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Finance for incremental housing; current status and prospects for expansion

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A B S T R A C T

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Appropriate finance can greatly increase the speed and lower the cost of incremental housing – the process used by much of the low/moderate-income majority of most developing countries to acquire shelter. Informal finance continues to dominate the funding of incremental housing. However, new sources have developed including housing microfinance, community-based finance savings and loan groups, and consumer credit for building materials. This paper examines informal and formal finance for incremental housing and makes recommendations for the vast expansion necessary to meet the affordable housing demand from the huge urban wave in developing countries projected over the next three decades.

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Introduction

Access to institutional housing finance has largely failed to improve habitat for low-income groups since neo-liberalism has spread around the globe. Table 1 shows mortgage finance as share of GDP for selected countries around the world. The very low penetration of mortgage finance in most developing countries stands out. Traditional mortgage finance is virtually irrelevant to the majority of households in developing countries for many reasons (Ferguson, 1999; Smets, 1997). Even in developed countries, institutional housing finance is in crisis.

In the USA, sub-prime lending increased when lenders started serving clients with low or fluctuating incomes and/or poor or thin credit records. About 10 years ago sub-prime lending was almost absent, but had reached a level of 20% of all mortgages in the USA by 2008. These sub-prime home lenders primarily focused on profiting from the upfront fees rather than sound underwriting. In a radical shift from historical precedent, many US home lenders offered mortgages with negative amortization, no down payment (sometimes, lending more than the appraised value of the house), sharp increases in introductory interest rates based on volatile indices, and no or little documentation from the borrower, believing that housing prices would always rise to cover their risk. A steep rise in securitization of US home mortgages spread the risks of these sub-prime loans around the globe by allowing other

financial institutions to purchase this paper. Rapidly growing problems with this sub-prime mortgage portfolio provoked a global credit crunch and economic crisis in 2008 that continues today.

However, most community banks in the US, other developed countries, and in developing countries that maintained appropriate underwriting practices have continued to perform reasonably, even when lending to lower-income groups. To put it another way, lending to the low/moderate-income majority need not harm the stability of financial markets, and can contribute in helping to strengthen economies through encouraging savings and developing good lending practices (Mitlin, 2008:3–4; UN-Habitat, 2005). Such affordable home lending practices can make a crucial contribution to improving world habitat. The needs and possibilities of slum dwellers, who build their house incrementally, illustrate this potential. Some classic studies have looked into the building strategies of slum dwellers. From the 1960s onwards many authors (e.g. Abrams, 1966; Payne, 2002; Smets, 1999, 2004, 2006b; Turner, 1972, 1976) analysed incremental building in slum areas and stressed its importance. Incremental building fits the livelihood strategies and conditions of the poor.

As families grow and as resources permit, low/moderate-income households build their homes step-by-step. Resources dedicated to incremental housing have to compete with other needs of the household. Not surprisingly, the incremental home-building process can take low/moderate-income families decades – a median of 16 years to complete a home in one study conducted in Mexico by CEMEX (Pralhalad, 2005). Incremental building accounts for 50–90% of residential development in most developing-country cities.

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Table 1
Mortgage finance as a share of GDP.

Country	Mortgage finance as a share of GDP
Argentina (2001)	4%
Brazil	2%
Bolivia (2001)	8.6%
Chile (2001)	10.8%
Columbia (2001)	7.0%
Indonesia (2007)	3%
Malaysia (2007)	25%
Mexico	2%
Panama (2002)	24.4%
Peru (2001)	2.9%
Uruguay (2001)	7.0%
United States	79.6%
European Union	42.6%

Sources: Galindo and Lora (2005); Unitus/Lehman Brothers (2007).

Although Turner and Abrams focus on 'informal' building, they neglect institutional arrangements concerning housing finance that can vastly increase the speed and efficiency of the process. Such institutional arrangements – which are often informal – play an important role in practice (cf. Pamuk, 2000). Housing and cities are built the way they are financed. Hence, the institutional arrangements for low/moderate-income housing finance matter greatly.

This article assesses the status and the prospects for the finance of incremental homebuilding, including informal housing finance, housing microfinance, community-based housing finance, and consumer credit for purchase of building materials. Low/moderate-income residential development requires a broad spectrum of credit methods suited to many types of housing and income levels. This article concludes by suggesting approaches to fill the gaps and improve these current practices in order to reach the massive scale necessary to house the 2.6 billion new urban residents for 2050 projected for developing-country cities (Cohen, 2005).

Informal housing finance

Informal housing finance encompasses individual and group savings, windfalls, fabrication of their own building materials by households, sweat equity, small loans from neighbours, moneylenders or pawnbrokers, barter arrangements and community self-help, and remittances from family living abroad (Baken & Smets, 1999; Ferguson, 1999: 189; Smets, 2004). Many studies suggest that low/moderate-income households join a wide variety of sources to build their homes.

Sheuya (2007) describes how different sources of finance are used for several stages of the building processes in 'informal' settlements in Dar es Salaam. In the initial stages of house construction, these families use their own savings. In the later stages, however, households tended to replace their own savings with a mix of other funding sources, including credit (p. 454). In Latin America, Stein and Castillo (2005) have found that 'informal' sources of finance encompass savings, loans from relatives and friends, remittances from family members and the sale of assets.

Smets (2004) has questioned 192 slum dwellers in Hyderabad, India. This study shows that many dwellers complete one stage of the homebuilding process and then wait for the opportunity to move on to the next stage of their construction process. As housing expenditures must compete with other needs of the household, the periods in between the steps can vary considerably. The example below from Hyderabad, India, illustrates such incremental building in four steps spread over a period of 23 years.

Lingam – a clerk at a local hospital – and Kamlana – a babysitter – built a hut (step 1) on a lot that they had acquired in an illegal

Table 2
Number of sources of housing finance used by interviewed slum dweller households in Hyderabad, India.

