



DEVELOPMENT INNOVATION

## Engaging Slum Dwellers and the Private Sector to Finance a Better Future

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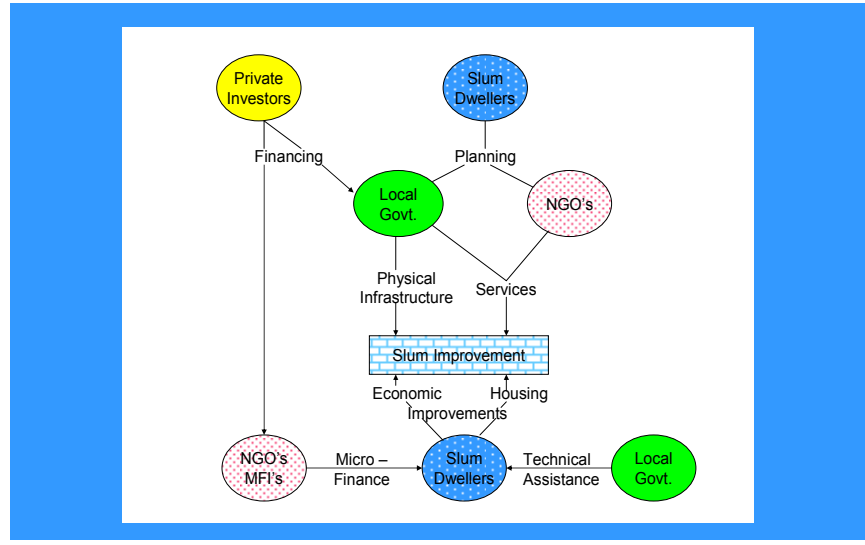
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Innovation through both Micro Finance and Infrastructure Finance

- Diverse models of microfinance for housing enable slum families to incrementally improve their own houses while also helping to augment their incomes through rents or micro-enterprise expansion.
- Cities can mobilize domestic private sector financing to substantially expand basic infrastructure into slum neighborhoods and thereby create an environment where slum families will want to improve their own housing.

### The Roles of Key Participants in the Slum Improvement Process



### Cost Projections & Need for Private Sector Financing

- The slum population in developing countries has passed 1 billion.
- U.N. estimates per person investment for slum upgrading is \$670.
- Upgrading all existing slum communities over the next 30 years: an average of \$22.3 billion per year.
- Additional \$26.8 billion per year needed to keep up with the expected growth of slum communities.
- \$49.1 billion per year for slum upgrading over the next 30 years is a formidable challenge.
- Investment from developing country governments and development agencies in slum upgrading was (at best) only \$6.6 billion in 2005.
- Engaging governments, international development partners, local capital markets and slum households themselves can mobilize 7 or 8 times the investment to make \$49.1 billion per annum achievable.



### Housing microfinance supports slum upgrading

- Housing microfinance is reaching low income households in developing countries, including slum dwellers.
- Incremental housing construction is the norm in most slums around the world, and best served by incremental housing microfinance.
- Housing microfinance relies on alternative forms of collateral, such as co-signers, group savings, home appliances and other non-mortgage forms of guarantee.
- The CEMEX/Patrimonio Hoy (PH) case demonstrates that the low-income population can be indeed a reliable and profitable segment of the market.



### Housing microfinance can be financially sustainable

- Housing microfinance providers can help national governments to upgrade slum communities.
  - For example, the Ministry of Housing in Morocco, currently undertaking a large slum upgrading program, estimates that 80% of slum dweller's financing needs will be met by incremental housing microfinance loans as opposed to mortgage finance.
- Mainstream financial institutions are critical to leverage local capital necessary to scale up housing micro finance and make it sustainable.
- The critical aspect for sustainability of housing microfinance is profitability (linked to reaching scale).



### To scale up slum dwellers' access to housing micro-finance...

- Reduce the risks perceived by private sector lenders/investors.
- Avoid premature and inappropriate regulations, especially interest rate caps.
- Establish strategic business partnerships to market housing microfinance.
- Develop capital market options to raise long term capital.
- Improve MFIs' housing loan portfolio performance, efficiency, technology, and ultimately, profitability.
- Promote research and best practice dissemination in the field of housing microfinance



### Municipal bonds support slum upgrading

- Cities scaling up their slum upgrading program city-wide need financing for municipal infrastructure.
- Municipal bonds have mobilized the necessary private investment to supplement local and central government funding, as well as international development assistance. Examples from India illustrate how this works.
  - In 1998, once it's the city's fiscal management was substantially improved, the AMC issued the first municipal bonds in India without a state government guarantee for Rs. 1 billion (\$25 million) for water infrastructure.
  - Eight towns surrounding Bangalore (a city of 5.7 million) in south central India have participated in a pooled bond issue as part of the financing for the Greater Bangalore Water and Sanitation Project (GBWASP). A core element of the slum upgrading efforts of these cities is the provision of water connections to poor households.



### Bonds for municipal infrastructure can be financially sustainable

- Municipal bond financing for infrastructure will be sustainable if two conditions are met.
  - First, borrowing municipalities must work to become financially sound.
  - Second, the institutional, legal and regulatory environment has to enable investors to feel they can accurately predict the risks of investing in municipal bonds.
- Liquidity in a country's long term capital market is needed.
- Investment policies of local capital market institutions fundamentally determine whether municipal bond financing is sustainable.
- Risk sharing is an important way for international development agencies and multilateral development banks to encourage the demand for municipal bonds.
- Encouraging and facilitating local revenue improvements is a way for central governments to promote municipal bond financing.
- Credit ratings help investors compare the risk of municipal bonds to alternative investments.



### To scale up the use of bonds to finance infrastructure for slums...

#### Scaling up will require...

- Initiative by municipal governments and their associations
- Support from central governments
- Support from international development agencies and Multilateral Development Banks
- Creative response from the local private sector



#### BRINGING THE PIECES TOGETHER – WHAT HAVE WE LEARNED?

- The basic lesson is that through innovations in financing, private sector actors can reach the poor in the slums and change their lives.
- The second lesson is that slum upgrading can be financed, in part, by slum dwellers and cities on market terms.
- A third lesson is that scaling up slum upgrading is facilitated by adopting both microfinance for housing and bond financing for infrastructure to supplement the resources of national governments and their international development partners.



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