Affordable Housing Finance
New market development in Africa

Kecia Rust
Tuesday, 29 May 2012

Housing Finance in Emerging Markets
5th Global Housing Finance Conference: Providing Shelter – Creating Jobs – Fueling Growth
Two sides of African cities: strong growth, clear demand, but poor housing
Performance in a number of key countries in Africa is attracting investor interest.

“Fabulous growth”

“Africa’s growth acceleration resulted from more than a resource boom. Arguably more important were government actions to end political conflicts, improve macroeconomic conditions, and create better business climates, which enabled growth to accelerate broadly across countries and sectors.” McKinsey (2010) Lions on the move: The progress and potential of African economies

“Sub-Saharan Africa is changing. The region’s resilience to the global financial crisis of 2008-2009 demonstrates this. It experienced a slowdown in growth to 2.8 per cent in 2009, before staging a robust recovery to 5 per cent in 2010. The only other two regions that experienced a slowdown in growth, rather than a recession, were developing Asia, and the Middle East and North Africa. This is a commendable performance.” FitchRatings (2011) Sub-Saharan Africa.

Massive urbanisation

Urbanisation rates mean more people are seeking accommodation in urban centres.

But…. tiny mortgage markets

Why? And if not with mortgages, how do people finance their housing situation?

Source: World Bank data, provided by Simon Walley
According to the World Bank, only 3% of the population in Africa has an income sufficient to support a mortgage. 36.5% of Africa’s population earn less than US$ 2,00 per day. This is the international poverty line.

In most cases, subsidies don’t bridge affordability to buy a new house. In others, they cause new affordability challenges. In part, this has to do with low levels of affordability for mortgage finance.

Source: AfDB Report on the middle class, 2011
Serviced land

- Functioning land registries
  - Rwanda / Uganda / Tanzania / Zambia
- Title deeds & registered land
  - Ghana / Mozambique
  - Benin: 3.2% of households have land title. Total titles, 22,820 (2006)
- Land for housing vs. other demands
  - Mauritius & Seychelles
- Speculation
  - Tanzania
  - Angola
- Infrastructure
  - Backlog estimated at US$93 billion for Africa
  - Municipal capacity constraints

Access to finance

- Term mismatch
- Limitations on capital
  - Pension funds restricted from investing in housing
- Barriers to investment
  - Exchange control regulations & risk
  - Tiny markets
- Better return options
  - Government bonds
  - Short term / high churn microloans
- Value chain constraints
  - Project/construction finance
  - End user finance
  - Market makers

And very limited affordable housing supply

Other challenges relate to a constrained housing delivery & finance system
A more nuanced approach opens up opportunities

According to the World Bank, only 3% of the population in Africa has an income sufficient to support a mortgage.

1. Bring mortgages down-market (and make houses cheaper).
2. Grow & develop housing microfinance.
3. Finance rental housing

36.5% of Africa’s population earn less than US$ 2,00 per day. This is the international poverty line.

18.8% earn above US$20 per day
10.8% earn US$10 - $20 per day
9% earn US$4 - $10 per day
24% earn US$2 - $4 per day
9% earn US$4 - $10 per day
10.8% earn US$10 - $20 per day

New players are beginning to carve out niche markets, serving a wider population / policy makers are recognising the value of partnerships.

Source: AfDB Report on the middle class, 2011
1. Bring mortgages down-market (and make houses cheaper) – but target subsidies carefully: South Africa

**1994 housing subsidy policy**
- 1 million houses in 5 years ➔ 3 million in 18 years
- But not enough: backlog the same as 1994 (2.1m houses)
- New gap market created

**2012 Presidential announcement**
- Finance linked subsidy
- Mortgage guarantee
- Tax incentive to developers
- Informal settlement upgrading

≤R300 000 (∘37 000)

South Africa’s housing subsidy history and current interventions offer useful lessons
2. Grow and develop housing microfinance: Angola

- KixiCredito (Angola’s first non-bank MFI) offers a housing microloan product: KixiCasa
  - 36 month sequential loans up to $5000 per phase per house
  - Raising further capital to grow loan book

- Development Workshop as developer
  - Partnership with CLIFF to scale up: 3000 home, incremental housing project in Huambo. CLIFF provides infrastructure financing; KixiCasa end user finance