Financial sources	Incremental building					
	Step 1		Step 2		Step 3–5	
	Abs.	%	Abs.	%	Abs.	%
1 source	101	53	46	65	16	59
2 sources	58	30	18	25	10	37
3 sources	29	15	7	10	1	4
4 and more sources	4	2	0	0	0	0
Total	192	100	71	100	27	100

Source: (Smets, 2004: 86) ($N = 192$, missing cases 39; $V = 0.11$; $\chi^2_{(6)} = 7.60$ $p > 0.05$).

subdivision. When their fifth child was born, they added an additional room (step 2). Once the eldest child reached 10 years of age, they started the construction of a new house with two rooms and asbestos sheets on the roof (step 3). They funded this new construction through a lump sum obtained from a financial self-help group in which they participated and credit from a friend. Once they moved into the newly constructed home, they rented the hut in order to repay their friend's loan. Three years later, the couple added a room constructed and replaced the asbestos sheets with a new a concrete roof (step 4). These final improvements (step 5) were also funded by a loan from a friend and a lump sum from the same financial self-help group.

In this study of Hyderabad, the majority of the dweller households use only one source of savings or credit for each step in the building process (see Table 2). The main single sources of funding are savings, friends, relatives and neighbours, financial self-help organisations (*chit funds*), moneylenders and pawnbrokers. The other sources mentioned in Table 3 are each only used by fewer than 10% of the interviewed dweller households.

By comparing the single financial sources used for the different steps in the construction process, the Hyderabad case suggests that the use of personal savings gains in importance in the later stages of the building process. These later stages of the building process appear less urgently and can therefore be saved more easily.

The use of *chit funds*, in which savings as well as credit provision can be combined, declines from the second step onwards. The sample for steps three to five is too small to draw any firm conclusions. The use of credit derived from friends, relatives and neighbours for step one declines enormously for steps two to five. Relatives and neighbours arguably feel more obliged to provide a loan for the first step of the building process, since it is more urgent than in later steps. The popularity of moneylenders and pawnbrokers for the second step of the building processes is

Table 3
Sources of housing finance used as single source by interviewed slum dweller households in Hyderabad, India.

Financial sources	incremental building					
	Step 1		Step 2		Step 3–5	
	Abs.	%	Abs.	%	Abs.	%
Savings	26	26	20	43	12	75
Friends, relatives and neighbours	27	27	5	11	2	13
Chit fund	21	21	5	11	1	6
Moneylender, pawnbroker	12	12	11	24	0	0
Employer	7	7	3	7	1	6
Retirement benefit, life insurance	5	5	0	0	0	0
Finance corporation	2	2	2	4	0	0
Gift, dowry	1	1	0	0	0	0
Total	101	100	46	100	16	100

Source: Smets (2004: 87) ($N = 192$, missing cases 39).

notable, which may indicate that these lenders look to secure the loan by keeping an eye on the borrower, whose behaviour can more easily be monitored if he/she has a fixed residence.

Interestingly, dwellers use credit from colleagues, a credit co-operative, a customer or a bank only in combination with other funding sources. A minority of those interviewed joined more than one source to fund each step. Virtually all of this credit comes from non-institutional loans. Informal credit may encompass more than finance only, and form part of balanced reciprocal relations among friends, relatives, neighbours and colleagues. Mutual trust maintains the relationship. In comparison, institutional lenders and borrowers have to earn others' trust, which has to be proved continuously. Bank loans are rather exceptional. In the single case observed, a close relative employed at a local bank office was able to arrange the bank loan (see Table 4).

Classifying 'informal' lenders is difficult, because they are so heterogeneous. However, a continuum from purely commercial relations to purely social relations appears to characterize these practices. A preliminary classification of 'Informal' credit providers includes personal lenders, commercial lenders and financial self-help organisations (Table 5).

Personal lenders encompass friends, neighbours, relatives, colleagues and employers. Flexible arrangements between lender and borrower characterize these personal loans. Moneylenders and pawnbrokers can be classified as commercial lenders as they offer credit on a strictly business basis. Financial self-help organisations in India organise groups with a monetary purpose. These most common organisations are also known as ROSCAs (Rotating Savings and Credit Associations), and ASCAs or ASCRAs (Accumulating Savings and Credit Associations). ROSCA participants make regular contributions to a fund that is given, in whole or in part, to each member in turn until every participant has had their turn. Then, the cycle finishes and may start again. In an ASCA, participants pool savings in a fund that will be used for providing loans. At the end of a cycle all money including interest repaid to the fund are shared among its participants. In this instance, all participants will receive their savings and a share in the profits made.

Housing microfinance

Since the late 1990s, housing microfinance has increased dramatically. Up to the late 1990s, Micro Finance Institutions (MFIs)

Table 4

Sources of housing finance used for incremental building by interviewed slum dweller households in Hyderabad, India.

	Used alone or in combination with other financial sources				Total
	Only source	+1 source	+2 sources	+3 or more sources	
Savings	58	56	20	4	138
Friends, relatives and neighbours	34	29	23	4	90
Moneylender, pawnbroker	23	29	23	5	80
Chit fund	27	28	19	3	77
Employer	11	13	9	2	35
Retirement benefit, life insurance	5	3	1	0	9
Colleagues	0	5	3	0	8
Finance corporation	4	1	1	0	6
Credit co-operative	0	3	2	0	5
Gift, dowry	1	0	0	0	1
Customer	0	1	0	0	1
Bank loan	0	0	1	0	1
Other ^a	0	4	9	0	13

^a Other includes unidentified financial sources, but the number of financial sources was mentioned by the interviewed slum dwellers.

Source: Smets (2004: 88) (N = 192, missing cases 39).

made loans almost exclusively for micro-enterprise. Housing finance, however, (Mitlin, 2008: 5), is not always an easy endeavour for MFIs (see e.g. Smets, 2006b).

