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Private sector crucial to resolve housing challenges

Developing countries are threatened by a housing crisis. New models are needed to produce affordable and sustainable housing on a large scale. What role can the private sector play?

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Decent, affordable housing is crucial to development. It determines living standards; its location affects employment opportunities, while its mass construction can generate thousands of jobs. In most poor countries, however, both public policies and commercial organizations have largely mimicked the processes of high-income countries, catering only for their elites. This has led to ordinary people being marginalized, with millions condemned to self-built structures in informal settlements.

Providing affordable housing is difficult. Publicly built and managed housing projects in developing countries, lacking the disciplines imposed by market processes, have a very poor record. And the informal housing sector has proved a failure too.

The provision of affordable housing is dependent on a range of public policies that between them support an efficient formal market. Urban land rights need clarity; housing needs have to be integrated with work places through transport planning; building sites need access to public infrastructure before development begins; building standards must relate to today's realities; tenancy and ownership rights have to enable new houses, whether rented or owner occupied, to function as collateral; and, as commercial banks are so reluctant to lend, central banks should encourage financial innovation.

This new issue of *Private Sector & Development* reports on a range of significant recent initiatives. In India, for example, a new subsidiary of Tata has been able to harness the benefits of scale and standardization to build decent housing at a unit cost of around $10,000. And in Mexico, a new initiative has managed to marry the scale benefits of formal cement provision with the cost-reduction of community self-build to meet market needs.

These, and the other articles underline the need for a new beginning that builds on the huge potential of decent mass housing and in the process acknowledges the enormity of past failures. New policies need to be matched by new business models.

Housing the world: leveraging private sector resources for the public good

By 2030, around 3 billion people in the developing world will need housing. That means 565 million new units, adding to the current gap of more than 400 million homes. Building these will provide much needed employment in the construction industry and the supply of materials, fixtures and services. Challenges both on the supply and demand sides, common to most regions, must be overcome, however, not least in making finance available to those most in need.

Simon Walley

Senior Housing Finance Specialist, World Bank

According to UN-Habitat, more than half today's world population lives in towns and cities, and, in the next 40 years, urban environments are likely to absorb most of the projected population growth of 2.3 billion people (United Nations, 2011), as well as drawing in others from rural areas. By 2050, 6.3 billion people will live in towns and cities, almost 70% of the world's population. This urban explosion has led to burgeoning informal settlements. The Millennium Development Goal of 'significantly improving the lives of at least 100 million slum dwellers by 2020' was achieved by 2012 and 200 million slum dwellers now have access to improved drinking water, sanitation facilities, and durable, less crowded housing. But despite the proportion of the population living in slums falling from 39% to 33%, the overall number of people living in informal settlements has risen by 100 million since 2000, to 863 million, equivalent to about a third of the developing world's urban population. While informal housing can be regarded as an inevitable and necessary part of growing cities, offering a low-cost stepping-stone to better lives for migrants, efforts should be made to smooth the evolution of slum housing into mainstream city accommodation. The urgency and magnitude of the need for affordable housing in coming decades is clear. To meet the challenge of accelerated urbanisation, new solutions are required as the public sector alone will be unable to build sufficient housing or provide the necessary infrastructure (Figure 1). UN-Habitat calculates that, by 2030, around 3 billion people, about 40% of the world's population, will need new housing together with basic infrastructure and services. Assuming an average household size of five, 565 million new units will be required, adding to the current gap of more than 400 million units.

"By 2030, around 3 billion people, about 40% of the world's population, will need new housing."

SIMON WALLEY

Simon Walley has worked at the World Bank since 2006, particularly on the development of secondary mortgage markets through the creation of liquidity facilities, mortgage-subsidy schemes and covered-bond legislation. Previously, he worked as an economist for the Nationwide Building Society and acted as a banking regulator at the Bank of England and for the Financial Services Authority. He was also the Deputy Secretary-General of the European Mortgage Federation.

HOUSING THE URBAN POOR: A GLOBAL OPPORTUNITY

The urban revolution offers opportunities to emerging economies as well-planned, densely-populated cities are places of ideas, diversity and innovation. Beyond meeting the need for shelter, providing housing to a growing urban population is part of the broader benefits which cities offer in terms of social inclusion, access to services and welfare.
There are multiple economic benefits, too. McKinsey values the opportunity of filling the housing shortage in 16 of the largest emer-

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The World Bank Group is one of the world's largest sources of funding and knowledge for developing countries. As part of its work on deepening financial markets and access to finance, the housing finance team work on five strategic areas – building housing finance markets; funding housing finance; housing finance for the poor; supplying affordable housing; and housing finance crisis response. The World Bank supports client countries in achieving deeper and more inclusive housing finance markets through a mix of loan programmes, advisory services and knowledge products.

ging markets at USD 600 billion (McKinsey, 2012). In India alone, the impact of building 2 million affordable homes could create 3 million construction jobs, 24 million in linked industries and services, and result in a 2% growth in gross domestic product (GDP). There would also be a USD 17 billion rise in the demand for credit, a 16 million tonnes demand for cement while the need for steel would rise by 6 million tonnes.

Environmental gains are also available. The Intergovernmental Panel on Climate Change (IPCC) calculates buildings account for 40% of global energy usage, but this can be improved at no additional cost. According to IPCC, 29% of the housing sector's energy consumption could be reduced by 2020, while retrofits, primarily improved insulation and updated, energy-efficient heating and cooling systems, could save up to 90% of a building's thermal-energy use (International Energy Agency, 2012). The carbon footprint of house building could also be reduced by using smart technologies, for example, those that reduce the use of cement. Understanding amongst investors, developers and policy makers that green buildings can reduce costs, boost efficiency, lower footprints and generate local innovation is growing. The challenge, however, is to apply green-building technologies on a mass scale.

Common constraints for the housing sector

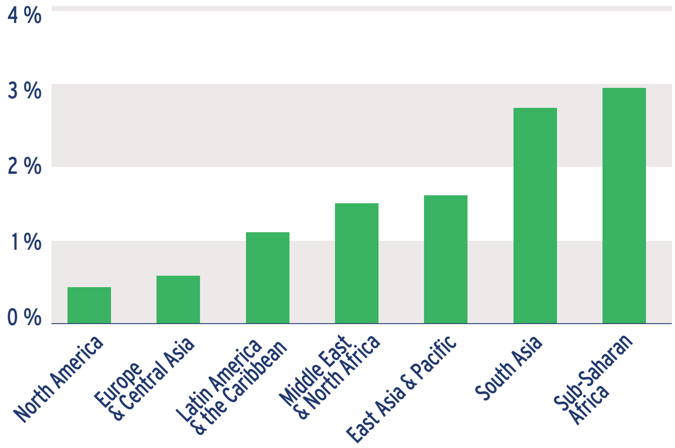
A common set of obstacles prevents the global urban boom from unleashing these opportunities. Although there are divergences in scale, the constraints on building more affordable housing are similar across countries and regions. They can be broadly categorised as impediments that limit demand, and ones that curtail the ability of developers to produce housing in sufficient numbers and priced for the mass market. Demand is almost limitless – those without housing need shelter and those with it want more room or improved conditions. However, turning this need or desire into effective demand is a challenge, with impediments typically related to finance. Housing finance has very low penetration in emerging economies where typically less than 5% of the adult population has a loan to purchase housing – it is 25–35% in the US, Canada and Western Europe.

"McKinsey values the opportunity of filling the housing shortage in 16 of the largest emerging markets at USD 600 billion."

This is despite the fact that in some markets housing finance has been taken up by the microfinance sector, which is well placed to serve lower-level market segments but is limited in outreach. The deep mismatch between demand for housing and the supply of investment is starkest in Sub-Saharan Africa and South Asia (Figure 2). Addressing this is problematic. Lenders face high credit risks, a lack of financial literacy among low-income households, difficulties in registering mortgage liens, the cost and time of foreclosing on properties, and a lack of access to long-term funds.

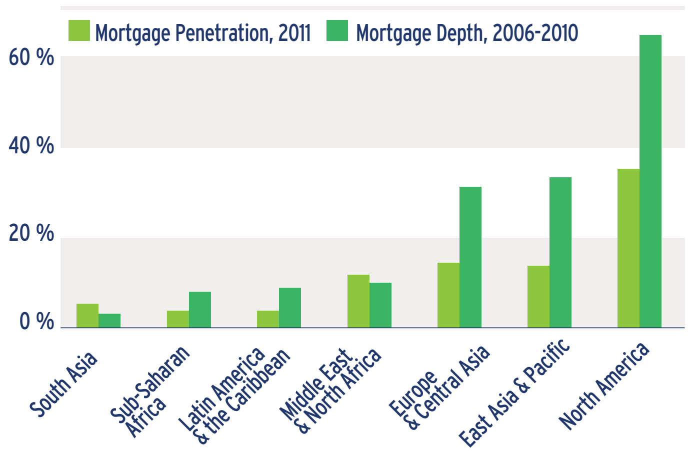
The supply side is challenging, too. Typically access to land and property rights limit the housing industry's ability to undertake large-scale affordable developments. Regulatory obstacles, such as difficulties in registering title or outdated building codes and planning regulations, add to the time and cost of building houses and limit affordability. Developers also often find it hard to access appropriate, long-term funding and ▸▸▸

FIGURE 1: ANNUAL URBAN GROWTH RATES BY REGION, 2015–2050



Source: United Nations, 2011

FIGURE 2: MORTGAGE PENETRATION IN 2011 AND MORTGAGE DEPTH FOR 2006–2010



Source: World Bank Group, 2011

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▶▶▶ can be required by lenders to provide such documents as feasibility studies that can only be produced once financing is in place. Effectively, the housing industry is hampered because lenders are unwilling to take the risks associated with new developments targeting social demand. A lack of public finances can also impede the state or local authorities in providing appropriate levels of infrastructure or public equipment to housing projects. Lastly, other common problems that developers face are the cost and availability of inputs including skilled labour, primary infrastructure – sewerage, access roads, electricity, etc. – and raw materials, which often have to be imported or are difficult to source in bulk in emerging markets.

"Governments, however, should not aspire to be the sole providers as the scale of demand now vastly exceeds fiscal resources."

From public-driven policies to public-private partnerships

In emerging markets, delivery of affordable housing solutions was considered the domain of governments, often with support from donor-driven institutions. Governments, however, should not aspire to be the sole providers as the scale of demand now vastly exceeds fiscal resources. Radically different approaches are required to address housing shortfalls at the pace required. This means mobilising commercial capital and embracing market-based housing solutions capable of addressing lower-income housing. Broken million-home promises, the inability to resolve land rights and failed housing banks must all be consigned to history.

Going forward, governments need to work with the private sector to create a business-enabling environment. There are a multitude of potential actors involved in housing delivery – households, sometimes represented by community-based organisations; financial institutions; developers, who feed a construction sector made up of many different-size companies from the local mason to international corporations; or municipalities. The role of government should be to put sound public policies in place to promote an efficient housing production chain and remove obstacles from the paths of potential actors to ensure they can work together effectively, enabled by the right incentive structures.

The housing industry requires sound macro policies guaranteeing low volatility, low inflation to promote longer-term finance, and lower interest rates – such an environment can do more to improve affordability than the largest subsidy schemes. Leveraging capital markets is another fundamental for ensuring that the right instruments exist to channel long-term funds from pension funds, insurance companies and investment funds into long-term housing investment. Access to land, whether for reasons of unavailability or insecurity of the regulatory environment, is another of the major hurdles to making housing accessible in emerging countries. Public authorities need to unlock what can be considered as 'dead capital', while better titling systems could expand property rights, making reliable and secure collateral available to all. Municipalities and local authorities also have a key role to play as the primary developers of urban plans. Sensible zoning, transportation systems and urban infrastructure planning provide the framework for efficient cities and can boost the economic rationale for developers to engage into affordable urban housing. To maximise the multiplier effects, housing policies should consider the whole housing value chain, including such related sectors as finance and real estate. Developing housing is also an opportunity for related areas, especially the construction sector. To promote inclusive housing solutions, instruments such as guarantees, subsidies or tax incentives that boost the availability of finance for housing units for the most disadvantaged should be developed.

Meeting the world's housing needs will contribute to the World Bank's objective of shared prosperity. Housing development has numerous multiplier effects, providing much needed employment, both in the construction industry and related sectors varying from the supply of materials, through finance to the supply of fixtures and services. Economic empowerment through housing may, however, require specific support to ensure housing solutions are made available to lower-income groups. Depending on the availability of government resources, this may involve targeted, smart subsidy schemes working hand-in-hand with the private housing and housing finance markets. It may also mean establishing the right conditions for a private rental sector to cater for the needs of low-income households. Good quality, affordable rental housing can act as a buffer for the absorption of migrants, but, without planned housing solutions, unplanned slums will result. ●

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A new generation of real-estate developers focusing on low-income housing

Developers who want to enter India's affordable housing market face many obstacles. But with an estimated market value of USD 245 billion, the sector is attracting growing interest. Tata Housing, one of India's fastest growing real-estate developers, is among a new generation of firms focusing on the low-income segment. Nonetheless, to achieve the sector's enormous potential, the Indian government will need to create a facilitating environment.