- HabiTec is a social enterprise supporting KixiCasa loans:
  - HabiTerra provides settlement planning, land registration and land allocation services – support to provincial government with participatory urban planning
  - AquaSan improves rural water supply, builds water systems
  - Wood factory produces furniture & other goods for homes and schools

Examples from Angola, Malawi, Kenya, Tanzania, Zimbabwe, Uganda and elsewhere show real progress
2. Grow and develop housing microfinance: Malawi

Select Africa / Habitat for Humanity International partnership

- Select (private sector MFI) provides HMF
- HfH provides construction technical assistance – cost covered by Select
- 1900+ households served in Blantyre & Lilongwe – 40% of Select clients
- Plans to grow to other urban centres
- “site visits are an invaluable branding opportunity for both Select and HfH”
- Future plans
  - Refining overall cost model for CTA to increase capacity, offer more services
  - Getting to the client before they start construction
  - Increase volume of site visits and inspections

Off-site CTA

- Technical information, leaflets, sample plans
- Professional services & training: meeting with client regarding plans

On-site CTA

- 3 levels relating to complexity of project and level of TA required
- Different professionals for different tasks
- Multiple visits

The need to link HMF with the housing supply sector (through construction technical assistance & other support) make this different from traditional microlending and supports a good housing outcome.
In Kenya:

- Rooftops Canada coordinated $83,400 commitment from Co-op Housing Federation of Canada to match $250,000 funding from CIDA to create a Fund.
- Part of this has been used as guarantee to leverage a loan to NACHU (National Cooperative Housing Union) from the Co-op Bank of Kenya over 62 months, for HMF.
- Loan sizes <Kshs 400 000
- Group loans for land purchase can be higher
- Max term 48 months, many shorter
- Further loan to NACHU from Canadian Fund helped secure a large piece of land
- 660 families benefiting from combined facility

- **MicroBuild Fund**: $50m fund established by Habitat for Humanity International, providing debt capital and technical assistance to MFIs to grow HMF
- **New Urban Finance Facility for Africa**: catalytic investment fund to support HMF and finance for basic services initiatives Africa: Phase 1 in Ghana, Kenya, Uganda, Tanzania, West Bank. Target $100m
- **CLIFF (Community Led Infrastructure Finance Facility)**: established by Homeless International, in multiple countries in Africa

New funds see promise in housing microfinance products and approaches: big challenge is the development of sound capital structures – space for DFIs to offer advisory services
3. Finance rental housing

- Niche markets are undersupplied
  - Urban workforce
  - Student housing
  - Transitional housing
  - Housing for the elderly

- Different housing types & landlords offer new opportunities:
  - Inner city building rehabilitation
  - Inner city building conversions
  - New construction
  - Backyard dwellings
  - Small-scale landlords
  - Developers
  - Institutional landlords

In South Africa, International Housing Solutions and the Trust for Urban Housing Finance are building a strong track-record in how to build and finance rental housing.

Rental housing creates an investment class of sufficient size and stature to attract long term investors such as pension funds.
Thank you!

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Affordable housing finance at the base of the pyramid

Formalizing the informal, and HALF

Presented at World Bank 5th Global Housing Finance Conference
Washington, DC ♦ 30 May 2012

David A. Smith, Affordable Housing Institute
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Affordable Housing Institute:
Who we are, what we do

- Non-profit (US §501c3) pro-poor consulting and research firm
  - Boston, MA, USA: work worldwide, mainly global south
  - “Developing successful affordable housing financial ecosystems worldwide”

- Consulting
  - “Pro-bono/ low-bono investment banker”
  - Financial product design/ program design
  - Program development:
    - Market principles + government aid = affordability

- Research
  - Develop, explore, test, refute what we believe
  - Mexico City: Formalizing informal land
  - Istanbul: Urban regeneration to reduce disaster risk

- 2x grants from Bill & Melinda Gates Foundation
  - Develop theory of change and impact
  - Create AHI Capital Gateway, a ‘HALF impact lender/ investor’
Today’s slum is tomorrow’s city:
Formality and informality

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Formal becomes informal:
Additions are inevitable, and self-designed

Bahrain:
Self-built additions are the norm across all low-income areas. Single-skin concrete with little structural support most common second-story materials.
Informal becomes formal:
Self-built housing, Austin, Texas
Informal becomes formal:
Self-built housing, Durban, South Africa

What a difference a day makes!
HALF case: From housing burden...