Two recent studies with comprehensive empirical data give insight into the current status of housing within the microfinance community. Both focus on Latin America, the region where this practice has advanced the most. First, *Accion* (as presented in Mesarina & Stickney, 2006 and Merrill & Mesarina, 2006) surveyed 10 of its regional affiliates in Latin America. The second study was done by the *Micro Service Consult GmbH* (GmbH, 2005), commissioned by Housing Microfinance Ltd,² a financial group planning to issue securities to finance low/moderate-income housing in order to assess market demand from MFIs for funding. The GmbH study surveyed 25 of the top microfinance institutions in Latin America on their housing credit products and plans. Although conducted independently for different purposes, these two studies arrive at highly-similar conclusions. For an overview of both studies see Boxes 1 and 2. Both studies show trends which are also confirmed by other studies of housing microfinance within MFIs by Habitat for Humanity International (Stickney, 2006) and the Cooperative Housing Foundation (Schumann, 2006).

Although housing microfinance is useful to build customer loyalty, it is a secondary adjunct product for MFIs that many extend only as a reward to their existing micro-enterprise client base and do not actively market. The core product is micro-enterprise lending, what MFIs view as fostering economic development directly. Moreover, the expansion of the housing microfinance portfolio is hindered by a lack of appropriate funding, institutional know-how, and operational problems.

Despite stumbling blocks in the expansion of the housing microfinance portfolio, housing microfinance has become 'hot' largely for two reasons. First, housing microfinance has the potential to serve many low- and moderate-income households. These families neither want nor can afford a large long-term traditional mortgage to purchase a developer-built complete unit. Instead, these households build progressively, by acquiring and upgrading title to a lot, building a makeshift shelter, replacing this makeshift shelter with permanent materials and expanding it, and lobbying government for services (Ferguson, 2003; Greene & Rojas, 2008). A series of small short-term loans can fund the steps in this progressive housing process with payments affordable to households. Small, serial loans can greatly increase the speed and lower the high cost (Ferguson & Navarette, 2003) of the incremental housing process.

The prototypical housing microfinance loan consists of a small, short-term unsecured credit (US \$500–2000) with a term of two to five years, depending upon context to a homeowner to expand or remodel their informally-built house. Sometimes, micro finance institutions (MFIs) offer somewhat larger loans (US \$3000–7000) at longer terms (5–15 years) for a family to construct a new home (often on a lot that they already own), occasionally secured by a mortgage. Small home improvement credit, however, is the main market for which microfinance institutions have created a housing microfinance product. However, small credits could also finance a wide range of other housing investments useful to low and moderate-income households. These include lot purchase, title regularization, construction of a floor/joist/roof structure that the homeowner builds out, adding rental units onto the homeowner's property through horizontal or vertical expansion, individual and communal infrastructure, the vertical or horizontal build out of a developer-built core unit or humid core (a bathroom/kitchen area containing plumbing and electricity) in pre-programmed steps.

² An author of this article, Bruce Ferguson, is a manager of this enterprise.

Table 5
'Informal' credit characteristics concerning shelter construction in Hyderabad, India.

	Accessibility	Collateral	Purpose loan	Loan amount	Term	Repayment schedule
Friends, neighbours and relatives	Relatively accessible	Social	Open, but monitored	Rs. 50–30,000	3 months – 11 years or open	Often flexible
Moneylenders and pawnbrokers	Relatively accessible	Mainly social but for pawnbrokers conventional	Open	Rs. 200–30,000	½–4 years	Flexible
Employers	Restricted access	Employment	Open, but often monitored	Up to Rs. 20,000	1–6 years	Often fixed
Colleagues	Restricted access	Employment	Open, but often monitored	Rs. 500– 10,000	Open, but exact term is n.a.	Flexible
Financial self-help organisations	Restricted access	Social	Open	variable	Max. 1.5–2 years, often shorter	Fixed, if flexible penalties are charged
Credit co-operatives	Not very accessible	Social and conventional	Open	Rs. 5000–42,000	26–80 months	Fixed

Source: Smets (2004: 106).

These investments could also be used for the completion (e.g. adding fixtures, cabinets, electrical equipment, additional plumbing, and painting) of an unfinished condominium shell in a high-rise building. Although small home improvement loans have become virtually synonymous with housing microfinance, other possible applications of housing microcredit will be considered in this article when strategizing how to expand housing microfinance to a relevant scale.

Social support programs joined with GDP growth have stimulated a rapid increase in household income of families in the bottom half of the income pyramid in many developing countries over the last decade. The potential market for small home improvement loans remains huge and, often, relatively uncontested; 50–80% of the population in most developing countries build their homes progressively. Market studies typically show that one-quarter of these families want and can afford a small home improvement credit at any one time. The demand for somewhat larger loans – US \$2500–\$10,000 – to the rapidly growing lower middle class of dynamic developing countries also remains largely unserved. Although each individual project is small to modest in size, the huge numbers result in an impressive total market potentially financed by such credit: US \$331.8 billion worldwide (Hammond, Kramer, Katz, Tran, & Walker, 2008). Affordable housing finance markets will grow exponentially as 90% of the net increase in world population of 4 billion people by 2050 is projected to reside in the urban areas of developing countries.

Traditional mortgage finance institutions have typically lacked the low-cost community-based systems necessary to lend to both of these markets. Hence, microfinance institutions have frequently faced little institutional competition in extending housing microcredit for home improvement and larger credits for purchase of a basic unit or major rehabilitation to these families.

A second reason that housing microfinance has become a developmental 'hit' involves its fit with the microfinance industry. Small home improvement credit offers a useful product that microfinance institutions can add to their core business; micro-enterprise lending. MFIs can successfully apply their existing loan methods and installations for micro-enterprise loans to small home improvement loans with little or no modification. Roughly 20% of funds nominally borrowed for micro-enterprise go to housing improvement in the absence of an explicit housing product.

Housing microfinance also fits well with the transformation of many MFIs from NGOs into financial institutions that are regulated because they take deposits from the public. The ability to take deposits could vastly increase and reduce the costs of MFI funding, which otherwise comes typically from other financial institutions or donors. The aspiration to own or build a house has historically

Box 1. Accion study on the current status of housing within microfinance community.