Pawan Sarda

Head of marketing, Tata Value Homes

India's urban population grew by 32% in the decade leading up to 2011, rising from 285 million to 377 million, out of the current total population of 1.2 billion. The housing sector has not kept up with this growing urbanisation, resulting in millions of families living in slums and a huge gap between the demand and supply of homes. The government, which estimates that there is a shortage of more than 18 million homes, is increasingly looking to the private sector to address the needs of low-income population. It is taking action at central, state, and local levels to try and overcome the myriad of obstacles faced by the affordable housing sector and create an enabling environment. India's real-estate market and its home loan sector traditionally focus on the higher-income segment. The estimated 22 million households in the low-income bracket have remained largely unserved. However, with an estimated market value of USD 245 billion, this segment is attracting growing interest from the private sector (Monitor Deloitte, 2013). Tata Housing, one of India's fastest growing real-estate developers, is among a new generation of firms focusing on the low-income population. In 2010, it created a dedicated subsidiary, Smart Value Homes Limited now Tata Value Homes Ltd (TVHL), to cater to this segment offering homes ranging in price from INR 40,000 (USD 640) to INR 100,000 (USD 1,600). TVHL has seven ongoing projects under two brands, Shubh Griha and New Haven in Mumbai, Ahmedabad, Bengaluru, Chennai and Pune.

PAWAN SARDA

Pawan Sarda is Head of marketing and product development at Tata Value Homes Limited, a subsidiary of Tata Housing Development Company. He is also part of a Tata group-wide customer loyalty programme. He was previously Chief Marketing Officer at India's Future Group, which runs chains of discount, department stores and warehouse shops. Pawan Sarda holds an MBA in marketing from the Institute of Finance and International Management in Bangalore.

A BUSINESS MODEL TAILORED TO THE LOW-INCOME SEGMENT

To provide low-income housing, Tata has developed a specific business model. Success in this sector depends on low prices, reduced production costs, a standardized range of products and a determination to prove that low cost does not mean low quality. The first major obstacle in India is finding land, which is available in only limited quantities in urban areas and which can rise in price by as much as 20–30% a year. Another constraint is the lack of infrastructure – public transport, sewage treatment, water and power supplies etc. – in the targeted areas, which usually makes it unviable for a developer to provide affordable housing without government support. ▸▸▸

"The first major obstacle in India is finding land, which is available in only limited quantities in urban areas."

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Formed in 1984, **Tata Housing Development Company**, a subsidiary of Tata Sons holding company, develops residential, commercial and retail properties; employs 650 people; and currently has 5.1 million m^2 at various stages of planning and construction. The company is involved in all consumer segments, from value housing to luxury homes, and invests in research and development to develop business models for low-cost housing. It aims to deliver quality construction through ethical business practices.

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▸▸ To overcome these constraints, Tata Housing selects developing townships that are well connected to the main city and where adequate infrastructure, and proximity to workplaces, shops, schools, and medical facilities make them attractive. Tata Housing aims to take advantage of the changing perception of such districts before land prices rise. The company does not own any land, rather it develops projects on a joint ownership basis with landlords, which helps the company maintain an asset-light model enabling higher rates of return and a shorter break-even period than is seen in more up-market developments. In order to reduce upfront acquisition costs, it also engages in public-private partnerships with government authorities for land where development approvals have already been secured.

To ensure houses remain affordable for low-income clients, operational costs have to be kept under control. This is achieved in part by developing a low-cost model that entails the building of smaller–sized buildings with standardised apartments and compact living spaces (32–46m^2). Keeping construction costs low is an enormous challenge as for affordable housing they constitute up to 60% of the total sale price – in up-market projects they make up around 20% of the price (Figure 1). The rising price of materials such as steel, cement and sand, and rising labour costs, have led to a 100% increase in construction costs over the past decade, adversely affecting affordable housing more than up-market construction (Jones Lang Lasalle, 2012).

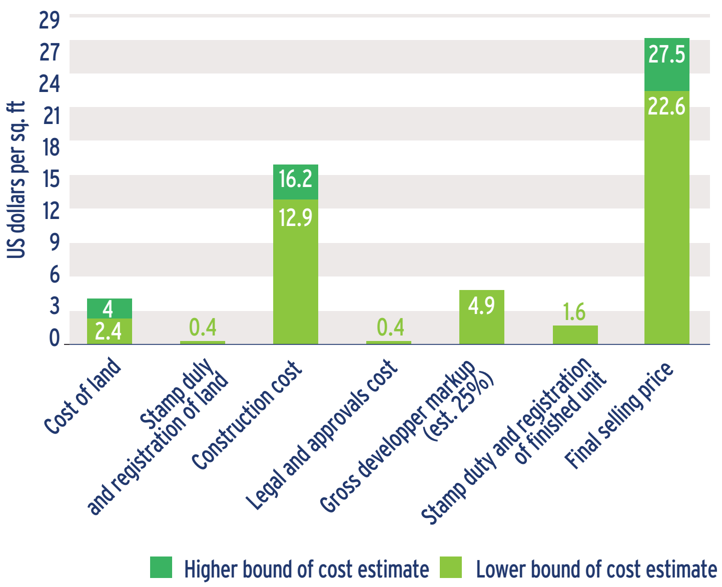
To protect themselves from this price volatility, Tata Housing seeks long-term contracts with vendors and suppliers. The use of low-cost technologies and raw materials such as reinforced concrete blocks, precast hollow blocks, precast lintels, floor tiles and polymer panels helps reduce construction costs by 20–30%. Technological innovation such as pre-fabricated buildings, made off-site and transported to the project, allow for multiple repetitions and quicker delivery while reducing dependence on labour and circumventing climate constraints. Achieving economies of scale is another vitally important element of the low-income housing model.

"Low-income solutions require minimizing costs whilst balancing the quality, safety and serviceability of the product."

ADAPTING THE OFFER

Low-income solutions require minimising costs whilst balancing the quality, safety and serviceability of the product. Tata drew on in-depth consumer research to design housing suited to the needs of low-income families. One of the most important requirements is to deliver quickly as low-income clients cannot afford delays. This means that an affordable housing project cannot emulate standard residential development schemes in which developers release their stock in tranches, expecting to realize gains due to rising real estate prices. With innovative technologies, such as prefabricated buildings, projects can usually be completed within a relatively short period of time of around 18–24 months. This also ensures Tata Housing speedy sales and reduced cash-flow risks, which is of great importance for low-income developers. Another important aspect is to offer sustainable housing, which minimises maintenance costs and energy consumption for clients. Tata Housing has been the leading proponent of sustainable developments in India – its premium, luxury and affordable housing schemes are all certified by the Indian Green Building Council (IGBC). Tata's IGBC-certified homes achieve 20–30% energy savings, compared to classical homes, by using for example glazed windows, energy-saving compact fluorescent lights, solar public lighting and 30–50% water savings through rain-water harvesting.

FIGURE 1: ESTIMATED CONSTRUCTION COSTS FOR LOW-INCOME HOUSING



Note: The model doesn't assume the capital structure of funds being used for development. Depending on the capital structure, a component of debt servicing will be added to final selling price.

Source: Jones Lang Lasalle, 2012

The combination of low-cost and easy credit is also key to the success of affordable housing initiatives. Commercial banks and other traditional home loans providers typically do not serve low-income groups. Developers like Tata can, however, partner with microfinance institutions to make home finance options available to buyers from the informal sector. Tata Housing works with the Micro Housing Finance Corporation to provide access to finance to end-buyers of Shubh Griha projects that cater for households with an annual income of less than the equivalent of USD 160. The success of a Shubh Griha project of around 1,000 apartments in Ahmedabad reflects the relevance of Tata Housing's offer. Around 10,000 people applied to buy a unit within a few days and lots had to be drawn to allocate the new homes.

Challenges of the affordable housing sector in India

The affordable housing sector may well be attracting a growing number of players, but the obstacles facing these developers are legion. Bureaucratic, regulatory and financial constraints prevent the market from achieving anywhere near its potential. Figures from the Town and Country Planning Organization show that 85,000–121,000 hectares of additional land are needed to cater for the demand of those earning less than USD 320 a year alone (KPMG, 2010). But finding land for development remains a major problem. It is a lengthy and costly process due to the difficulty of obtaining accurate transactional data – notably transaction prices – and the lack of comprehensive land mapping. Buyers thus lack access to reliable information on the options available to them and have to contend with an unregulated sector, with many uncertified intermediaries, for their land transactions. Policy measures, such as free-sale areas or extra Floor Space Index (FSI)[1] to facilitate access to land and encourage developers to create affordable housing, exist but they should be expanded and combined with further policies and proper urban planning. Mass housing zones should be included in city plans, and land records need to be rationalised to improve planning and the utilisation of land (Jones Lang Lasalle, 2012).

"Bureaucratic, regulatory and financial constraints prevent the market from achieving anywhere near its potential."

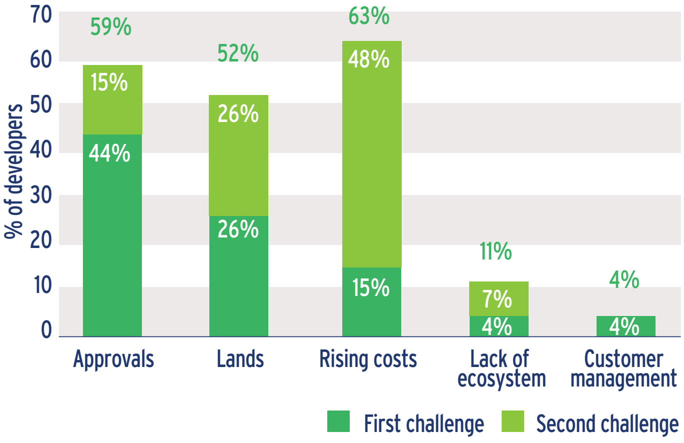
[1] *The ratio of a building's total floor area to the size of the piece of land upon which it is built. An increase in FSI means that more construction can be done on the same piece of land.*

The long approval process required by authorities is another major challenge facing developers in the affordable housing sector, as the business model relies on relatively fast completion (Figure 2). A typical development at present needs around 18 months to secure approval and takes a further 18 months for construction (Jones Lang Lasalle, 2012). Delay often leads to cost overrun, while if approvals were granted more quickly, the same developer could produce up to twice as many low-income housing units with the same capital (Monitor Deloitte, 2013). Reducing the number of approvals needed and providing time-bound approvals would be of great help.

Another issue is the lack of land with good infrastructure. Laying out infrastructure on the outskirts of cities would open up more areas for construction, would potentially dampen price escalation of serviced land and would also increase the supply of homes to the country's poorer families. Increased efficiency of urban local bodies – which oversee city planning, provide urban services and provide development approvals – and of urban development departments are key factor to creating a conducive environment for developers.

Frequent changes in real-estate and infrastructure policies, drastic modification of regulations, and overlapping guidelines are other factors that make project planning precarious (Jones Lang Lasalle, 2012). Developers buy land for projects that can take years from inception to completion, and are naturally perturbed if regulations are modified along the way. Inadequate regulation, combined with the absence of codified definitions and the lack of an ▸▸▸

FIGURE 2 : TOP TWO CHALLENGES AS STATED BY LOW-INCOME HOUSING DEVELOPERS



Source: Monitor Deloitte, 2013

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▸▸▸ authority to enforce building laws, is a disincentive for developers considering venturing into affordable housing. It is hoped that the planned creation of a new regulatory body will change this scenario. If the government, which takes 25% of the sale price of a property in taxes, ensured a level playing field, this would encourage more private players to enter the market to cater for the rising demand seen in India's rapidly-urbanising landscape.

Home financing, a major obstacle

The odds are also stacked against low-income developers when it comes to securing finance for their projects. Many are excluded from access to commercial banks because these lenders mostly do not provide loans against land; instead they have to turn to private borrowing at prohibitive interest rates. Some banks will lend to them, but at exorbitant rates of around 18–19%. High finance costs add 10–25% to the unit sale price (Jones Lang Lasalle, 2012).

"There is [...] a need to include the real-estate sector in priority-sector lending for Indian banks."

In the case of Tata Housing, which is part of a multinational group, access to funding has been relatively easy. It used internal group funding to recapitalise the company with USD 16.5 million in 2008 and USD 82 million in 2012. Tata Housing will have to seek additional funding for new ventures and is evaluating several options, such as setting up a real-estate fund, as well as a mix of other options like equity, internal accruals, mezzanine and debt financing. The situation is, however, different for most other private real-estate developers that lack cash or other collateral to support a construction loan, and the capacity to produce satisfactory project feasibility studies.
For its part, the housing finance industry is seeing strong opportunities in the growing housing sector. But the opportunity to provide lower-cost mortgages to the end customer could be missed if housing finance companies and microfinance institutions are unable to access long-term affordable debt for refinancing purposes. Housing finance companies acquire debt at 10–14% and lend at 11–17% but microfinance companies are unable to get funding at less than 15–17% for tenure less than 3–4 years, making it problematic for them to lend for mortgages (KPMG, 2010). Through the National Housing Bank,[2] the government could provide more low-cost credit to financial institutions serving low-income customers, while ensuring this benefit accrues to the customer. Finally, there is also a need to include the real-estate sector in priority-sector lending for Indian banks, which have traditionally considered it risky. This would ensure that housing loans are more easily secured than at present.

