HiFi NEWS

This newsletter brings together the experiences of groups working with savings and loans for shelter investments in the South.

AT THE WORLD URBAN FORUM

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Introduction

The world of housing finance has changed very significantly over the last ten years. In particular, small-scale lending for land purchase, infrastructure investment and housing improvements has increased significantly. Ten years ago, the state programmes in Thailand had barely started, while the housing subsidy programme in South Africa was being conceived of as a capital grant. Microfinance agencies had a "toe in the water" approach to shelter lending, and the urban poor funds that now are a firm feature of SDI programmes had been launched in only one country. NGO shelter lending continued, and had been taking place for many years, but programmes remained relatively disconnected from other financial systems and institutions. Hence they remained small-scale revolving loan funds assisting relatively small numbers of families. The landscape is now very different.

What has changed?

Microfinance for shelter has become a significant area of work for many microfinance agencies. Small loans help home-owning families improve their living accommodation. Experimentation with group loans has multiplied, as more agencies have become concerned with providing finance for land and infrastructure. Such loans give tenants and squatters threatened with eviction opportunities to purchase and/or improve access to basic services such as piped water.

Neo-liberal ideologies have increased the scope and scale of markets. The growth of microfinance agencies has increased the experience of the professional development sector in lending to the poor and, in many places, has reduced the cost of borrowing for some of the urban poor. While in the initial period lending was (supposedly at least) for enterprise development, consumer demand and growing confidence in their commercial capacities has encouraged the extension of microloans to the housing sector. Small loan provision for shelter investment appears to be growing rapidly in at least some countries of Asia and Latin America. Such loans are well suited to housing improvements.

The inadequacy of accommodation, and the associated needs for improvement, in Southern towns and cities is increasingly being recognised. Equally evident is the lack of state capacity to address the issue. In this context, development agencies, particularly NGOs, are innovating to find more replicable ways of financing the scale of improvements that is needed. In the present context, market options gain precedence. There is a growing interest in finding ways to enhance individual investment capacities and to speed up the process of shelter improvement and consolidation.

However, there are many shelter-related improvements that cannot be made individually. **Group loans** enable investment in land purchase and infrastructure improvements; not only is a collective process essential but it also helps to make the improvements more affordable. Individual lending is not relevant in this context, both for reasons of affordability and for other practicalities. Lending to groups is seen as more risky than lending to individuals, with fears about adequate responsibilities and "free riders" (i.e. those who enjoy the benefits and avoid their share of the costs). Despite these risks, development agencies have been willing to consider these strategies because of the need to invest in secure tenure and improved basic services such as water connections, because of the incapacities of the state, and the inability of individuals to make such investments individually.

A further set of approaches uses the collectivity generated by group process to address the deficit in pro-poor government. Savings and lending for secure tenure becomes a way to build up grassroots movements that can pressure the state for a more proactive investment strategy. Community-managed savings – the accumulation of finance – goes to the heart of what it is to be poor and excluded in a market-based economy. Building movements around community-managed finance helps to ensure a very strong organizing core that has essential skills and capacities, and that has succeeded in establishing trust between residents. The more immediate development objectives are two-fold. First, to increase the amount of finance that the state is willing to allocate to improving urban low-income settlements: the understanding is that inclusive developments will never take place if subsidy funds (including finance, free or low-cost land, infrastructure capital) are not made available; savings helps to secure state support. Second, to ensure that these funds are allocated to the priorities of the poor and support ongoing activities of the poor to improve their own livelihoods. This requires a strong local group with a capacity to manage money.

This issue of *HiFi News* reviews what has happened in each of these areas and draws out policy implications. Previous issues have been concerned to illustrate the nature and type of innovations in housing finance, and this issue synthesises the experiences to offer an assessment of the "state of the art" in shelter lending to the poor.

Microfinance for shelter

Microfinance for shelter assists individual homeowners to improve the quality of their accommodation. Such loans are typically less than US$ 500, with loan periods of up to five years. Interest rates are frequently lower than comparable loans from the same agency for enterprise development, both because of the belief that housing loans are "non-productive" (i.e. not generating any income) and in recognition of the burden created by larger loans over longer loan periods. Some agencies allow a grace period for the construction to take place. It is not possible to define the "typical" improvement, but such small loans may be used to add a room, to replace a floor or roof with more permanent building materials, and/or to improve bathroom and/or kitchen facilities.

