key concepts of formal housing finance and an overview of how both the formal and informal systems of delivering housing finance work, especially with regard to the urban poor. The guide provides insights to innovative ways in affordable housing finance for the urban poor living in Asia's cities.

More information can be found on the website www.housing-the-urban-poor.net

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