From 2002 to 2005, the housing microfinance portfolio of the ten Latin American Accion affiliates surveyed grew from US \$38 to 117 million, and home improvement lending increased from US \$20 to 74 million. Interestingly, almost as many of these Accion affiliates offered home purchase loans (70%) as home improvement loans (80%), indicating that MFIs are seeking to serve moderate-income households that buy or construct a new unit as well as low-income households that upgrade a lower-cost housing solution.

The housing microfinance portfolio grew from 12% of the total portfolio of these 10 microfinance institutions to 19%, but still represented only 9% of the total network portfolio of Accion. Repayment rates on the housing-microfinance portfolio of the surveyed MFIs were superior to that on micro-enterprise lending. This datum bears out the impression of many microfinance lenders that households prioritize repayment of housing credit over micro-enterprise credit.

These 10 MFIs surveyed by Accion stated that demand for housing microfinance is immense. Most of these MFIs do not market this product, although some competition is beginning to emerge from building materials suppliers and finance companies. This finding is in accordance with the conclusion of a market study conducted in three Mexican cities (Capital Advisers, 1998) that border the US that the effective demand for housing micro finance totalled four times that for micro-enterprise finance in this same geographic area. 15% of Mexican households surveyed by this study both wanted and could afford a small loan at market rates with short-terms for home improvement. The general sense of MFIs is that roughly half the households of Latin American countries are interested in improving or adding to their homes, although only about a third of this half of the population can afford market-rate finance in a given moment.

The Accion study concluded that housing microfinance has proved useful to build customer loyalty, but is not a core product of these ten MFIs. The core mission of these MFIs continues to be fostering economic development through micro-business lending. In general, these MFIs do not view housing as an integral part of their core mission.

Box 2. GmbH study on the current status of housing within microfinance community.

The GmbH study showed that 17 of the total 25 MFIs surveyed had products for low-income housing, while the remaining eight were seriously considering developing such a product in the short run. These institutions had extended a total US \$84.2 million for housing loans. Overall, housing loans represented 8.8% of the total micro loan portfolio of these MFIs. Housing credit accounted for over 15% of the portfolio in only three of these MFIs. Despite this small share, many of these MFIs valued housing credit because it fits well within their overall business strategy. Housing microfinance helps to diversify their portfolio, and meets the housing credit need of their existing client base of micro-entrepreneurs.

All 17 MFIs with a housing product surveyed by the GmbH study make loans for home improvement, but only 9 offered finance for purchase or construction of new homes. Maximum maturities lie between 10 and 20 years for MFIs offering new home loans and between two and five years for MFIs offering home improvement loans. The average loan amount was US \$1925. Almost all institutions funded their housing loans at least partly from their own equity. Eleven of these 17 institutions used credit lines mainly from national public banks and international development banks for refinancing their housing portfolio.

The institutions surveyed by the GmbH study were interested in roughly doubling their housing credit volume over the next three years, although their core mission continued to be micro-enterprise credit. This expansion would raise their housing loan volumes from 8 to 10% of their total loan portfolio to 15–20%; a significant increase but hardly a dramatic one relative to the immense demand for this product.

These MFIs surveyed by GmbH said the 'lack of availability of appropriate funding' was the most important constraint for the expansion of their housing portfolio. However, donors, investment banks, and others have flooded the microfinance industry with liquidity. Hence, such 'lack of funding' statements may sometimes indicate other problems (such as high costs and inefficient operation that make funding at competitive rates unprofitable for these MFIs) and, therefore, deserve analysis on a case-by-case basis. These MFIs cited lack of institutional capacity and technical know-how as the second most important problem in limiting the expansion of their home lending. Given the multiplicity of sins that 'lack of appropriate funding' often indicates, technical assistance to remedy institutional and operational problems appears to be as important as simply more or better funding.

proved the main motivation for families to save in developed countries (normally in banks) as well as developing countries (where savings groups and housing cooperatives serve the same purpose). Hence, adding a home improvement credit as well as savings products makes sense for MFIs seeking to take deposits – the least expensive type of funding – and become regulated financial institutions.

Small serial credits largely for building materials to improve a homeowner unit, which has come to be called 'housing micro-finance', began expanding a decade ago mainly because of these synergies with the microfinance industry. By this time, roughly 200 microfinance institutions worldwide had become commercially viable (Robinson, 2001). Increasing competition had slowed

growth opportunities available to MFIs in some markets (e.g. Bolivia, Bangladesh). Major figures, such as Hillary Clinton, lauded the achievements of the *microfinance revolution* publicized widely at this time (Robinson, 2001) and the concept of housing micro-finance enjoyed legitimacy by association.

In addition, a series of events, papers, and books (Daphnis & Ferguson, 2004, 2006) on housing microfinance during this period disseminated awareness of housing micro finance throughout the international housing community and microfinance networks, and brought these two audiences into communication for the first time.

Several studies (Merill & Mesarina, 2006; Mesarina & Stickney, 2006; Schumann, 2006; Stickney, 2006) show rapid growth of housing microloan volume within MFIs, although from a small base. MFIs have discovered that housing microfinance is profitable and has immense potential for expansion. Thus, housing microfinance – particularly small home improvement loans – is now well-established as a recognized niche product for MFIs. From the perspective of many MFIs, their housing product is on track to fulfil its institutional missions: to diversify risk, to support development of savings products and the transition to a regulated deposit-taking financial institution, and to offer an additional product popular with their core micro-entrepreneur clients.