For India to achieve affordable housing for all, a key policy of the government, there is a need to realistically address the constraints faced by private developers and to formulate policies that encourage their participation in the affordable housing sector. Supply-side measures to encourage developers need to be expanded. These include reduced taxes, faster approvals, earmarking land for housing for those at the bottom of the income pyramid, mortgage-guarantee schemes to minimise the credit risk for the banks that finance the developers, and interest-rate subsidies (Monitor Deloitte, 2013). Demand-side interventions also need to be increased, including interest-rate subsidies through lower-cost refinancing for housing-finance companies and reduced taxes such as stamp duty and registration costs. To strengthen the market, the central government should also continue to oversee the development of a set of standards – clear definition of beneficiary segments, minimum size of housing units, criteria for projects to qualify for subsidies, etc. – that can be used by state and local governments for policy guidelines (Monitor Deloitte, 2013). ●

[2] *National Housing Bank, a fully owned subsidiary of the Reserve Bank of India, was set up primarily to accelerate housing finance activity in India and promote the Housing Finance Companies by providing them with financial support. It acts as the regulator of the housing finance industry.*

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Promoting housing policies coordinated with the private sector

To meet the housing challenge, developing countries need to create new housing production models. They need to collaborate with the private sector and support the entire housing sector in an integrated manner to achieve this. Securing land ownership and increasing funding for sector are the key conditions necessary to encourage private stakeholders to produce affordable housing on a massive scale.

Isadora Bigourdan and Thierry Paulais

Investment officer, AFD
Deputy director of Africa department, AFD

Public housing policies in developing countries – often supported by international funding agencies, applying formulas that have worked in the North – are struggling to meet the needs of rapidly growing populations. Housing generally remains accessible only to the better off, while the number of people living in substandard accommodation is growing by 25 million a year. Cities often expand haphazardly, with the majority of people living in informal settlements where sanitation and security are extremely poor.

ISADORA BIGOURDAN AND THIERRY PAULAIS

Isadora Bigourdan, a lawyer and graduate of Sciences Po Paris, is the investment officer in charge of coordinating housing finance issues for Agence française de développement (AFD). She joined the AFD in 2005, having previously worked for a legal practice, at Paris Chamber of Commerce and a subsidiary of Veolia Environnement specialising in civil engineering.

Thierry Paulais is deputy director of the AFD's Africa Department. After working with Caisse des Dépôts et Consignations, he joined AFD in 2000 as head of the Urban development division. He subsequently led a research programme for the Cities Alliance, supported by the World Bank. He has written several books on cities and housing – including Financing Africa's Cities (World Bank and AFD, 2012).

Confronted with proliferating slums, governments, as in South Africa and Côte d'Ivoire, initially concentrated on building free or low-cost social housing. These programmes, however, primarily benefitted state employees rather than those in poverty, while insufficient funding made them incapable of meeting growing demand. Then, governments turned to the private sector, tasking it with the mass production of low-cost housing. In Angola, Brazil and Mexico, for example, real-estate developers were granted fiscal incentives and subsidised land to build industrial-scale housing on the periphery of urban centres. With little planning, and driven solely by the need to recover production costs, many of these developments proved poorly suited to the needs of local people. Geographically marginalised and disconnected from urban networks – infrastructure networks (electricity, water, roads), economic networks (transport, retail, business districts) and social networks (education, healthcare, etc.) –, their unsuitability was quickly revealed, with housing sometimes abandoned by people who had received subsidies to facilitate homeownership or remaining vacant.

"Governments turned to the private sector, tasking it with the mass production of low-cost housing."

The failure of these real-estate projects highlights the need to analyse local populations' requirements more effectively and understand people's living spaces within a wider context. These days, it is gen- ▸▸▸

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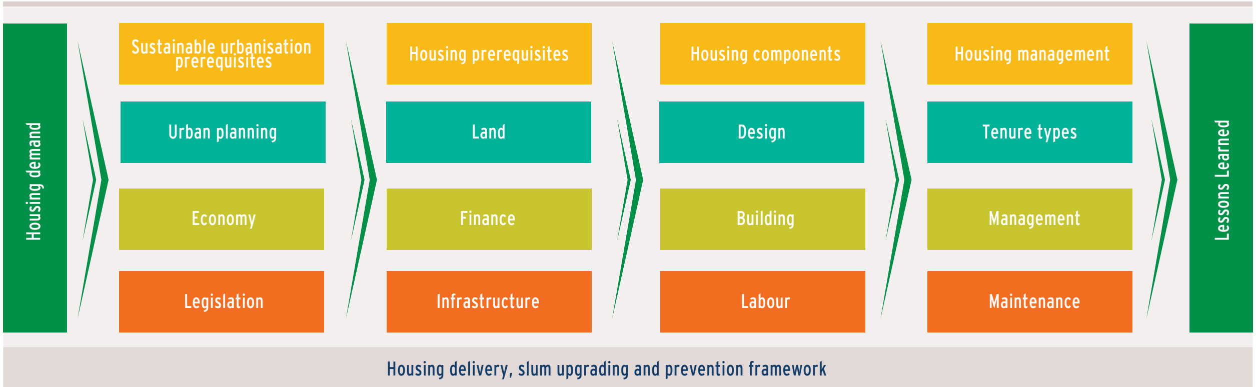
FIGURE: HOUSING FINANCE VALUE CHAIN



Source: UN-Habitat, 2012

▸▸▸ erally agreed that it is imperative to adopt a new method of housing production, integrating it within overall, sustainable urban policies. A genuine paradigm shift is therefore taking place as housing policies progressively abandon a narrow focus on buildings in favour of more broadly framed strategies.

Public funding will never be sufficient to meet housing needs entirely – which means that collaboration with the private sector is indispensable. Yet this is not about artificially supporting a sector by means of subsidies; rather putting in place incentives designed for optimum effectiveness. These incentives are especially important where the aim is to promote access to housing for low-income populations – a market that is not naturally taken into consideration by private developers. Governments must endeavour to create an environment favourable to private investment, while at the same time establishing a regulatory framework to guarantee the system's stability – and without forgetting to accurately identify the reality of housing demand across all population segments: a key factor in ensuring success. Furthermore, to be effective, a housing policy needs to involve integrated action across the entire sector, from macroeconomic fundamentals through to the types of building permitted – and include land availability, sector financing and the building of infrastructure (Figure). It is also crucial to actively involve all stakeholders.

"Across the developing world […] land regulation remains inadequate, increasing the perceived level of risk for private investors."

Securing ownership and planning land use

The risks inherent in real-estate operations – legal uncertainty in transactions, slow registration procedures and increased production costs – very often deter private investors investing in the production of affordable homes. The most frequently cited issues are those of land tenure and the legal system governing ownership. Across the developing world, particularly in Africa, land regulation remains inadequate, increasing the perceived level of risk for private investors. The coexistence of state and customary laws – which effectively govern land rights in many developing countries – creates serious problems: difficulties in establishing clear land ownership, lack of clarity in land regulation, low availability of land-related data, etc. The resulting land insecurity obstructs private investment and requires radical reform.

To establish a stable legal framework, governments particularly need to work to integrate customary law within the legal system. In Ghana, South Africa and Uganda, for example, reforms of this kind have led to the adoption of new land laws. Other measures such as land division using the cadastral model, simplifying plot registration procedures, establishing anti-eviction regulations and granting collective rights would also help (Paulais, 2012). States also need to clarify the laws governing real-estate collateral, taking account of specific local circumstances, to facilitate the growth of mortgage lending. In India, for example, a regulatory framework enabling lenders possessing the original mortgage deeds to assert their rights without recourse to law has been adopted. Together, these measures should help improve land regulation, a key first step towards the emergence of a sustainable local housing sector.

Land-use planning, which naturally follows on from the process of land organisation, has also been neglected by governments and international funding agencies, especially in Africa. Its absence creates a market bottleneck, impeding the housing sector's development. In the absence of public investment, developers often have to bear the cost of infrastructure before construction can begin. This additional cost is ultimately passed on to households through the increased price of the buildings and can undermine the profitability of real-estate programmes. Indeed, many African developers have had to shelve projects because they lack the necessary capital for these infrastructure investments; when these developers go bankrupt, they swallow householders' deposits, undermining market confidence. Morocco is an exception: with the support of international funding agencies, it created Al Omrane, a public operator dedicated to both housing and planning, actively facilitating an integrated approach to urban development policies. To encourage the construction of social housing, Al Omrane allocates productive land to stakeholders. This type of operator – public or quasi-public – effectively puts the issue of land-use planning back at the heart of housing policy and demonstrates why creating such institutions is a priority.

Responding to the scale of financing needs

Finance is the cornerstone of sustainable growth in the housing sector. Private developers need significant capital to start their projects and householders need to be able to borrow over the long term. The banking sector, however, is still reluctant to meet the financing needs of either people with low or average incomes, or private developers – focusing instead on the construction of housing targeted at higher-income households. The current investment deficit for new housing is estimated at USD 700 billion, while the mortgage market for Africa alone is estimated to be worth USD 1 trillion[1] (CSAE, 2012).

To promote the development of a market and attract private capital, public authorities need to facilitate access to long-term finance and put risk-sharing mechanisms in place. It is with this aim in mind that some governments have set up second-tier banks specialising in housing finance, enabling traditional banks to access long-term funds, making use of savings reserves held by pension and social security funds. These banks – public or quasi-public institutions, supported by international funding agencies – issue long-term real-estate securities guaranteed by mortgages and refinance local banks. Nigeria recently created such an institution – the National Mortgage Refinance Company.

To further encourage the banking sector, the public authorities can also put guarantee mechanisms in place to cover the initial losses of affordable housing construction programmes. Guarantee mechanisms of this kind can also be used to cover a portion of banks' mortgage credit risk – as it is the case in Mexico, Nigeria and South Africa. Finally, an increasing number of governments is supporting real-estate development programmes in the form of public-private partnerships, through the creation of companies dedicated to specific projects. Governments contribute the land, all necessary permissions and tax exemptions to reduce overall project cost. International or regional funding agencies cover the feasibility studies and the initial investment. The developers realise their programmes on behalf of the project company, which verifies the quality of the programme and subsequently sells the assets. The private investors can finance the operation in senior debt,[2] guaranteed by the project sponsors – the government and the funding agencies. In this way the risks are shared between the public authority and the private sector. The Akumunigo project, initiated by Shelter Afrique (SAHF), Development Bank of Rwanda (BDR) and the city of Kigali, to develop a mixed residential programme of 2,500 units, is a good example of this kind of initiative.

"The mortgage market for Africa alone is estimated to be worth USD 1 trillion."

New informal solutions to be encouraged and regulated

Public authorities should also take an interest in informal solutions developed by local people to meet their own housing needs (Box). Initially devised in response to an urgent need, these solutions spread rapidly and now need to be regulated. Here the private rental sector could make a valuable contribution as the vast majority of ▸▸▸

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Historically, AFD has been active in the housing sector, particularly in French overseas territories, as a shareholder or manager of real-estate companies. In emerging and developing markets, AFD's efforts focus on supporting financial intermediaries operating in this sector, leading a group of funding agencies financing housing in Africa and encouraging the emergence of new, affordable and sustainable housing solutions for excluded populations.

[1] Estimate based on 20 million households taking out loans of USD 50,000.
[2] 'Senior' debt benefits from specific guarantees and takes priority over other kinds of debt for repayment.

Private sector crucial to resolve housing challenges

▸▸▸ households worldwide rent their accommodation in unregulated environments. As a result, landlords can, for example, demand the payment of one or two year's rent in advance, as in Tanzania and Nigeria, or demand high rents for substandard housing with impunity. Yet, an effectively regulated rental sector can meet the housing needs of all population strata, simultaneously providing a way of harnessing domestic savings – and the savings of migrants – and generating tax revenues for local authorities. The adoption of specific regulations relating to the private rental sector in South Africa has encouraged the emergence of new, profitable business models. One example is the success of South Africa's Affordable Housing Company (AFHCO), which acquires former squatter settlements in the centre of Johannesburg, renovates them and rents units out.

"It is urgent to move beyond familiar models and innovate – both in terms of the construction itself and the way the sector is financed."

Self-build housing is another example of spontaneous, grassroots initiatives. Households with informal or irregular incomes have been able to acquire plots of land and build their own housing by adapting traditional microfinance products. As these experiments have often resulted in poor-quality housing, the state should regulate this kind of initiative to ensure that these districts do not become permanent informal settlements and set up a dedicated legal framework for housing loans. Nonetheless these private initiatives have fulfilled a need and should therefore be supported. The construction industry is taking a close interest in such initiatives – the Mexican cement group CEMEX, for example, has forged partnerships with microfinance institutions to help householders purchase construction materials using microcredits. The scheme is accompanied by technical support for the design and realisation of renovation or construction. Lafarge, the French construction group, has developed similar programmes in Asia, Africa and Latin America. This industrial-sector interest indicates the potential of the self-build construction market.