There is a considerable difference of opinion about whether or not technical assistance should be offered. Some agencies continue with a minimalist approach to lending, even in the case of shelter, and assume that borrowers are able to construct for themselves or with the assistance of local skilled workers that they employ. Others require that borrowers accept technical advice about the nature of the planned improvement.

Equally varied is whether or not a track record of borrowing for enterprise development from the same agency is required. In most circumstances it is not, with agencies preferring to have the possibility to develop a separate clientele for shelter microfinance lending. However, in some cases, the agency seeks to reduce its risk by requiring a good history of borrowing for income generation and the successful realisation and repayment of enterprise loans.

Collateral is particularly tricky for shelter micro-loans. The use of a mortgage bond on a property is extremely rare because of the associated expenses, and equally because the agency has no real interest in repossessing the property if the repayments are not maintained due to resale difficulties. A major strategy in enterprise lending, that of small repeat loans, is of less use given the amount of time taken for each loan to be repaid and the size of each loan. As a result, agencies are forced to be innovative. Many seek some kind of legal claim over other possessions. Another popular strategy, often used in combination with others, is to apply social pressure, perhaps using groups with co-guarantors from within the group.

For those with secure tenure

The need to maintain high levels of repayment encourages the agencies to restrict lending to those with fairly secure, even if not formal, tenure. However, shelter microfinance is generally restricted to those with reasonably secure tenure who need to upgrade and otherwise improve their homes. The consequences of a lack of finance are well known. Without access to adequate loan finance, households either must borrow at penal interest rates from the informal financial sector, borrow (where possible) from family and friends, or delay making the improvements until finance is available. Shelter microfinance can speed up incremental housing developments, however adequate land tenure is crucial. This means that groups like the Grameen Bank, who have a programme to address rural housing needs that has given more than half a million loans, cannot take the same strategy into urban areas because of a lack of secure tenure and the difficulties that the urban poor face in obtaining access to land.

Increasing scale of activity

Shelter microfinance is now being provided by microfinance agencies throughout Latin America and Asia. Groups like BancoSol in Bolivia and SEWA in India have created shelter microfinance programmes to respond to the needs of their members. At least part of the motivation for microfinance agencies is market share. Consumer loyalty often means that borrowers prefer to use a company that they are familiar with and which has provided good service. If consumers are looking for and are able to access shelter loans, each microfinance agency is anxious that they are not forced to go elsewhere. In higher-income countries, such as Colombia and Chile, commercial financial agencies are also exploring the possibilities of using more formal lending systems to offer small loans for shelter improvements. Another group that has been attracted into this market, notably in Mexico and other Latin American countries, is building materials suppliers, who are always looking for ways to increase their consumer base. A further institution helping to support small-scale lending for housing is the traditional savings activities that take place within many low-income communities. *HiFi News 12* described the work of UCISV (La Union de Colonos, Inquillinos y Solicitantes de la Vivienda, Veracruz –the Union of Settlers, Renters and Housing Applicants of Veracruz). This longstanding and independent grassroots organization led by women has as its main objective to improve the living environment in the low-income areas of cities in the state of Veracruz. Their loan programme is based around a traditional savings and loan scheme called TANDA, a group savings scheme where each woman contributes the same every week, and every week a different member of the group receives the funds until the cycle is complete.

In Africa, there is much less activity in shelter microfinance (with the exception of South Africa). There are much lower levels of affordability. In South Africa, groups like the Kuyasa Fund (*HiFi News 11*) provide additional finance for families wanting to extend housing provided by the state through a subsidy programme. This programme, like the example from Veracruz and many others, focuses particularly on women borrowers. The focus on women remains strong in shelter finance – it is the same in many programmes lending for micro-enterprise investment. In this case, it is driven by women being better at repaying loans and by the poverty focus of some such programmes. In the case of shelter, the focus on women is further reinforced by the frequency with which shelter responsibilities are attributed by gender. The Kuyasa Fund, as is the case with many shelter finance programmes, emerged from the Development Action Group, an NGO working on urban development and urban poverty issues. There have been further innovations in African countries, notably in Kenya, associated with agencies such as K-Rep and NACHU, and in Namibia with the government-financed Build Together Programme, but generally, their scope and scale is limited.