Motiben in Ahmedabad
- Home-based worker
- Mother
- Spins thread for a living

... took 3 loans ...
- To improve her house/workplace
- Totaling Rs.18,000 ($400)

First she built a front porch
- Uses as her workplace
- Not disturbed by family activities
Monsoon was a problem
- During monsoon, Motiben unable to work
- Clay floor used to get wet and slippery
- Cut ‘charkha’ productivity and damaged the yard

So she tiled her floor
- Also with the loan funds

and plastered her walls
- Reducing dampness during rains
- Lengthening life of materials

Result: Motiben's productivity **tripled**, and her earnings increased from Rs.700 per month to Rs.2,000 per month.
Home Asset Loan Finance (HALF)

HALF-way between mortgage finance and microfinance

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Home Asset Loan Finance (HALF) : the ‘missing middle’ of lending

Mismatch in demand and financial product type supply

Providers
Size of sphere indicates relative number of loans available

- Banks
- MFIs
- Unfilled

Market size
Size of sphere indicates relative size of demand

- Demand for enterprise-based microfinance
- Demand for traditional mortgages
- Unmet demand for Housing Asset Finance

Missing supply between microfinance and mortgages

Unmet demand for mid-sized, mid-length loans for housing
It’s not mortgage finance (‘too informal’)
It’s not microfinance (‘too big, too long’)

Not mortgage finance
- No formal title
- Usually will not meet building codes
- High rates (usury laws?)
- Can you repossess the collateral?
- What is the resale value?

- “To a mortgage lender, this looks like a small short-term loan with rickety security”

Not microfinance
- Too big a loan amount
- Does not ‘finance income generation’
- Low rates (profit margins?)
- How will the borrower repay the loan?

- “To a microlender, this looks like a huge loan over a long time to somebody you don’t know”

• Neither will grow organically into the other
• Too many dimensions of difference
• Too much organizational gravity and business-model culture
Home asset loan financing: Requires creating new financial products

- Larger amounts
- Longer tenor
- The home as an asset figures in the credit decision
  - Use value, not exchange value

<table>
<thead>
<tr>
<th>Amount of loan</th>
<th>Duration of loan (tenor)</th>
</tr>
</thead>
<tbody>
<tr>
<td>$3,000</td>
<td>20</td>
</tr>
<tr>
<td>$2,000</td>
<td>10</td>
</tr>
<tr>
<td>$1,000</td>
<td>5</td>
</tr>
<tr>
<td>$500</td>
<td>3</td>
</tr>
<tr>
<td>Microfinance</td>
<td>1/2</td>
</tr>
</tbody>
</table>
What makes an informal home a HALF candidate?

- **Physical durability**
  - Good: it holds its value over time
  - Bad: it can deteriorate or fall apart

- **Demonstrable occupancy/use value**
  - Good: rentable or informally resell-able
  - Bad: occupant will not be motivated to protect

- **Longevity of tenure**
  - Good: family has history of residency, savings
  - Bad: transients, absentee landlords

- **City services**
  - Good: Mail, water, sanitation, electricity
  - Bad: “Off the grid”
HALF in the spectrum: Product and risk characteristics

<table>
<thead>
<tr>
<th><strong>Product features</strong></th>
<th><strong>Microfinance</strong></th>
<th><strong>HALF</strong></th>
<th><strong>Mortgage</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan (average)</td>
<td>$500</td>
<td>$2,500</td>
<td>$10,000</td>
</tr>
<tr>
<td>Tenor</td>
<td>0.25-1.0 year</td>
<td>2-5 years</td>
<td>5-30 years</td>
</tr>
<tr>
<td>Purpose</td>
<td>Improve income</td>
<td>Improve housing</td>
<td>Buy formal</td>
</tr>
<tr>
<td>Credit decision</td>
<td>Personal</td>
<td>Personal + use</td>
<td>Resale value</td>
</tr>
<tr>
<td>Collateral?</td>
<td>None</td>
<td>Partial</td>
<td>Yes; home</td>
</tr>
</tbody>
</table>