To be effective, housing policy needs to create an environment that encourages private initiative. Its efforts should focus on establishing a secure operational environment and implementing targeted incentives to promote the emergence of a stable, autonomous housing sector. Traditional public policies, or those lacking sufficient legal foundation, have proved unfit for purpose. In most countries, structural reforms have therefore been initiated to enable investors to develop mass, affordable housing production models and to support the mortgage market. Confronted with needs on the current scale, it is urgent to move beyond familiar models and innovate – both in terms of the construction itself and the way the sector is financed. The challenge here, after all, is to facilitate the production of affordable housing on a massive scale – and in a way that is sustainable over the long term. It is a considerable challenge. •

BOX: INTERNATIONAL FUNDING AGENCIES' HOUSING SECTOR ACTIONS

The community of funding agencies, led by the World Bank, has been active in the housing sector for many years. In macroeconomic terms, their efforts have primarily concentrated on defining rules for establishing land-tenure security and facilitating the emergence of a private homeownership market – to the detriment of the rental sector and other instruments such as rent-to-buy. Initially, most of the funding provided aimed to provide long-term funds at affordable rates of interest – to finance housing construction on the one hand, and mortgage lending on the other. After this came funding targeted at supporting buildings' energy efficiency, viewed from a Northern perspective. Noting that the households benefiting from these programmes belonged to the affluent middle class rather than those in poverty, the funding agencies are now looking to develop a new model to encourage the private sector to mass-produce affordable, sustainable housing. In particular, a number of agencies and key players in the sector (notably World Bank, International Finance Corporation - IFC, African Development Bank - AfDB, AFD, the Department for International Development - DfID, European Investment Bank - EIB, Finmark Trust) have formed a working group as part of the Making Finance Work for Africa initiative to coordinate action in this area.

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Regulated rental sector can meet the urban housing challenge

Governments in developing countries have rightly promoted homeownership as a way of alleviating poverty. But, faced with rapid population growth and the prospect of millions ending up in slums, they must focus more on developing rental housing solutions. Regulating the existing rental market and guiding its expansion will be essential to attract the private investors required for the delivery of adequate and affordable housing stock.

Marie Huchzermeyer

Professor, University of the Witwatersrand (Johannesburg)

To face the housing challenges of rapid population growth, most governments have in recent decades promoted homeownership. This form of tenure is seen as providing long-term housing security, relative autonomy for households and a solid basis for formal credit. When homeownership is effectively targeted at urban households, often through subsidies, it is credited with alleviating poverty and boosting political stability. Housing policies have promoted homeownership by improving finance systems, in particular by reducing barriers to mortgage finance, by adjusting taxation for owners and builders and by providing infrastructure for suburban homeownership to expand (Gilbert, A., 2008). In some developing countries – South Africa, Colombia, Chile, Costa Rica, Ecuador and more recently Brazil – homeownership for poor urban households has been promoted through subsidy programmes. In South Africa, fully subsidised or 'free' owner-occupied homes are widespread, with more than 2.8 million created since the advent of democratic government in 1994. Although there is currently an equal number of households inadequately housed. In other countries, homeownership for the poorest has been promoted via title registration for informal settlements. Peruvian economist Hernando de Soto argues that using registered property as collateral for formal loans – for home improvement, education or family businesses – can lead to the accumulation of wealth (De Soto, H., 2000). His critics counter that there is little evidence of a formal market for such properties and therefore banks are unlikely to accept them as collateral (Fernandes, E., 2002; Bromley, R., 2004).[1]

MARIE HUCHZERMEYER

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The limitations of homeownership

Homeownership policies are often promoted in low-density suburban settings and are criticised for failing to achieve the compact urban form sought by proponents of urban sustainability. New suburbs are located where land is available, mostly on the urban periphery, far from employment opportunities and amenities. This perpetuates dependence on cars and causes inconvenience and exclusion, especially where public transport is not provided or affordable. The titling of individual plots in informal settlements cements existing exclusion unless it goes hand in hand with state investment in infrastructure. For homeownership to succeed as a policy to increase the asset base of households, a formal property market that enables buying and selling and a move up the housing ladder must exist. Deeds registries, effective town planning and strictly implemented zoning and building regulations are required. For homeownership that is not fully subsidised, a well-developed banking system is needed to increase access to long-term mortgage ▸▸▸

"Homeownership policies are often promoted in low-density suburban settings."

[1] *It has further been found that the urban poor are risk averse and not readily taking up loans. This remains disputed in policy debates.*

Private sector crucial to resolve housing challenges

▸▸▸ finance. The World Bank has long recommended the expansion of homeownership for developing countries, but the requisite conditions are often lacking.

Formal homeownership remains an elite privilege in most developing countries. In middle-income states such as South Africa and Brazil, homeownership markets are larger than in low-income countries, and banking systems more developed. But they remain exclusionary, as illustrated in the following example. South Africa has faced insurmountable challenges in making two key institutions, deeds registry and banking, relevant to the lower-income sector. This has resulted in a skewed distribution of homeownership. In the population pyramid for income, the narrow top (upper-middle class) qualifies for mortgages, and the broad base at the bottom qualifies for fully subsidised homeownership. But this leaves much of the population stuck in the middle without access to either mortgages or fully subsidised housing. South Africa has tried to close the gap through targeted subsidies in the form of collateral support or mortgage underwriting, by promoting public transport and by unlocking rental housing acceptable to this income category. The reality is that 42% of households in South Africa do in fact rent. Much of this, however, is in inadequate, informal and unregulated rental stock.

"Formal homeownership remains an elite privilege in most developing countries."

Renting, a vital housing tenure option

While homeownership has been promoted in the developing world, few governments pay serious attention to developing or regulating rental housing. Experts argue that policies have long ignored the potential of private rental housing (Andreasen, J., 1996, Gilbert, A., 2008). UN-Habitat refers to rental housing as 'the neglected sector'. Yet, in many parts of the world, much of the population rents (UN-Habitat, 2003). The proportion of households renting is over 80% for most Kenyan cities, and in Port Harcourt in Nigeria. In Johannesburg, despite policies promoting and subsidising homeownership, 42% of households rent (Huchzermeyer, M., 2010).

Rental housing provides flexibility and lets households move easily from one home to the next, which is especially important for households when they need cheaper housing because income becomes tight. It is more affordable than homeownership as the payment of rent generally does not depend on securing a loan or paying house maintenance costs. When rents are monthly, with a deposit paid in advance, the tenant does not need to secure a large amount. However, rental housing is not always affordable or responsive to the changing needs of households. In Ghana and Nigeria, rents are charged in advance on a yearly basis, requiring households to amass significant sums before moving in (Arku, G., Luginaah, I., Mkandawire, P., 2012). Rental housing takes a variety of forms: houses, flats, rooms or huts, on a separate plot or in shared property, in formal or informal settlements. Kenya has a large stock of public rental housing as well as private stock ranging from poorly constructed rooms in informal settlements, single rooms or apartments in multi-storey tenements, and better-equipped and spacious middle-class homes in gated developments. However, much of this stock falls outside of the regulatory framework. Many rental districts in Nairobi include sub-standard buildings of eight floors, without lifts, with 100% plot coverage, housing more than 5,000 people per hectare, possibly the highest residential densities in Africa.

Landlords tend to build as many units as possible on their land. In properly regulated systems, this results in compact buildings through effective design, providing convenience to tenants and satisfying landlords' interests. But in poorly regulated markets, as in Nairobi, landlords often put their desire for profit well above the needs of their tenants. Tenants' health and safety are compromised by overdensification coupled with a lack of basic services. Landlords often fail to maintain their buildings, with the result that much of what UN-Habitat refers to as 'slums' consists of deteriorated rental housing (UN-Habitat, 2003). Although they produce much of the housing stock, such landlords are not acknowledged as stakeholders in urban policy forums, nor are efforts made to regularise this form of investment (Huchzermeyer, M., 2011).

Promoting regulated private rental markets

The production of affordable rental housing requires policies that encourage landlords and developers to make long-term investments.

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It provides supervision to a large cohort of PhD students drawn from South Africa, other developing countries and the global North. The School is host to the Centre for Urban and Built Environment Studies as a base for collaborative research within the School and beyond.

These policies should create a banking system that provides loans to landlords and developers. They should also deliver a regulatory system that protects tenants but also allows for sufficient building densities that enable investors to make meaningful long-term returns. Nairobi lacks such a system. The result is that landlords in the tenement market often invest in a maximum number of units per plot and expect to make their return in as little as three years. If the stock deteriorates after ten years, the landlord has still made sufficient return and can afford to write off the investment, allowing it to deteriorate into a slum (Huchzermeyer, M., 2011).

Regulatory frameworks need to balance the interests of landlords with tenants' rights. In South Africa, legislation exists to protect against arbitrary evictions. This is often violated by landlords, although in some cases litigation has led to tenant protection. One example that illustrates the problems caused by the lack of properly enforced regulation can be seen in South Africa, particularly in the high-rise centre of Johannesburg. So-called 'hijackers' have taken over buildings by force, extracting rent but not paying rates or taxes. In Nairobi, landlords sometimes resort to violent eviction measures, with relative impunity. Thus, in neither South Africa nor in Kenya can one speak of an adequately regulated rental market. For policy to regulate the existing private rental market and guide its expansion, land has to be made available in appropriate locations and with appropriate regulations. Incentives in terms of taxes or special development rights must be in place to ensure affordable units are built there. In land acquisitions, rental investors compete with those wishing to invest in units for sale. Increasingly, urban policies in developing countries try to shift away from the land-use separation that dominated urban planning in the post-World War II era. They now seek to mix incomes, tenure forms and land uses. Most cities in the developing world face the challenge of ageing infrastructure, in particular water supply, sewerage and electricity. Regulation of the rental market, with the extraction of fair taxes, is thus essential for the adequate servicing of new housing areas.

Another policy measure that would boost rental stock is to encourage a range of rental investors, from individuals to large-scale developers. South Africa subsidises social landlords – housing associations providing housing on a not-for-profit basis. Municipal housing stock also forms an important component of the not-for-profit sector. Not-for-profit actors in the rental market can play an important role of moderating private competition, in terms of rents charged and quality of units provided. Rental housing is a necessary component of any city's housing stock. Where new incentives are developed and stock provided through government subsidies, provisions must be in place to ensure these reach the intended market. Down-raiding the displacement of low-income households from adequate housing by the better off, must be anticipated and countered. This can only be done by balancing the housing supply and ensuring long-term conservation of subsidised low-income units for that target group.

"Regulatory frameworks need to balance the interests of landlords with tenants' rights."

In the rapidly urbanising developing world, there is clearly a role for both homeownership and rental housing. State subsidisation of homeownership and rental housing is relevant in contexts of extreme inequality. However, in both rental and homeownership, the private sector has a role to play and needs to be guided through policy. For homeownership, it is primarily affordable financing that should be promoted. For rental housing, policies must ensure appropriate investment in stock, the financing of this investment, and good management. This requires policies which guide financial institutions and investors into sustainable and inclusionary practices. Legislation and regulation are also required to curb excesses, such as exploitation and exclusion, which are the norm in unregulated markets. Changing entrenched practices and landlord entitlements is a major challenge for policymakers. Landlords and investors must also be embraced as stakeholders in policy debates to ensure their commitment to delivering much needed affordable housing stock. •