The 'lack of funding', which MFIs cite as the main bottleneck to expand housing microfinance, is also on its way to solution. For example, Mexico's second-tier housing development bank, the *Sociedad Hipotecaria Federal* (SHF), which previously offered liquidity only for mortgage loans mainly for middle-income home purchase, has had a housing microfinance window since 2005 and now offers a subsidy that can be joined with a small housing loan. Many Latin American countries join market-rate credit with subsidies (in the form of vouchers) and downpayments of households in affordable housing programs. Such "direct-demand subsidy programs" started with Chile (which has served as a model for other countries), and have spread widely to Costa Rica, Mexico, Ecuador (see Klaufus, in this issue), Jamaica, Brazil, El Salvador, Columbia, and elsewhere. These "ABC" programs (named after the Spanish terms for their financial components: *ahorro* – household savings, *bono* – direct-demand subsidy, *credito* – credit) typically work well for the middle class and, sometimes, moderate-income households, but have had difficulties reaching low-income households (Ferguson, Rubinstein & Vial, 1996). The government of Colombia has tried to start a secondary market for housing microfinance. Investment groups and capital market institutions are establishing financial vehicles to fund home credit of MFIs. Magowan (2008) describes the considerable progress in issuing securities on public markets for on-lending to MFIs to finance low/moderate-income housing in developing countries. These major achievements deserve recognition and further support in order to consolidate them.

However, three interrelated factors seriously limit expansion of housing microfinance within MFIs.

First, an explicit housing product typically has a slightly lower interest rate and longer tenor, and can cannibalize their existing micro-enterprise loan business. That is, the MFI's micro-entrepreneur clients could nominally borrow for housing to fund their business and get better terms than they would under a micro-enterprise credit. The reverse pattern – using MFI business loans for housing – has long occurred. For example Athmer and de Vletter (2006: 53) report:

'Interview results from Novobanco and Tchuma indicate that 20–30% of the clients applied their credits at least partly for housing construction and/or purchase of durable goods. The (...) analysis showed that among the 2 lower categories a minority of clients applied their loan exclusively for business purposes.'

Thus, the development of an explicit housing product might mainly lower profits, unless marketed to a new clientele or unless the MFI monitors the use of the funds for housing.

Second, the Accion and GmbH studies confirm that MFIs consider housing an adjunct secondary product. From the perspective of most MFIs, housing credit deserves little attention and is unrelated to their core mission of 'promoting economic development.' Many studies as well as common experience show that most households build wealth mainly through homeownership and housing investment plays a crucial role in national economies. Nevertheless, microfinance institutions continue to relegate housing to a trivial role in their business strategy aimed, supposedly, at 'economic development.' With a few notable exceptions, MFIs lack the interest to make housing a major focus.

Third, microfinance organizations offer far too small an institutional base in many countries for the expansion of housing microfinance to a scale relevant to demand, even if MFIs were interested in this role. Even after 25 years of development, the MFI industry consists of less than 300 commercially-viable institutions, serves only a fraction of the market for micro-enterprise loans in most countries, and offers housing microcredit in minuscule volumes relative to demand.

Community-based housing finance

Typically, individual loans to families best finance house construction. However, many aspects of incremental residential development – from acquisition of a land parcel for subdivision to provision of communal infrastructure and services – frequently involve many households in a common enterprise. In advanced industrialized countries, the cost of these communal components of housing usually get charged to the developer ('impact fees'), who passes on these costs more or less into the purchase price of the house. A substantial literature (e.g. Lowry & Ferguson, 1992) has developed that analyzes the distribution of the ultimate costs and benefits of these charges to households, developers, landowners, and government. In principle, local governments attempt to recoup the cost of these communal services from others, but may end up paying a portion that they then finance through taxes and user fees.

In developing countries, however, most low/moderate-income households must find some way to acquire these communal residential development infrastructure and services as the institutional and financial arrangements of developed countries are largely absent. Government upgrading programs typically subsidize a portion of the cost of basic services in well-established low-income neighbourhoods but lack sufficient funding to cover much of the need.

Community-based housing finance groups can help resolve this problem. These groups form not only to fund individual house construction but also to purchase land parcels and acquire communal infrastructure (roads, drainage, water distribution and connection etc.) Acquiring these communal components of residential development typically involves negotiations with other stakeholders involved – such as the original landowners of the parcel and government.

Community-based housing finance groups typically organize households to save and/or borrow sums necessary for the development, construction, and maintenance of the resulting housing. Such community funds encourage community empowerment, land acquisition or security of tenure, infrastructure development and obtaining or improving shelter (Nilsson, 2008).

Governments often support community-based housing finance in some form. In the Philippines, the Community Mortgage Programme (CMP) offers groups of 'informal' settlers a mortgage for an undivided track of land. Such land can be obtained initially by

occupation with or without permission of the owner, but the private or public owner must agree to sell their land as part of the program. Once land is acquired, this program provides loans for site development and housing. For projects without a defined site, it is hard to organize heterogeneous groups. Even projects with a defined site sometimes face problems with group size, cohesion and mutual cooperation. A weak monitoring system in combination with corruption and poor enforcement of internal rules resulting in low repayment rates and high arrears complicate the operation of this program. One of the lessons derived from the experiences with CMP is that group-based loans with a short-term – e.g. 90 days – are administered and repaid more easily than larger, longer-term group credit. The experiences of MFIs in the Philippines show that excessively large group loans encourage members to withdraw from the effort and drop their financial commitment (Llanto, 2007).

Yap and De Wandeler (in this issue) describe how community networks in Bangkok, Thailand, supported by NGOs, negotiate with landowners. This process typically results in land sharing and/or resettlement with compensation. The government provides subsidies for infrastructure and housing, and exempts these areas from building regulations. The NGOs orient and organize these communities so that these settlements gain sufficient cohesion and strength to negotiate with the government and others. Such community networking has led to more power for poor urban neighbourhoods that promotes upgrading, land sharing, and resettlement.

Yap and De Wandeler also show that networks of community organisations join with networks of savings groups in Thailand. Savings groups can obtain a government loan from the national government's Urban Poor Development Fund for income generation, land purchase and housing construction or improvement once they have proven that they can manage community finance.