In Latin America in particular, some of these programmes have learnt how to increase the value of their contribution to addressing shelter needs by extending access to state subsidy programmes that involve a tripartite financing plan with state subsidies, household savings and commercial loans. The Step-by-Step programme in Ecuador (*HiFi News 13*) illustrates how such financing systems can work; this programme helps households put down the deposit they need to access a state subsidy of up to US$ 1,800. The poorest households find it hard to save, but once they secure access to the state subsidy they can significantly improve their housing options.

Collective lending (market-based)

While shelter microfinance can assist those able to obtain land with some degree of security, it is not relevant to the many others who are tenants or are squatting on very insecure sites.

Addressing the core challenge of reducing the extent of "slum" housing and providing adequate land security and basic services for the estimated 900 million currently in need requires another approach. Both cost and practicalities determine that the residents of a neighbourhood have to work together to improve their living conditions (slum upgrading). The same is likely to be true if they purchase a new site together, although in some cases such an area is provided through the commercial market, either by a private contractor, microfinance agency or NGO. An example from El Salvador is the Salvadoran Integral Assistance Foundation (FUSAI), a microfinance agency that has also started to be operational in land development in order to address the needs of clients. FUSAI buys land and undertakes infrastructure development. The land is then sub-divided and allocated to families that have been accepted by FUSAI according to income and capacity to pay criteria. Families first pay back the loan for the land and infrastructure. In this case, there is a requirement for a savings contribution, and a state subsidy to help reduce the loan burden. A collective approach is needed for upgrading an area, as plots may have to be moved to enable roads, pathways and access for piped services. Residents, especially those who are to be moved or have their plots reduced in size, have to agree to such a re-blocking, including any compensation that is negotiated. New land will need to be identified and its potential assessed.

Improving affordability

As importantly, costs need to be shared if they are to be affordable. Few can afford the full cost of basic services, including connections to mains services, if they have to cover these on an individual family basis. Equally, land costs for individual plots are likely to be prohibitive; by sharing these costs, they can be made affordable. In some cases, residents' associations may be able to access lower connection fees and other benefits. Groups may also be successful in negotiating discounts in the case of land purchase. Moreover, by working together, groups can help to identify new resources and find new possibilities. The recent growth of group lending (as opposed to individual family support) within the Chilean housing subsidy programme is indicative of an increasing recognition of the effectiveness of such approaches when it comes to the poor and poorest.

Group loans are generally offered by specialist sectoral agencies, such as WaterAid, or in some cases by government authorities, rather than by microfinance agencies. The primary reason is that microfinance agencies (and other commercial institutions) do not have the capacity to work with a community and prepare them for both the physical investment and the borrowing process. The professional agency generally seeks to support the emergence, or otherwise strengthens, a local representative association able to receive and manage the finance.

Terms and conditions vary significantly. Generally, some kind of subsidy is involved but the ways and means through which it is delivered vary considerably. In some cases, it is simply professional advice that is offered for free. In other cases, the interest rate will be very low, perhaps even zero. Sometimes, part of the capital is subsidised. This assistance follows a fairly traditional NGO grant-financing route. Financial support is given to the poor by professional agencies established to raise funds to help the poor.

The level and nature of government involvement also varies considerably. In some schemes, technical assistance will be provided by a utility or municipality through existing support schemes for low-income communities. In other cases, municipalities may provide further financial assistance to communities, such as some of the micro-hydro schemes offered loan finance by Practical Action in Peru. In a limited number of countries, these programmes have been taken beyond civil society initiatives, with more substantive investment from governments and public agencies. National programmes have been created as demonstrated by the experiences of schemes such as the Community Mortgage Programme in the Philippines and Build Together in Namibia. In both these specific examples, there is the significant involvement of local government and an increasing interest in finding new ways to decentralize activities.