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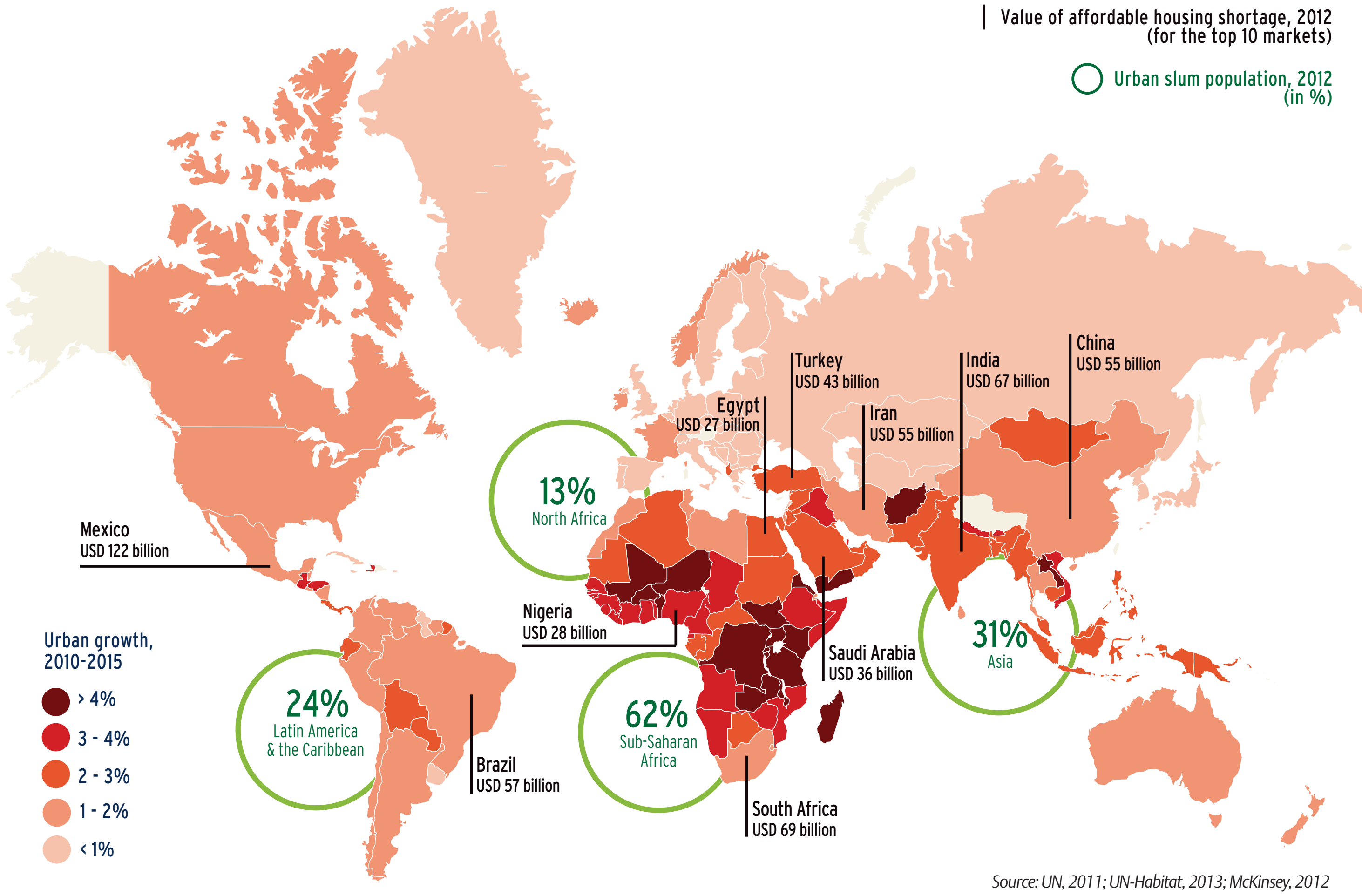
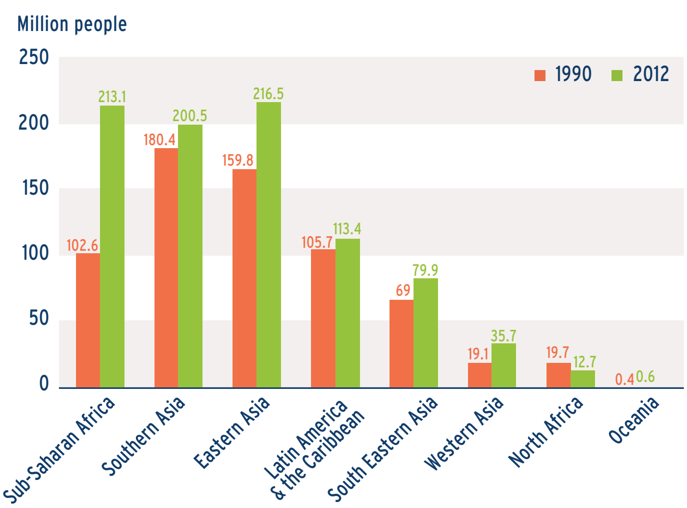
Intense urban growth and a high proportion of the urban population still living in slums makes accessible housing a major economic and social issue in developping and emerging countries. It is also a de facto high-potential market in which the private sector must play a prominent role. The challenges to unleash this potential are however many: deepening of the housing finance sector, access to land, contained construction costs, simplification of administrative and regulatory procedures, etc.

Potential and needs for affordable housing



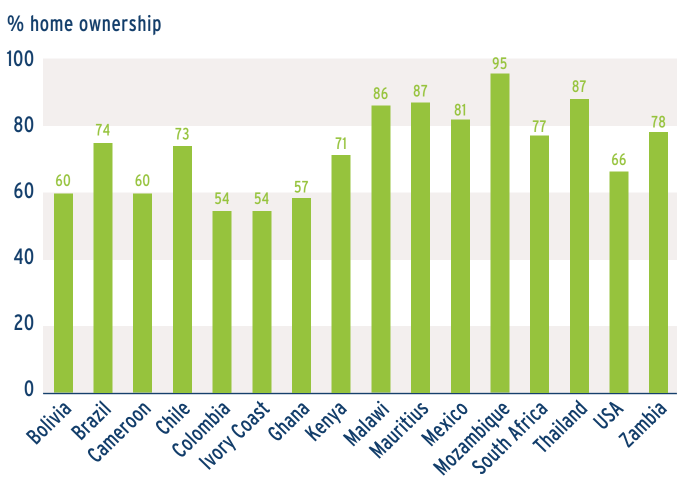
Source: UN, 2011; UN-Habitat, 2013; McKinsey, 2012

Urban slum population by region, 1990-2012



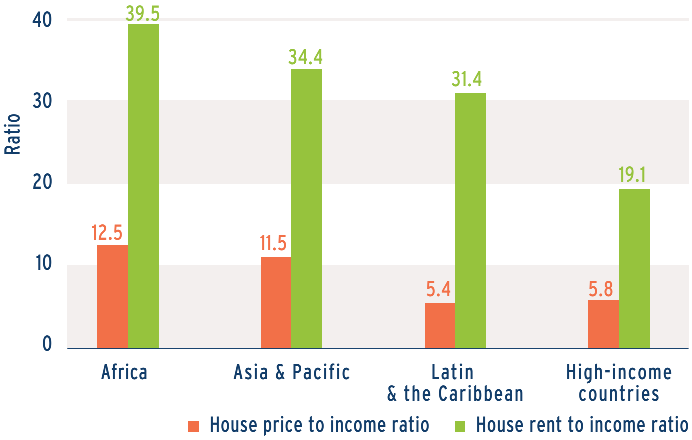
Source: UN-Habitat, 2012

Housing tenure, 2011



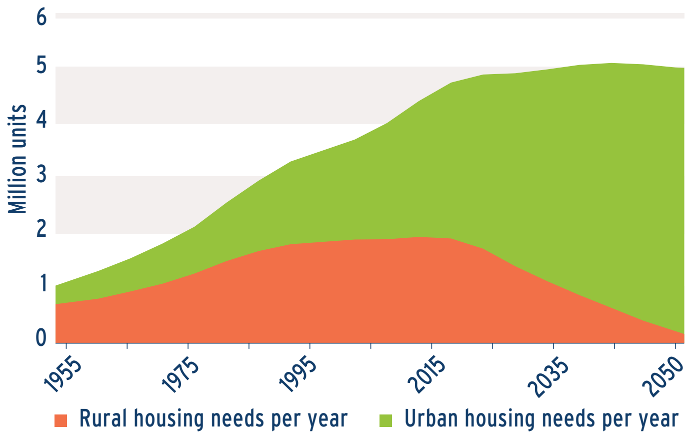
Source: UN-Habitat, 2011

House price and rent to income ratio, 2011



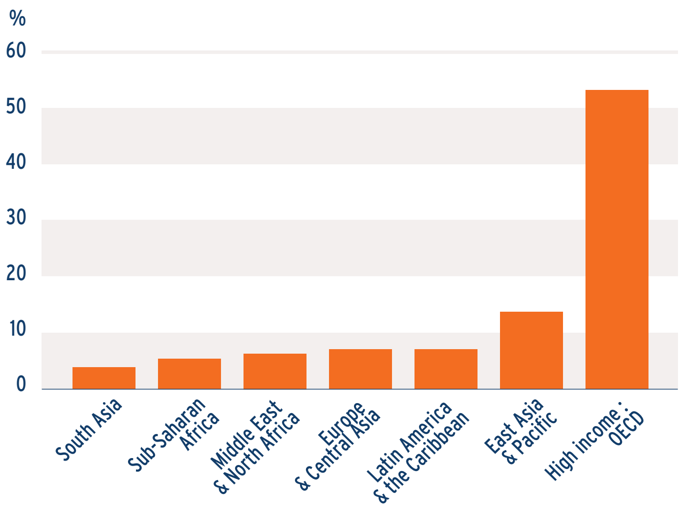
House price to income ratio: Median house price divided by median household income.
Rent to income ratio: Median annual rent divided by median annual renter household income.
Incomes are median gross incomes of private and public renter households.
Source: UNCHS, 2001

Africa's new housing needs, 1955-2050



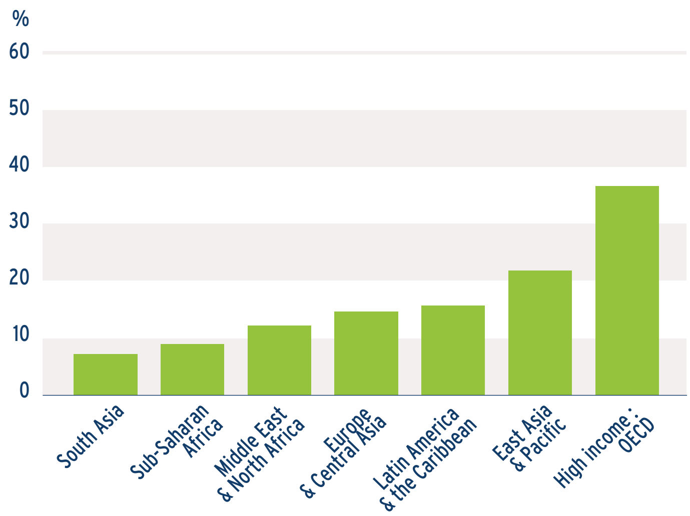
Note: These figures reflect new housing needs and not existing back-log or stock depreciation.
Source: Walley, S., 2012

Housing loans value by region (as a % of GDP)



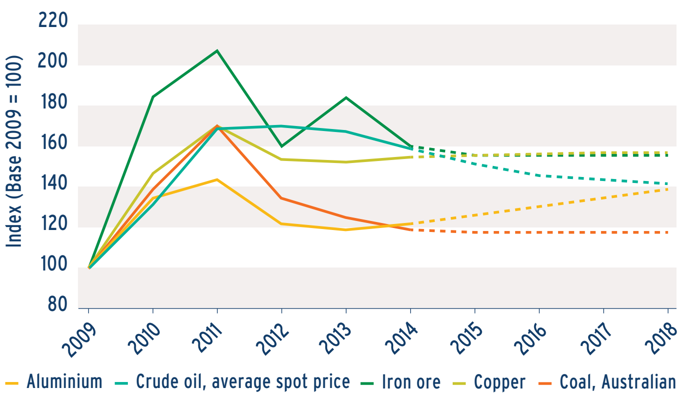
Source: World Bank, 2011

Housing loans value by region (as a % of the overall loan portfolio)



Note: For Sub-Saharan Africa, the average would be less than 7% without South Africa.
Source: World Bank, 2011

World commodity prices, 2009-2018



Note : Looking forward, the International Monetary Fund (IMF) forecasts that most metal prices will continue to fall over the next 3-4 years. Aluminium prices are however forecast to rise, partly as a result of exposure to increases in energy costs.
Source: IMF, 2013; EC Harris Research, 2013

Time and cost for property registration and construction permit, 2012

	Time		Cost	
	Registering property (in days)	*Obtaining construction permit (in days)*	*Registering property (as a % of property value)*	*Obtaining construction permit (as a % of income per capita)*
OECD	*24.1*	*147.1*	*4.4%*	*84.1%*
Sub-Saharan Africa	*58.9*	*171.1*	*9%*	*736.8%*
Middle East & North Africa	*33*	*145.7*	*5.9%*	*283.3%*
East Asia & Pacific	*81*	*146*	*4.5%*	*104.7%*
South Asia	*99.4*	*193.3*	*7.2%*	*850.7%*
Latin America & the Caribbean	*65*	*215.5*	*6%*	*136.6%*

Source: Doing Business, 2013

Private sector crucial to resolve housing challenges

The complex challenge of building a home loans market in Ghana

Inadequate real-estate supply and the absence of a deep capital market have hampered the development of the home loans market in Ghana. The rapid success of Ghana Home Loans shows that there is a large and unmet demand for these products. Sustained efforts by the government and regulatory authorities are required to build an enabling environment and to create the conditions for increased access to mortgages.

Dominic Adu

Chief Executive Officer, Ghana Home Loans

It is a truism that in developing countries demand for housing outstrips supply. In Ghana the deficit is estimated at more than 1 million housing units, and growing by up to 70,000 units a year (UN Habitat, 2011). Much of this demand is for low-income social housing. The 2010 National Housing Policy was crafted to incentivise the private sector to provide housing for all income brackets, notably through tax holidays and financial guarantees for real-estate developers or zero tax on equipment and machinery imported for housing construction. The long-term effect of these policies still remains to be seen since private real-estate developers provide only 10% of the new housing supply, with the remaining 90% being delivered by householders themselves. Few Ghanaians can afford to acquire their homes and most of them lack access to home loans facilities. Most banks neglect the home loans market and focus instead on short-term lending and investment such as risk-free government bonds and trade finance facilities that can offer higher returns while consuming less capital. Only 4 of Ghana's 26 banks officially offer home loans as a product. The total home loans book in Ghana is around USD 180 million and the number of borrowers just under 6,000 (Figure).