The Village Savings and Loan Associations (VS&LA) that started in 1991 in Niger have spread over 16 African, two Latin American, and two Asian countries offer a quite different approach. Originally, this organization focused only on rural areas but now includes urban areas. VS&LA are independent financial self-help groups in which members pool savings from which credit will be distributed. Each association keeps books on all financial transactions. The participants determine for which purpose loans are eligible (VSLA associates, n.d.). These financial self-help groups, which Rutherford (2000) calls Accumulating Savings and Credit Associations (ASCAs) and Bouman (1995) ASCRAs, are also reported by Brook, Hillyer, and Bhuvaneshwari (2008)³ for a South Indian peri-urban area. Financial self-help groups collect savings and deposit them in a bank account. Brook et al. (2008: 159) ascribe advantages to these self-help groups: 'they can be more flexible with regard to the purpose for which loans are taken (...); and they are less bureaucratic, which is important in cases where the poor and illiterate are intimidated by formal institutions.' Participants must repay previous credit before becoming eligible for a new loan.

'Anecdotally, it was found that some thought this was inflexible and so took out bank loans if they needed more than one loan at a time. These six members used their SHG loans to pay off moneylenders, thus incurring a debt with a much lower rate of interest.' (Brook et al., 2008: 160).

Such juggling money is of extraordinary importance to enable the livelihood strategies of the poor (Lont, 2005; Smets, 2000).

In India, many auction *chit funds* are non-banking financial institutions under jurisdiction of the central bank. These *chit funds*

³ Brook et al. (2008) refer wrongly to the ROSCA (Rotating Savings and Credit Association), where savings pooled will be allocated to each participant by turn. In ASCAs savings are used to provide loans.

are a type of ROSCA that pool savings and, then, allocate them to the participant accepting the highest discount. All participants obtain the pooled savings one during a cycle. Any remaining amount gets distributed among all members (Smets, 2000).

In Brazil, a system of housing cooperatives and associations (*consorcios*) pools savings of groups of households to find and purchase land parcels, subdivide, and build housing projects (Ferguson, 2007). A housing *consorcio* is typically a group of 100–144 families that agree to make monthly payments for a specified number of months, and take the pool of funds gathered each month and allocate them to one or more members to actually buy a house. This system is highly controlled today by the Central Bank.

Consumer credit for purchase of building materials

Boxes 3 and 4 profile two studies on consumer credit for the purchase of building materials: one commissioned by Ashoka (Leonardo Letelier & Soares, 2007) and one contracted by Cities Alliance and the municipality of Sao Paulo (principal investigators: Frederico Celentano & Alex Abiko, 2007).

Both studies of consumer credit for the purchase of building materials concluded that households select the place where they buy construction materials by taking mainly into account the price, method of payment, store brand, and the distance of the store from their house. Many pay for their building materials by cash, but serial consumer credit for building materials is on the rise. Moreover, consumer credit for building materials already covers 20% of housing investments in Sao Paulo and has a huge potential for growth. More favourable interest rates, terms, products and services can facilitate a sustainable expansion. Otherwise, a consumer credit explosion may occur, with mass defaults. Here, microfinance expertise can be brought in through business alliances with building material retailers.

Incremental housing finance: filling gaps and expanding to scale

Evidence examined in this paper suggests that current approaches to incremental housing finance are heterogeneous. However, many are high cost, unreliable, and relatively small-scale. Filling the gaps left by these practices and expanding to a size relevant to the low/moderate-income housing challenge requires fundamental new strategies. We make eight recommendations below.

Recommendation 1. Broaden the institutional platform for support of small credits for the low-income housing/upgrading process by using the building materials and real estate development industry and commercial banks as the base and employ MFIs as intermediaries

Small home improvement loans have become a niche secondary product useful to many MFIs. In most countries, however, microfinance institutions lack the capacity and the interest to expand low-income housing credit to massive scale.

In contrast, homebuilders and building materials manufacturers and retailers must provide housing loans for the bottom of the income pyramid, as a large portion of their sales come from this segment. Big corporations such as CEMEX of Mexico – one of the top three cement manufacturers in the world – provide a much broader, powerful, and more robust institutional platform for small home credits than do microfinance institutions, particularly in large countries. Although they recognize they must channel credit to grow their core business, building materials retailers and

Box 3. Building material consumer credit in Sao Paulo- the Ashoka Study (2007)

The Ashoka study surveyed 12 local building materials stores, 237 households and conducted a number of household focus groups in two shantytowns (*favelas*) in Sao Paulo. Virtually, all households in these two *favelas* owned their own home. The municipality has provided basic services in these *favelas* and 91% of households intended to improve their homes through expansion and/or remodelling. Families prioritized price, financing, store brand, and distance from their house as the main factors in choosing stores to purchase building materials.

Half of all purchases were made in cash. Families financed about a third of their purchases mainly using consumer credit but sometimes with a credit card, either their own or of a friend. These stores reported that their sources of financing typically qualified customers for a maximum of US \$1500 in credit – the average cost for the building materials to add one room. These building materials stores offered credit of their own by accepting two to three monthly instalment payments.

These stores also channelled bank credit for materials purchase at market rates (3.5–6% per month) with 12–48 monthly instalments, and offered negligible amounts of highly subsidized FGTS (Fundo de Garantia de Tempo de Servico – incantatory contribution by formal sector workers to a housing/Social Security fund) housing ‘microcredit’ (at 0.5% per month, with up to 96 monthly instalments) due to its scarcity (and reported non-payment rates of 30% on such ‘microcredit’ government programs). These interest rates for consumer credit compared to market-rate mortgage interest rates of around 15% per year at the time, with inflation running around 4% per annum. For many reasons, Brazil has historically had some of the highest real interest rates in the world, which plague economic activity, in general, as well as the housing industry, in particular.

Households accepted the market rates of consumer credit charged for building materials purchase as the cost of doing business. In fact, 40% of households surveyed were unable to remember the interest rate at which they took consumer credit. In comparison, moneylenders typically charge much higher rates – 10% per month in Brazil – while credit card companies charge stiff penalties when debt is carried from month to month, resulting in effective interest rates of as high as 140% per year.