**Risk features**

<table>
<thead>
<tr>
<th>P = Odds default</th>
<th>Low</th>
<th>Medium</th>
<th>Higher</th>
</tr>
</thead>
<tbody>
<tr>
<td>L = Loss default</td>
<td>Nearly 100%</td>
<td>Unknown</td>
<td>Under 10%</td>
</tr>
<tr>
<td>Risk manage</td>
<td>Deny repeat</td>
<td>Assess use val</td>
<td>Underwrite prop</td>
</tr>
<tr>
<td>Risk mitigation</td>
<td>Repossess?</td>
<td>Pursue evict</td>
<td>Foreclose</td>
</tr>
</tbody>
</table>
“We need a really big insect”
“No, we need a really small airplane”

“An insect can be only so big”
“An airplane can be only so small”

“Anything in between is impossible”
Questions?
Email me: dsmith@affordablehousinginstitute.org

Sao Paolo: “We’re building a house.”
Affordable housing finance at the base of the pyramid

Formalizing the informal, and HALF

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Factors driven demand:
- Housing shortage estimated around 500,000 houses;
- Demographics characteristics and evolution:
  - Young population: 37% less than 19 years; 56% less than 29 years;
  - Households growth rate of 2.3%: 150,000 new households each year;
- Urbanization: 58.3% in 2011 against 51.3% in 1994 and forecasted to 60% in 2015
- Increased income:
  - 26.4 thousand MAD in 2011 against 14.4 in 2000
  - Unemployment rate less than 9% in 2011 against 13.6% in 2000
- Available lending: Housing loans/ GDP 16.9% in 2011 against 7.1% in 2000

An improved offer due to government incentives and emergence of large real estate developers:
- Doubling the offer between 2000 and 2011
Background

A strong and increasing housing demand

Housing Policy

A sound macroeconomic framework

Conclusion

- Structural rationals for a comprehensive mortgage finance system: A growth (average of 5% during 2006-2011) achieved in a stable macroeconomic framework, structural low inflation and interest rates benchmarks

6.2% between 1990 and 1995

1.9% between 1996 and 2011

Government securities interest rates
• Structural rationals for a comprehensive mortgage finance system: A financial sector reform carried over decades

<table>
<thead>
<tr>
<th>1st Generation</th>
<th>2nd Generation</th>
<th>3rd Generation</th>
</tr>
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<tbody>
<tr>
<td>90'</td>
<td>2000'</td>
<td>Currently</td>
</tr>
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</table>

- Liberalization and implementation of a new market architecture
- Consolidation of supervision and instruments
- Convergence to international standards and access to financial services

- Banking sector total assets of 130% GDP, lending 85% GDP and a medium solvency ratio of 12,3% (core equity 9,7%)
- Stock exchange capitalization of 74% GDP
- An important insurance industry and pension funds (on regional standards)
- A strongly regulated financial sector
- A financial market infrastructure with the main actors and instruments;

• Role of the Public authorities: developing a sound financial sector that allows financing housing of a market base and then address market inefficiency
Main affordable products/programs

• Main affordable products:
  – Social houses: Cost less than 250,000 dirhams (~$30,000);
  – Very low cost houses: Cost less than 140,000 dirhams (~$17,000). Used notably for slum households

• Supply incentives:
  – Cities without slums program: housing for over 300 thousands households financed notably by a tax on cement;
  – Mobilization of public land at competitive cost;
  – Tax incentives for social housing:
    ➢ Developers which commit to produce at least 500 social houses over 5 years do not pay income tax on revenue generated by this activity;
    ➢ Objective: encouragement of small and medium size developers to engage in social housing.
    ➢ Since 2011, agreements have been signed with developers for the production of almost 1 million social units over the next 5 years
Demand incentives:

- Tax incentives for main residence:
  - Deduction of interest payments of mortgage loans
  - VAT exemption on social houses for purchasers occupying the acquired home as their main residence for a period of at least four years;
- Before 2005: demand subsidies essentially based on Interest buydown (IBD) system (interest subsidies):
  - Main aim: to lessen the cost of financing;
  - A system that showed its limits:
    - Targeting: mainly medium income wage-earners benefits;
    - High cost
    - Complexity and cost of management of the system
  - Weak marginal impact
  - Macroeconomic stability permits a large decline in interest rates
  - Solution: move to more targeted system focusing on irregular and low-income households
- In the end of 2004: Implementation of Fogarim a mortgage insurance fund
Objective of Fogarim: encourage banks to finance low and irregular (informal) income households by securing their loans against credit risk;

Targeting:
- Informal income: precondition not have formal revenues (wages);
- Low income: social houses and monthly payment less than 1500 DH ~$176;
- Not a homeowner;
- Practice an activity that generates income

Parameters of Fogarim:
- Risk-sharing: The guarantee of 70% of the loan
- Only fixed interest rates
- Guarantee commitments are limited to 8 times the fund equity;
- Life insurance and mortgage security on the house;
- A premium fee correlated to LTV (introduced only in 2009): Annual premium of 0,325% for LTV less or equal 50% to 0,65% for LTV 100%.

Management of Fogarim:
- Strategic decisions: a steering committee headed by the MoF, with representatives of MoHousing, « Caisse Centrale de Garantie », Banks and real estates associations
- Operational management « Caisse Centrale de Garantie » a public financial institution supervised by the central bank
Currently around 1200 beneficiaries each month

Around 80,000 beneficiaries up to now

Outstanding guarantees:
11 billions DH (1.3 billions $)
Fogarim - Access to mortgage loans for informal income

Fogarim key figures: Characteristics

- **Interest rate (%)**
  - Average duration: 21 years
  - Duration (years)
  - LTV(%)
  - Monthly payments (MAD)
  - Average duration: 21 years
Fogarim key figures: Default (6’years generation of loans)

- **Cumulative Default Year +6**
- **Annual Default Year +6**

- **Cumulative Default**:
  - **Cities without slums program (~20% of Fogarim)**
  - **Fogarim excluding cities without slums program**

- **Annual Default**:
  - **Cities without slums program**
  - **Fogarim excluding cities without slums program**
<table>
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<th>Background</th>
<th>Main affordable products/programs</th>
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<td>Housing Policy</td>
<td>Fogarim - Access to mortgage loans for informal income</td>
</tr>
<tr>
<td>Conclusion</td>
<td>Funding instruments</td>
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</table>

- Securities and bonds issued by Banks and major real estate developers
- Securitization effective since 2002 and amended in 2010 but still underused: issuance of 4 billions dirhams (~$500 millions) and other expected operations.
- New covered bond act (draft) expected to be effective in 2013.
  - Double recourse: a claim on the bank (issuer) and a privilege on a cover pool of financial assets in priority to all other creditors (bankruptcy remote);
  - Cover pool:
    - Eligible assets: primary mortgage loans with LTV less than 80% for residential loans and 60% for commercial loans with additional limits (share in the total cover pool)
    - LTV can exceed 80% if a public guarantee fund is involved (Fogarim)
    - Minimum overcollateralization (5%) and coverage in stocks and flows
    - Specific supervision, controle and prudential regulations on the cover pool
  - Issuance limit (20% of total assets) with possible specific limits for bank with specific risk profile (bonus/malus)
- Other sources of financing real estate developers
  - New Housing contractual saving scheme: effective since April 2012:
    - Three years minimum saving, no tax on earned interest
  - New private equity law: expected to be effective by the end of 2012;
  - Real estate mutual funds project (expected for 2013): commercial and residential rental
On the supply side:
- An integrated policy for housing taking into account activities zones: public equipment, employment, ...
- Medium class households products
- From national to local strategy:
  - the forecasted production should cover the potential demand on the national level;
  - adequacy between the demand and offer at the local level remains an issue
- Urban zoning to be improved

On the demand side: FOGARIM (Damane Assakane)
- Moral hazard for « Fogarim VSB »
- New risk sharing parameters: portfolio approach, better modulation of the risk premium according to risk parameters, ...
- Move the system to a mortgage credit insurance institution

Other challenges: What role should play the government in mobilizing long term source of funding for social housing?