A business model tailored to Ghana's market

Ghana Home Loans (GHL) was launched in 2006 as a non-bank financial institution (NBFI)[1] specialising in home financing to respond to the large unmet demand for home loans. GHL is the only non-bank housing finance operator in Ghana with a portfolio of USD 84 million and a market share of around 50%, which it achieved within just a few years. Ghana Home Loans modelled its operations on South African Home Loans (SAHL), a very successful non-bank home loans provider, and was supported by the same shareholder, Standard Bank, a major South African bank. The NBFI status was chosen over a banking model because of the relatively lower start-up capital requirements and the fact that being a bank did not offer any immediate advantages because of the lack of the long-term savings in Ghana needed to provide long-term home loans. In addition, this pure-player business

[1] *A non-bank financial institution is any financial institution other than a fully-fledged bank licensed and supervised by Bank of Ghana.*

FIGURE: MORTGAGE MARKET IN GHANA

	Portfolio (in million dollars)	Market share (%)
Ghana Home Loans (GHL)	84	47
HFC Bank	47	27
Fidelity Bank	24	14
CAL Bank	6	3
Ghana Commercial Bank	4	2
Barclays Bank	12	7
TOTAL	177	100

Source: GHL, 2013

DOMINIC ADU

Dominic Adu co-founded Ghana Home Loans, the leading residential mortgage finance provider in Ghana, in 2006. He previously acquired private equity experience working for ten years as an investment principal with Actis, a UK-based emerging markets private equity fund manager. He was responsible for major investments in West Africa. Dominic is an economics graduate from the Universities of Manchester and London and a qualified chartered accountant.

model is able to deliver a more efficient and tailored service to customers than banks can provide (Box 1).

Initially GHL only offered loans for the purchase of completed properties. That sector currently accounts for 82% of its portfolio. But given that some homeowners in Ghana prefer to build their own homes, the company has greatly expanded its product range. It now includes loans to complete a house that the borrower has started building; loans to build a house from scratch; loans to buy land; and home equity releases.[2] Since commencing operations, GHL has disbursed more than USD 115 million to 1,600 households, with an average loan size of USD 69,000 (World Bank, 2013), and strong asset quality with a level of non-performing loans of less than 3%.

"The only possibility for GHL is to secure long-term funds from foreign development finance institutions [...] in US dollars."

In the absence of a mature financial market in Ghana offering long-term resources and a securitisation framework, the only possibility for GHL is to secure long-term funds from foreign development finance institutions (DFIs) in US dollars (Box 2). This funding from the DFIs has compelled GHL to lend in US dollars although half of its borrowers earn local currency salaries. Therefore, cedi-earning borrowers face an exchange-rate risk as historically the cedi has depreciated by 13% per annum. However, this is compensated by annual wage increase of 15%. In order to protect borrowers against higher than expected cedi depreciation, GHL has set up a scheme to encourage borrowers to pay approximately 10 % more in local currency than the precise scheduled monthly repayment. This allows them to build a reserve so that if the currency depreciates they can use that reserve to make up for any shortfalls in their repayments prior to any salary adjustments.

Lending in US dollars obviously has its risks, but it actually enables the borrower to afford a property. Interest rates in US dollars are far below local-currency rates, which can reach 30% per year and are thus unrealistic for most customers. While US dollar loan interest rates are lower than cedi loans, they are still high, up to 15 % for dollar loans. Inevitably GHL's products are mostly accessible to middle-income earners. The ambition of GHL is, however, to target lower-income segments in the future. The deepening of the financial market as well as changes in the real-estate sector will be needed to achieve this objective.

[2] A loan, using a property already owned as a collateral, for specific purposes such as home improvement, medical, education and business expansion.

The specific challenges of Ghana's housing sector

The mortgage market in Ghana is still in its infancy. With a total home loans book of USD 180 million, it is far less developed than the market in South Africa, which is valued at approximately USD 170 billion. The huge difference in size is due to various economic and financial factors and to the nature of the housing market in each country. In Ghana, the stock of mortgageable properties is small, while in South Africa it is large and coupled to a well-developed secondary property market supported by an extensive real-estate broker network, which makes it easier for home loans providers to achieve scale rapidly. The South African non-bank sector has grown rapidly and has been boosted by its mortgage switching facility.[3] In Ghana, real-estate brokers are still informal, although professional institutions such as Broll and JHI of South Africa have begun to enter the market. Ghana Home Loans predominantly writes loans on new properties and took over five years to disburse USD 100 million. By comparison, SAHL reached USD 1 billion within three years, mainly due to ▶▶▶

[3] Switching mortgage is where a borrower switches their loan liability from one lender to another to benefit from a more competitive interest rate.

FOCUS

Ghana Home Loans (GHL) is the country's only residential mortgage specialist with assets of USD 100 million. It was founded by three Ghanaians with funding from Standard Bank of South Africa; Dutch development bank, FMO; and United States development finance institution, OPIC. It was also funded by Proparco; the International Finance Corporation (IFC); Shelter Afrique; and German development bank, DEG. It has funded more than 1,600 homes with total loans of USD 115 million. It is pioneering mortgage-based securities in Ghana.

BOX 1: THE STRENGTH OF THE NON-BANK MODEL IN SOUTH AFRICA

The home finance market in South Africa is dominated by the big retail banks – Nedbank, ABSA, Standard Bank and FNB – who have a 90% market share. Their dominance is due to the size of their balance sheets, unrivalled access to data on customers, extensive branch networks, brand recognition and a wide product range. Though only relying on securitisation, non-bank home loans providers such as SAHL and Interger are nevertheless able to compete with large banks as their focus on one type of product enables them to offer a faster service without incurring the cost of maintaining branch networks. The sustainability of the non-bank financial institutions (NBFI) model is evidenced by the fact that even in mature economies like Britain, non-bank institutions such as Paragon still exist. South African NBFIs, after mastering securitisation funding mechanisms, have demonstrated their ability to succeed. The market in Africa is growing and is potentially large enough in many countries to accommodate both banks and NBFIs.

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▶▶▶ borrowers switching to them from banks to avail themselves of better interest rates. The development of a secondary property market in Ghana, currently impeded by the fact that homeowners see their properties as purely for accommodation rather than as an investment, will be required to fuel the growth of the home loans market and to enable home loans providers to achieve scale.

«The development of a secondary property market in Ghana [...] will be required to fuel the growth of the home loans market.»

The limitations of the capital market in Ghana have proved another challenge to GHL. So far, the only access to long-term funds at competitive rates has come from DFIs. In South Africa, NBFIs have been helped by increasingly deep and sophisticated capital markets that have given them access to securitisation since 1989, enabling them to obtain funds at costs similar to banks and to fund their loans using capital markets and in local currency. This is a luxury not available to GHL, whose funding model involves negotiating long-term facilities with DFIs. At this stage, GHL is not able to diversify its funding sources because the capital market in Ghana is small and illiquid and a securitisation framework has still to be built.

In Ghana, as in many developing countries, home loans providers such as GHL or the local commercial banks face many other challenges, such as inadequate property supply, unsophisticated underwriting techniques due to a lack of well-developed and resourced credit reporting systems, and delays in title registration. They also suffer from difficulties in collateral enforcement, which are exacerbated by a lack of government incentives such as mortgage tax relief or first-time home purchase subsidies, and by a lack of long-term capital in the capital market.

Prospects for the home loans sector in Ghana

The home loans market environment in Ghana has recently seen signs of significant improvement. These include the introduction of credit bureaus that give lenders access to the credit history of borrowers within seconds; legislation to speed up the foreclosure process, reducing it from 18 months to just over 90 days; and a new collateral management regime that allows for immediate online registration of collateral at the Bank of Ghana – prior to 2010 the process took up to 18 months.

There has also been a gradual extension of local-currency bond tenors – from five to seven years – while government and regulatory institutions have prioritised the development of a viable bond market. Additionally, pension reform has granted the private sector access to pension fund management – previously a state monopoly – and thereby created a new pool of long-term commercially investible funds. It is in this context that GHL is striving to build an adequate securitisation framework with all relevant stakeholders to issue its first mortgage-backed security in Ghana by the second quarter of 2014.

Though significant progress has been made, the government needs to also consider subsidising developers so that construction costs will be reduced and passed on to homebuyers, or subsidising buyers, via measures such as mortgage tax relief, to increase affordability. Urgent areas for reform include introducing the legal and regulatory framework for securitisation, and faster title transfer, building approval and foreclosure processes. Ultimately, as in many emerging economies, it is only with a deep, liquid, long-term local currency bond market with the adequate regulation, fiscal and legal frameworks and enabling institutions, such as credit rating agencies, that Ghana will be able to create a viable home loans market.

The GHL experience has been that, despite the difficult operating terrain, the demand for home loans is very strong and that most borrowers are firmly committed to meeting their loan obligations. This underlines the need for further efforts to create an enabling environment. This will be a key condition for lowering interest rates, which in turn will help improve access to home loans for all income brackets. •

BOX 2: SECURITISATION, POOLING LOANS AS COLLATERAL TO ISSUE BONDS

Securitisation is a process by which a lender creates an homogenous pool of home loans and uses the cash flows from this as collateral to issue securities (bonds) to local or international investors. The value of the pool used as collateral is often higher, normally by 10%, than the amount raised by the issuance. Credit-rating agencies, lawyers and accountants are employed to evaluate the pool in order to assure buyers of the securities that they are not being sold non-performing loans. The home loans lender can use securitisation to gain further liquidity to write new loans and may benefit from a lower regulatory capital requirement. The home loans lender also looks after the loans on behalf of the investors for a fee. Investors get a better match of their liabilities, often long-term periodic pension payments, to their assets, the proceeds from the securities.

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Housing public-private partnerships in Latin America: lessons from Mexico and elsewhere

In the early 1980s, Latin American governments abandoned direct production of public housing in favour of the enabling housing markets approach. They heavily subsidised private developers and mortgage lenders to go down-market in an attempt to reach low- and medium-income households. But, as illustrated by the case of Mexico, this approach has performed poorly. A new housing entrepreneurship, led by innovative public-private partnerships, is now emerging to satisfy the mass market.

Bruce Ferguson

Independent consultant

National and state governments in Latin America first responded to the challenge of accelerating urbanisation and growing slums by developing housing units and financing these projects directly. Large government agencies, often called Institutes of Housing,[1] contracted private developers to build these units. National governments mobilised funds for financing these projects through mandatory salary taxes on formally-employed workers. The housing finance agencies often doubled as pension/ social security schemes to ensure that long-term savings would match fund long-term investments for mortgages. However, Latin America's public housing systems produced relatively few units of inconsistent quality, often in poor locations, frequently lacking basic urban services and land title. They were also highly expensive as builders had little incentive to keep their costs down. Governments typically contracted private builders with cost-plus-inflation pricing to carry out these projects. Patronage and political affiliation heavily determined the choice of builders and beneficiary households. Families paid back very little of the true costs of production of these units. As public housing production fell further and further behind demand and slum formation, government housing agencies turned to the less expensive option of upgrading slums, and site-and-services projects.

BRUCE FERGUSON

Dr. Bruce Ferguson specialises in affordable housing finance, value chain analysis for housing products and basic infrastructure. He has worked at the Inter-American Development Bank and the World Bank as a housing and urban economist. Dr. Ferguson started his career in mortgage banking revenue bond lending and affordable housing development in California. Bruce Ferguson has published more than 40 journal articles. He served as team leader for large housing finance projects in Mexico for five years.

The shift to enabling housing markets

These serious drawbacks, as well as the global shift to markets in the early 1980s, persuaded major donors and Latin American governments to abandon the direct production of public housing in favour of enabling housing markets. The seven main enabling instruments were outlined in a key World Bank document (Mayo and Angel, 1993). It recommended strengthening legal property rights, developing mortgage finance and rationalising housing subsidies. It also called for the provision of infrastructure for residential land development, the regulation of land and housing development, and better organisation of the building industry. Finally, it recommended the creation of a national institutional framework for managing the housing sector.

The enabling strategy has had an uneven impact. Most Latin American governments shifted from mortgages at below market rates to more transparent and quantifiable direct demand subsidies (DDS) for households. This finance method, consisting of three parts (ABC),[2] typically ▸▸▸

[1] Institutos de Vivienda in Spanish.
[2] In Spanish, these direct demand subsidies were often called ABC programmes, named after the Spanish initials for household savings (Ahorro), the subsidy (Bono) and a loan (Crédito).