In addition to credit for building materials, the Ashoka study reported that roughly half of households expressed a strong interest in specialized labour for construction. Families had hired qualified workers for roughly a quarter of work conducted in the past, wanted to reduce the amateur level of construction, and – because of increasing household incomes – were willing to pay for more professional help in the future. Prior to the research, Ashoka investigators thought that community members frequently helped each other with construction; such as barbecues to pour foundations. In fact, they found little evidence of such mutual self-help. The Ashoka study concludes by recommending a pilot project in one *favela* in the greater Sao Paulo metropolitan area that joins consumer credit, discounts on building materials negotiated with local stores, and technical assistance to families in construction.

manufacturers frequently do not want to become lenders to poor families and communities.

Commercial banks have ignored the bottom two-thirds of the income pyramid in the past in most developing countries and

Box 4. Consumer credit for building materials in Sao Paulo – the Municipality/Cities Alliance Study.

The Cities Alliance/Municipality of Sao Paulo study conducted extensive interviews with public and private financial institutions offering credit for building materials purchase and with building materials stores. Private banks typically targeted their credit towards their account holders or the clients of building materials stores with which they had formed business alliances. Public agencies and financial institutions targeted credit to low-income households earning up to three minimum salaries. Maximum amounts financed varied from US \$2000 to 10,000. Interest rates for private-sector institutions ranged from 2 to 6.5% per month, and maximum terms from 12 to 48 months. Not surprisingly, households with no credit record tended to receive smaller loan amounts, higher interest rates, and shorter terms within these ranges.

Virtually all of the financial institutions that extended building materials credit required verification of household income and confirmation that the property has no liens by checking registration records in the local cadastre. Commercial banks often insisted that borrowers open an account in that institution, while other programs often demanded that a guarantor co-sign the loan.

Profit levels varied dramatically among stores. The stores surveyed sold mostly to homeowners (40–60%), then to renters (10–30%), and finally to construction contractors (5–10%). Small stores purchased most materials very frequently – either weekly or every two weeks. These frequent purchases allowed small stores to save money by maintaining a small stock, but did not permit negotiating better prices through bulk discounts with suppliers. A key bottleneck in their business model is finance to buy larger quantities at one time from suppliers, and the capacity to negotiate better prices through bulk discounts.

These building materials stores lend based on knowledge of their client base and relationships of trust developed over time. Households pay largely in order to maintain their credit with the stores and place in their community. This logic closely parallels that of microfinance institutions. However, these stores' consumer credit lacked the rigorous methods of microfinance institutions, was highly fragmented, and suffered from lack of integration into other aspects of the store's business.

The Cities Alliance/Municipality of Sao Paulo study arrives at a number of key conclusions. Consumer credit finances approximately 20% of housing investment in Sao Paulo and is a huge business involving virtually all the major financial institutions of the country. However, enormous demand for small serial credits for housing remains unsatisfied. The study finds that housing microfinance could be greatly expanded to facilitate progressive housing if current consumer credit practices were revised to adapt to the needs of clients.

In particular, interest rates, terms, and the products and services must better suit customers. The extremely high interest rates charged to households without credit records in Brazil (4–6.5% per month) are clearly unsustainable, and threaten to provoke a consumer debt crisis. Consumer credit should allow the finance of specialized construction labour rather than just building materials. While building materials retailers must offer or channel consumer credit to be competitive, they are not specialists in extending loans to low-income households and conduct this aspect of their business casually without integration into their larger business. Thus, there is a strong need for microfinance

expertise, which could be acquired by forming business alliances.

The market for small housing loans goes far beyond construction materials for improvement of homeowner units in 'informal' communities; i.e. prototypical housing microfinance. There is huge market demand in Brazil for small loans to finish, remodel, and improve government-assisted housing projects – both high-rise apartments and core-units subdivision – that essentially deliver an unfinished shell unit. Even most renters of central-city tenements (*corticós*) have expressed interest in credit to fix up their units.

creamed only the top of the market. However, the saturation of upscale lending markets, the increasing competition in domestic financial markets, and a growing awareness of the opportunities presented by the rapidly expanding lower middle class, have focused the attention of commercial banks on this income segment. Increasingly, commercial banks see extension of housing credit to these households as a key product to capture these families' savings and sell them other products. In order to reach these markets with housing loans, commercial banks often form business partnerships with a wide variety of housing suppliers and, sometimes, MFIs. In Guatemala, *G and T Commercial Bank* has formed a unit that works closely with 12 housing suppliers of various types – from building materials retailers to commercial affordable housing developers – as well as MFIs to extend credit for housing development and purchase to large numbers of low/moderate-income families (Vance, 2008).

In big developing economies such as Mexico, Brazil, India, and Indonesia, some microfinance institutions may become specialized niche lenders for large distribution networks of suppliers of inputs to the progressive housing process or for large commercial banks. Various studies have suggested the use of MFIs as intermediaries for housing microfinance, particularly in Asia (e.g. Monitor Group, 2007). This option has many attractions. It builds on the comparative advantage of MFIs; their ability to keep in close relationship and work with low-income households. In comparison, large building materials manufacturers and commercial banks face considerable difficulties in working directly in low-income communities.

Recommendation 2. Informal housing finance institutions deserve a place alongside formal systems

Many interventions, even those of NGOs, Community-Based Organisations, and MFIs tend to neglect informal financial institutions. Instead, they start (housing) microfinance schemes in urban neighbourhoods or villages without knowledge of the informal financial networks active in that specific local setting. It is often believed that areas unserved by formal financial institutions lack all financial services except unscrupulous moneylenders. However, MFIs charge similar or even higher interest rates than money lenders with some frequency. Not surprisingly, the governments of some countries (e.g. Colombia) have reacted by placing legal limits on the interest rate that financial institutions including MFIs can charge.