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▸▸▸ gives households a substantial grant to which families must add a market-rate mortgage and their own down payment to purchase a new developer-built unit. The idea is that the purchasing family receives a voucher, which the household uses to choose a home from a wide variety of houses and units, rather than specific projects sponsored by builders or housing agencies. The success of DDS in Chile has influenced many other governments in the region to attempt this approach. The integrity and capacity of the Chilean bureaucracy and its fiscal commitment to the subsidy has made this administratively complex approach work. Most other Latin American governments, however, lacked these strengths and fiscal commitment. Many took the easy way out and allocated funds to projects sponsored by homebuilders and financial institutions, rather than to households, while adopting the three-part format of DDS programme. In short, the selected developers and mortgage lenders ended up with the ability not only to choose the location and type of homes but also the buyers who would get the finished homes. This supply-side decision making lies at the root of the problematic habitats created by government housing programmes attempting to go down-market in much of Latin America: standardised, miniscule units packed into sprawling developments on distant urban fringes or slums largely neglected by formal-sector institutions. Furthermore, this approach has allowed large homebuilding firms and the mortgage finance industry to benefit from substantial subsidies. It has mainly worked for the upper middle-class, spreading traditional mortgage finance to the elite worldwide. But it has performed poorly in reaching most households and funding most housing investment, contributing to bipolar habitats in much of Latin America.

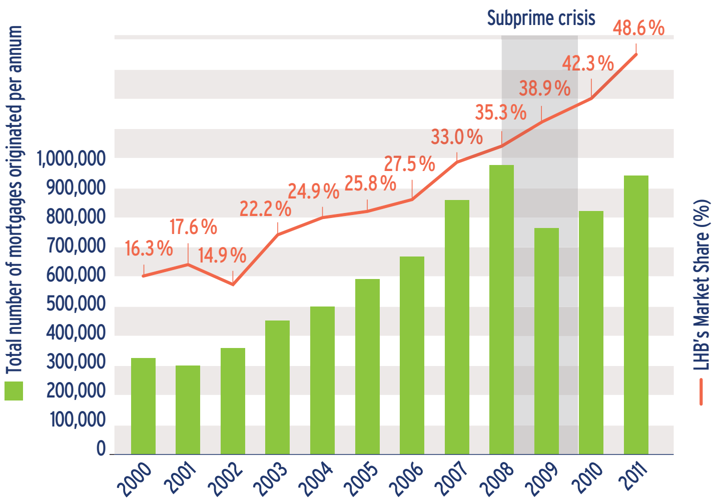
With few exceptions, subsidised developer-built housing in Latin America has been affordable to only the top 20–40% of the income pyramid in the form of new owner-occupied units (Ruprah, 2010). Institutionally, the enabling housing markets approach has created a boom in secondary housing finance liquidity facilities[3] to raise and lend money at market rates. Nevertheless, many provident housing funds and Institutes of Housing dating from the public housing era continue to exist, but have changed function or clientele, or shrunk in size and importance. Institutes of Housing often went bankrupt because a large share of their loans went uncollected, as households did not take repaying these public sector agencies seriously.

THE CASE OF MEXICO, 2000–2012

Mexico embraced the enabling housing markets approach at the start of the administration of President Fox in 2000, instituting an array of housing market reforms. In short order, the Mexican Federal Government created a National Housing Commission (CONAFOVI) to coordinate housing-sector efforts and a secondary-market housing finance liquidity facility, the Federal Mortgage Society (SHF). It began a thorough transformation of Mexico's ailing National Workers Housing Fund Institute (INFONAVIT),[4] which receives 5% of all private-sector formally-employed workers' salaries and provides them with a range of housing-related mortgage products – making it the largest public mortgage bank. An industry of 14 niche mortgage lenders, initially called SOFOLES, emerged to channel mortgage finance on market terms raised largely by SHF. Both INFONAVIT and SHF have increasingly adopted the three-part format of DDS but have retained supply-side decision making. These institutions and Mexico's top six com-

"Subsidised developer-built housing in Latin America has been affordable to only the top 20–40% of the income pyramid."

FIGURE: NUMBER OF MORTGAGES & LISTED HOME BUILDERS' (LHB) MARKET SHARE



Source: Mexican Housing Day, 2011

[3] *Second-tier housing finance involves funding, guaranteeing and packaging into securities mortgage loans originated by first- tier lenders directly to households.*
[4] *As of 2000, INFONAVIT had over a 40% arrears rate on its mortgage loans and failed to collect much of the salary tax mandated by national law from many formal-sector employees and employers.*

mercial developers (Consorcio ARA, Casas GEO, Consorcio Hogar, Homex, SARE, Urbi) ended up controlling Mexican federal housing. In contrast, Mexican households have had little choice but to accept the outcomes. To benefit from their INFONAVIT account and purchase a house, they had to accept the project conditions: the type of house, the location and a burdensome mortgage.

These measures underlay a dramatic increase in the number of mortgage loans from around 350,000 a year in 2000 to 700,000 a year at the end of President Fox's term in 2006, almost equaling the rate of new household formation, a rough proxy for demand in Mexico (Figure). The huge increase in mortgage credits for new developer-built units at first appeared a great success. But, aside from the 40% of Mexico's population that is excluded from INFONAVIT mortgages because it is informally employed, cracks soon appeared in this façade (Memoria, Congreso Nacional de Vivienda, 2013). More than two-thirds of mortgage credits went to fund Mexico's largest developers to build huge sub-divisions consisting of miniscule core expandable units on distant urban fringes, with 31 municipalities each having at least one new housing project of more than 25,000 new units.

"Many Mexican households – one in five – have left their properties either vacant or temporarily occupied."

First, this rapid development created low-density urban sprawl far from jobs and services. And for a variety of reasons, such as the high cost of transport, lack of basic services, or social isolation, many Mexican households – one in five – have left their properties either vacant or temporarily occupied. Developers for their part were left with swathes of housing units they could not sell. Secondly, land oligopolies have increasingly excluded the lowest earners and local government. Mexico's large developers started to stockpile land far in advance of use largely by taking advantage of the country's opaque *ejido* communal rural land-ownership system, which now includes roughly 50% of developable parcels on the fringe of major urban areas – dramatically reducing access to homeownership by bottom half effectively excluded from formal finance and development. Finally, although this new system of mortgage banking appeared to work well from 2000 to 2007, the financial crisis of 2008 resulted in escalating arrears rates and bankruptcy of many of the SOFOLES. Since 2007, Mexico has begun to recognize these drawbacks and shift from homebuilding on the fringe to urban densification, high-rise building and better regulation of the rental sector.

Shaping the market for the majority: the new housing entrepreneurship

A third paradigm is now emerging for habitat and urban development in much of Latin America (Ferguson *et al.*, 2014). Rising real household incomes have made affordable housing a huge new market opportunity for the private sector. The new urban lower-middle class currently numbers approximately 2 billion people and is projected to grow to 4.9 billion of a total world population of 8 billion by 2030. This group both demands and can afford a market-rate home, as can many low-income fami- ▸▸▸

BOX 1: AFFORDABLE HOUSING ENTREPRENEURSHIP, TWO MEXICAN EXAMPLES

Echale a tu Casa delivers sustainable community development through social housing production in Mexico. It organises communities of 100 households and provides training, machinery for eco-block brick production and technical supervision to middle-income families seeking to improve or purchase a house. Prices are far below the cost of contractor-built housing. A 44m^2 complete house costs USD 8,100 compared to USD 18,000 for a similar contractor-built unit. Eco-block construction also uses much less energy and generates less pollution than cement buildings. The federal housing agency, CONAVI, extends mortgage credit to *Echale* at 11% per year and *Echale* on-lends to households at 31% per year for 5–10 years. The national workers housing fund, INFONAVIT, plans to work with *Echale* to ramp up production.

Patrimonio Hoy (PH) is a programme of the huge Mexican cement maker Cemex to help low-income families build or expand their homes. It organizes groups of three families who commit to a 70-week saving programme. Following the *tanda* model – the Hispanic Latin American name for tontine, each group member takes his or her turn collecting payment. To ensure that savings get spent on construction materials, families receive raw materials rather than cash. PH advances microcredit in the form of building materials at an effective annual rate of 16% – far below microcredit and consumer credit rates in Mexico. Cemex hires local promoters – 98% of them women – to market the programme, screen potential clients, and resolve communication/payment problems. Over its first decade of operation from 2001 to 2011, PH helped 250,000 Mexican households to add bedrooms, saving these families an average of a third of total cost and finishing construction in a quarter of the time of unassisted incremental building. Cemex's PH operations have proved profitable, with earnings coming from a variety of sources beyond the sale of cement including a margin on other building materials, a membership fee and microcredit. Cemex has now expanded PH to a number of other Latin American countries. Other cement makers such as Lafarge and building materials manufacturers have taken notice of PH and are experimenting with similar initiatives in many other countries.

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▶▶▶ lies. The affordable housing market, however, consists of many distinct segments, reflecting the great variety of urban conditions, incomes, and life circumstances of the Base of the Pyramid. The public sector and the private sector must collaborate to create viable products for these many segments. Large modern corporations have started to view affordable housing in dynamic emerging economies as a business worth pursuing. Corporate building-materials manufacturers, retail chains and the new breed of affordable-housing developers offer the most powerful institutional platform with the greatest ability to reach mass markets. Modern management methods, particularly a value-chain approach, appear eminently well-suited to organising, streamlining and squeezing the costs of the incremental housing process used by most of the low-to-middle-income majority (Ferguson, 2008; Schmidt and Budinich, 2006). Mexico has some iconic examples of this new housing entrepreneurship (Box 1).

"Large modern corporations have started to view affordable housing in dynamic emerging economies as a business worth pursuing."

This first generation of initiatives for the base of the income pyramid provides key insights for expanding market-based affordable housing finance and development (Samaranayake *et al.*, 2011). They show that market-based affordable housing is a radically different business from traditional mortgage finance of developer-built new units. Seizing this opportunity requires careful market studies followed by the creation of pilot projects before expanding to scale. New companies should be created to carry out the process, as opposed to it being done by departments of existing companies, and conventional business models need to be avoided. Another lesson learnt is that stakeholders must work together to package the products and services suited to the diverse segments of the base of the income pyramid. Typically, the lead organization must partner with others to acquire missing pieces of the product package, including citizen-sector organisations to market the product, screen households and troubleshoot.

In this context, the single most important role of government is the provision of serviced urban land. A successful example of this can be seen in Thailand (Box 2). Local governments usually hold many of the key levers to the price and accessibility of urban land. Balancing the interests of peasant landowners on the fringe, urban householders, the homebuilding industry and government itself – by recouping the public investment in urbanisation – requires a strong multi-pronged urban land strategy that is currently missing in most of Latin America. The key to success is providing low-to-moderate-income households with the voice, the choice and the information necessary to shape their habitat. The way forward involves developing a public-private institutional infrastructure capable of producing the diverse housing solutions suited to the many submarkets of the base of the income pyramid. •

BOX 2: COMMUNITY-DRIVEN SLUM UPGRADING IN THAILAND

The government-funded Community Organizations Development Institute (CODI) organises slum communities, extends loans to groups of 100 households to purchase the land on which their shanties lie, create a rational road network, extend services and build housing. The CODI has upgraded the communities of 90,000 families in Thailand, who typically earn USD 333–666 per month – small vendors, taxi drivers, day labourers, etc. It assists cooperatives in negotiating the purchase of land from the private sector or long-term leases from public agencies. The cooperative then manages disbursal and repayments, pro-rating the community loan among individual families and overseeing the upgrading process. Housing plans must be approved by local authorities and must meet quality standards. The programme has led to the creation of networks of community organisations throughout Thailand and similar programmes exist in other East Asian countries. In comparison, slum upgrading in Latin America typically depends on the initiative of government agencies, resulting in high cost per household, low cost recovery and slum upgrading falling far behind slum formation.

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Involving third-party partners to finance the rehousing of Morocco's slum dwellers

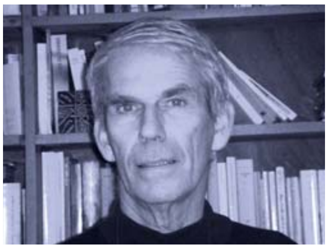
Morocco has implemented social housing construction programmes involving public- and private-sector partners. Alongside these projects, ad hoc initiatives of varying degrees of formality have also been taken up and supported by the authorities to respond to the housing deficit for low-income households. The 'third-party partner' mechanism is one such measure – enabling families from the slums to be rehoused free of charge in new, good-quality homes.

Olivier Toutain

Independent consultant

By 2030, two thirds of Morocco's population will be living in towns and cities, as compared with 59% today. This means that over the coming 20 years homes will need to be found for six million additional urban residents – the current housing deficit already stands at 840,000 units. The other major challenge will be to eliminate existing substandard housing. Estimates suggest that unregulated building, that is building constructed without either authorisation or access to urban amenities, accounts for more than one third of housing production. Moreover, despite the efforts of the public authorities, 8.2% of Morocco's population is still living in slums, particularly in Casablanca (UN-Habitat/MHU, 2012). Access to decent housing, guaranteed by Morocco's new constitution of 2011 is therefore one of the major challenges of the coming decades.

Since independence, the Moroccan state has pursued an active policy of improving access to housing. It first supported supply-side growth – in particular, by making public land available and bearing the costs of servicing that land with roads and amenities – and has encouraged demand by subsidising interest rates on housing loans. From the mid-1990s onwards, faced with a worsening housing deficit, the public authorities have focused on actively involving the private sector by means of financial and fiscal incentives designed to encourage private investment. It was in this context that the programmes for social housing priced at MAD 250,000 and MAD 140,000 came into being (Box). The partnerships set up under these programmes undoubtedly helped to re-energise the production of social housing, structure the private sector and facilitate the emergence of large Moroccan real-estate groups: Addoha, Chaabi and Alliance. At the same time a major drive to eliminate sub-standard housing got under way with the *Villes Sans Bidonvilles* (VSB – Cities Without Slums) programme. Launched in 2004 in the wake of the UN's Millennium Declaration and in response to the 2003 bombings,[1] this programme has the goal of eradicating all the slums, nearly 360,000 households, in 85 towns and urban centres in Morocco. To date, in-situ slum restructuring, rehousing in multi-dwelling units and resettlement – allocating serviced plots for development via assisted self-build housing schemes – have been the three modes of intervention preferred by Morocco's Ministry of Housing and the state operator, Al Omrane.[2] Alongside these operations, initiatives of varying degrees of formality have emerged to eliminate the slum districts and respond to the demand for housing. Recognised and regulated by the authorities and integrated within the official programmes, they represent genuine innovations that ▸▸▸



OLIVIER TOUTAIN

Olivier Toutain trained as an architect and started his career by taking part in several urban planning studies. He now works as an expert in urban issues and local development. In Morocco, where he has spent a large proportion of his career, he has also worked on the issues of informal settlements and slums. He recently directed a social impact study on the programme for eliminating Morocco's substandard housing and slums.

[1] *The attacks of 16 May 2003 were carried out by young suicide bombers from the Douar Thomas slum in Casablanca's eastern suburbs. They prompted a return to more stringent government regulation and the allocation of unprecedented levels of funding for eliminating Morocco's slums – perceived as the breeding ground for Islamism in the country.*

[2] *Al Omrane is a public organisation supervised by the Ministry of Housing and Urban Policy (Ministère de l'Habitat et de la Politique de la Ville). State-controlled but financially autonomous, it runs slum clearance, land-use planning and urban development projects. One of its key remits is implementing the VSB programme.*

Private sector crucial to resolve housing challenges

▶▶ might interest private-sector businesses, too. This is the case, in particular, with the 'third-party partner' (*tiers associé*) mechanism initiated in Casablanca as part of the VSB programme.

THIRD-PARTY PARTNERS: RECOGNITION OF AN AD HOC PRACTICE

The practice of involving third-party partners has developed in Casablanca, the Moroccan city most severely impacted by slums. In 2005, the country's economic capital had more than 500 slum districts housing nearly 500,000 people – 13% of the total population of Greater Casablanca. Resettlement projects were launched to remedy this situation, as part of the VSB programme, and are continuing today. Serviced plots– provided with roads and urban amenities – are developed on public or state-owned land to provide homes for slum dwellers who are assessed as priority cases. Slum households are allocated a serviced plot at a subsidised price[3] where they have to build their own home. The average cost to be borne by them ranges from EUR 10,000–15,000 – a sum they often find difficult to raise. However, the third-party partner model adopted by the local authorities and public operators in Casablanca has helped to release slum families from the burden of financing their new home. This arrangement offers two slum families sharing the same plot[4] the option of entering a contractual partnership with a third party ineligible for the VSB programme – a developer, investor, home-buyer, etc. The third party undertakes via this contract to guarantee the construction of a four-storey residential building and to supply a housing unit to each family as well as covering the cost of the land ordinarily payable by the slum dwellers – MAD 70,000 in total, equivalent to around EUR 6,200. In return, the third party is allocated the two remaining storeys – either for their own occupancy, for renting or selling – allowing them to benefit from heavily subsidised land costs.

"The third-party partner model [...] has helped to release slum families from the burden of financing their new home."

The third-party partnership principle was inspired by practices from the 1980s which involved allowing the recipient of a slum resettlement plot to team up with a third party to finance the construction of their home. This model was subsequently prohibited to prevent 'external' third parties from profiting from a public subsidy on the cost of the land. Yet the arrangement set up under the VSB programme recognises the value of a practice that is both long-standing and often informal – and provides a regulatory framework for its operation.

THE POSITIVE OUTCOMES OF THE THIRD-PARTY PARTNERSHIP SYSTEM

The third-party partnership system has been a resounding success – as evidenced by the fact that it has been adopted by the large majority of households benefiting from the VSB programme in Casablanca: just over two thirds of

[3] The plot costs just over one-fifth of the price of a serviced plot on the open market.

[4] The distinctive feature of the third-party partner intervention mode adopted by the public authorities is that two slum households are allocated a single plot – compared with one slum household per plot in traditional rehousing programmes.

BOX: THE 250,000 AND 140,000 DIRHAMS SOCIAL HOUSING PROGRAMME

The programme for social housing priced at MAD 250,000, around EUR 22,400, was launched by Morocco's Housing Ministry in 1999. Under this arrangement, the state grants complete exemption from taxes for real estate developers who undertake to build multi-unit housing at the agreed price. The housing units comprise a minimum of three rooms with a floor area of 50–100 m². Although no required income threshold is stipulated, beneficiary households must live or work in the city concerned and must not already be property owners; they also undertake not to resell their asset within a minimum of four years.

In order to meet demand from the lowest-income groups, this scheme was supplemented in 2008 by the low-cost housing programme priced at MAD 140,000, around EUR 12,500. Beneficiary households must not have monthly incomes of more than 1.5 times the guaranteed minimum wage. The housing units comprise a minimum of two rooms with a total floor area of 50–60 m². The real-estate developers benefit from the same fiscal advantages as for the homes priced at MAD 250,000 on condition that they complete a programme of at least 500 group-housing units in an urban environment.

The MAD 250,000 programme has undoubtedly boosted the production of social housing in Morocco. Yet this success is heavily dependent on the fiscal benefits granted by the state – and in a fragile economic environment it is anything but certain that these will be maintained. Moreover questions remain about the efficiency of the tax exemption mechanism and the urban integration of projects that are often located on the periphery of urban areas. The programme for MAD 140,000 homes has not proved as successful. The low involvement of private real-estate developers is explained by the difficulty of marketing these programmes – realised on public land often located on the distant urban periphery or in relatively undynamic satellite towns. New measures have been put in place to make the programme more attractive: raising the upper monthly income limit, making the conditions for marketing the properties more flexible, modifying restrictions on building height, etc. These mixed results clearly show how important it is that these projects represent profitable opportunities for the private developers – unless a minimum threshold is maintained they are unlikely to commit. Finally, buy-in for the schemes from their target populations cannot be secured unless a certain level of 'urban quality' is maintained, too – location, infrastructure, employment opportunities, etc.

the total for two of the main projects, Essalam Al Loghlam and Medinat Errahma. It has enabled these families to own their new homes free of charge. A social and economic impact study conducted by Al Omrane shows that these initiatives have provided them with access to decent housing and basic services (AFD, 2014).

The third-party contract arrangement also provides these households with guarantees regarding both the financing of the construction – which generally costs EUR 70,000 – and its realisation, in terms of both quality and timing: under the terms of the contract, the third-party partner is obliged to deliver the works in accordance with a detailed schedule covering structural works, finishing, connection to the water and power supply, sanitation and fittings. The partner also has to complete construction within a maximum of six months and undertakes to meet temporary rental costs for the families concerned in the case of any delay.

The other key indicator that this arrangement is working is a resale rate significantly lower than the average observed in standard resettlement operations. The 'slippage' effect that arises when plots are resold by recipient households prior to construction – whether for financial, personal or other reasons such as family disputes, refusal to live in the new accommodation, etc. – is one of the primary hazards of slum clearance programmes.

Success factors

According to Al Omrane's investigation, housing finance seems to be one of the key difficulties for the families targeted by the VSB programme, in particular those at the lowest income levels or in socially precarious situations. According to the Al Omrane survey, 20% of beneficiaries have no financial resources and 36% of the working-age beneficiaries are unemployed. The key benefit of the third-party arrangement, therefore, is that it frees slum households from having to meet construction costs. The attractiveness of the benefits offered to private investors is also a key factor in this mechanism's success. Granting two of the four homes built to the third-party partner is a clear incentive to investment. The one-to-five differential between the purchase price of the serviced plot and its market value[5] – in the context of high demand for real estate in the Casablancan market – undoubtedly encourages third-party investors to take part. The substantial rental market for this kind of real-estate product offers attractive profitability to the third-party partner. Creating homes for rental in this way also helps to meet the demand from families, many of them from the middle class, who cannot afford to buy their own home.

The third-party partnership model also supports the government's objective of urban densification, in a context of diminishing land availability. This experiment is based on the construction of four-storey residential blocks – buildings of one or two storeys higher than those in previous projects. This key feature also makes it possible to house more families, increasing the profitability and the attraction of the scheme for the third-party investor. This attractiveness could well encourage the emergence of more structured private interventions originated by professional stakeholders, property developers or other institutional investors. To date, the third-party partners have still mainly been individuals rather than organisations – often people related or closely connected to the families involved. Nonetheless the impact study highlighted the purchase of 40 plots by a Moroccan citizen resident in Italy – which could be the start of a more organised, large-scale response.

"The one-to-five differential between the purchase price of the serviced plot and its market value [...] undoubtedly encourages third-party investors to take part."

The practice of financing construction by involving a third-party partner has now extended across the entire VSB programme in Casablanca. It highlights the benefit of these initiatives, which echo the principle of the 'additional development rights' introduced in various cities worldwide – notably in Mumbai, India, where investors are granted additional surface areas in exchange for financing housing within slum-eradication programmes. The Moroccan experience of the third-party partner mechanism clearly represents a useful experience for other cities in developing countries – especially in Sub-Saharan Africa. Its replicability will depend on the terms of the public-private partnership involved. Public incentives for access to land, a regulatory framework for the scheme, dynamic local real-estate markets and endorsement by local people will be the key conditions driving the success of such initiatives. •

[5] *The purchase price granted to the beneficiary by Al Omrane is EUR 147 per square metre; the market price for a roughly equivalent serviced plot is around EUR 730 per square metre.*

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Lessons learned from this issue

BY FANETTE BARDIN, EDITOR IN CHIEF

Housing has become one of the central development issues for emerging and developing countries as a result of population growth and fast-expanding cities. In many countries, access to property remains the privilege of an elite while the number of people living in sub-standard housing is rising by 25 million each year. Informal settlements – the corollary of unbridled urbanisation – continue to proliferate on the outskirts of cities. Between 2000 and 2012, the number of people living in slums increased from 767 to 863 million. It is estimated that to meet population needs, some 565 million new homes need to be built by 2030 in addition to the current gap of more than 400 million units. This implies producing affordable housing quickly and on a massive scale, while developing a proper urban planning policy.

With demand far outstripping public resources, governments must adopt a new approach. They need to work with the private sector and turn towards market solutions to encourage the sustainable building of affordable housing. But the private sector has shown little inclination to invest massively in this market. Private developers are often deterred by the difficulties in acquiring land, the legal uncertainties surrounding transactions and the limited access to funding. Added to this are regulatory obstacles, sluggish procedures, a lack of qualified labour and higher raw material costs, all of which impact on building timetables and construction costs, and ultimately on the price of homes. Furthermore, the low penetration of mortgage lending in developing countries substantially reduces the possibility of relying on a solvent demand to support the market.

It is therefore essential that states create an enabling environment for private initiative. It is not a question of governments supporting the private sector through extensive subsidies alone, but rather of focusing their efforts on safeguarding operations and introducing targeted incentives. Intervention across the entire industry to promote a structured, autonomous and sustainable sector will be a decisive success factor. This means improving land tenure regulation as well as providing land for development with essential infrastructures (transport, power, social services, and so on). Banking institutions must also be encouraged to meet the financing needs of developers and households, by facilitating access to long-term financial resources at affordable rates or placing risk-sharing mechanisms at their disposal, for example.

In the face of the housing challenge, governments must take on a coordinating role and support the private sector so that socially, environmentally and culturally sustainable solutions can be developed, for they are the guarantors of quality urban planning. Their action is also crucial to ensure housing needs are fully taken into account and that housing initiatives benefit the most disadvantaged sections of the population. Failed experiments, such as the ghost towns of Mexico or Angola, have shown the limitations of private industrial large-scale projects designed with no planning and with the sole aim of amortizing production costs.

The magnitude of needs also requires breaking the mould and using new models. Few governments, for example, have paid real attention to the housing rental sector, even though it is a potential solution to housing low-income sections of the population. In addition to supporting formal housing, the authorities should also explore informal solutions created by those sections of the population themselves. Recognised and supervised by the public authorities, they represent genuine innovations which could very well be developed on a larger scale by the private sector. Self-build housing, which is now beginning to interest major industrial groups, is a perfect example. Another promising avenue is the emergence of a new generation of developers who have come up with low-cost solutions tailored to the needs of populations at the bottom of the pyramid.

Access to housing is not only a moral imperative. It is also a driver of economic growth and employment, and a vector for development. Providing decent housing for all requires the unprecedented buy-in of all stakeholders, both traditional and new.

In our next issue

Unlocking the potential of the private sector to improve education

Issue coordinated by Jean-Nicolas Beasse, Adeline Lemaire (PROPARCO) and Isadora Bigourdan (AFD)
To comment on the articles, go to our blog at : http://blog-private-sector-and-development.com

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