Lacking conventional collateral, informal housing finance typically uses social collateral, especially financial self-help organisations. Such mutual cooperation is based on trust, which the intervention of NGOs can harm. In a slum in Hyderabad, India an NGO set up financial self-help groups among local people without taking into account how informal networks had long selected community residents for participation. These groups collapsed from lack of trust. Another Indian case shows that trust relations

require 10–15 years to develop to the point that people dare to participate in a financial self-help group (Smets, 2006a).

Hence, a kaleidoscope of formal and informal financial institutions creates opportunities for competition so that clients may pick the financial services that fit them best. Access to various sources of credit is also a vital part of the livelihood strategies of the poor.

Recommendation 3. Package housing microfinance with other key inputs to the low-income housing value chain through business partnerships and new business models

The key to creating value and, thus, markets in affordable housing is not only to lower the costs of each step in the value chain but also, more importantly, to innovate and join products and services together into new business models that address larger segments of the problem (Ferguson, 2008a, 2008b). No corporation or organization contains the range of products and services necessary to support progressive housing comprehensively. Hence, assembling appropriate packages requires business alliances among microfinance institutions, building materials retailers and manufacturers, banks, homebuilders, citizen-sector organizations, and government. Credit is only one of various important pieces of this puzzle.

In large markets dominated by modern building materials retailers and manufacturers and major financial institutions, these large corporations and commercial banks are the most likely candidates to organize such business partnerships.

Recommendation 4. Expand beyond small home improvement loans to extend credit for the enormous variety of low/moderate-income housing investment in developing countries

Housing microfinance has come to be synonymous with small home improvement loans (typically, US \$500–2000) of short duration (typically two years) at high interest rates (3–6% per month) for building materials to expand a homeowner's unit. This is largely because microfinance institutions found in the late 1990s that they could apply their existing loan methods and organizations to such loans with virtually no modification.

However, housing markets in developing countries have evolved rapidly in the last decade. Low-income families earn more and a large new group of households – about 20% of the population of dynamic countries including Peru, Mexico, Brazil, India, and Indonesia – have graduated into the lower middle class. Small serial home loans can help fill many of the new market niches created by this dynamism. For example, market assessments of Brazil show large demand for small credits to finish or expand government-assisted shell units – either in high-rises or core-units in subdivisions – and for professional labour rather than just building materials. However, Brazilian banks and consumer credit providers lack products useful for these needs.

The small share of rental housing (less than 20% of housing stock) creates enormous problems for many low/moderate-income families in many Latin America and Caribbean countries. Elsewhere – such as much of sub-Saharan Africa – most urban households rent, but no institutional financing or means of formal support exists for rental housing. Gilbert's seminal study (2003) of rental housing in developing markets has shown that the main rental supply comes from 'informal' low-income communities. In this regard, small credit could be extended to build or remodel accessory spaces and units for rent.

The governments of densely-populated dynamic East Asian cities (e.g. those of China) have little choice except to build shell condominium units in high-rises for low-income housing. Small

credits could be used to build out the shell so that the unit becomes habitable.

Pakistan has largely opted for the sites and services model for low-income housing projects. However, collusion between local government officials and clandestine land developers that benefits both at the expense of the public predominates. Typically, the result for the low-income households is a plot of raw land in a distant subdivision with, at best, communal water and dirt roads without legal title to the property. Such clandestine subdivisions account for most low-income land development in most developing countries. The case of Saiban in Karachi (Ferguson, 2008a, 2008b) demonstrates the many ways that small housing loan can improve this dismal reality when joined with other parts of the low-income housing value chain. Van der Linden (1997) has emphasized the importance of removing exploitative patronage relationships – such as those between local politicians and the poor – to enable settlers to invest efficiently in low-income housing.

In many sub-Saharan African countries (e.g. Rwanda and Kenya), few urban low- and moderate-income households individually own the land on which their houses stand, which is often communal tribal property or owned by others. In such contexts, some MFIs have begun to accept evidence of security of individual tenure (rather than ownership rights) – such as land leases – for underwriting small housing credits (Unitus/Lehman Brothers, 2007). Housing microfinance can play an important role in financing low-income urban land development, the largest bottleneck to housing the poor (Ferguson, 2008a, 2008b; Freire, Ferguson, Cirra, Lima, & Kessides, 2007) as the example of Saiban in Pakistan discussed below illustrates.

In addition to the many new uses for microloans, huge unmet demand exists for somewhat larger loans (US \$2500–10,000) for the housing solutions preferred by the rapidly growing lower middle class of dynamic developing countries (much of Asia and Latin America). Meeting this demand requires longer loan duration (e.g. 10 years) and lower interest rates, new methods (for funding, underwriting, processing, servicing, and collecting, loans, and risk management), and institutional innovation. The development of distinct products and institutions for this market has largely yet to occur. Thus, housing microfinance is only one step in the creation of a wide spectrum of innovative credit products necessary to meet the massive demand for affordable housing in developing countries.

Recommendation 5. Incorporate housing microfinance into the core mission of MFIs

This recommendation of the mentioned Accion study presented by Mesarina and Stickney (2006), is particularly important in smaller countries and markets where MFIs may well continue to play a lead role. In this regard, MFI networks must bring to the attention of individual MFIs the crucial importance of housing to their core mission of the 'giving people the tools they need to work their way out of poverty' (Accion's stated mission). More frequently than in high-income nations, owner-occupied housing generates income through rental of spaces and accessory units, provision of the location for micro-business, and as the main social security in old age in developing countries with precarious or no pension systems. Most fundamental, homeownership is the main means used by families to create wealth, which many studies show is the principal route out of poverty and to upward mobility.

Raising the profile of housing credit in the MFI industry will require more technical know-how on this topic – that is, putting the housing back into 'housing microfinance.' It will also involve formation of business alliances with other key players in the low-income housing industry including government, an institution that MFIs have long sought to avoid.

Recommendation 6. Channel government housing subsidies through second-tier housing banks experienced in working with developers and financial institutions in the form of small grants that complement housing microcredit

MFI in Colombia, Nicaragua, and elsewhere have had trouble joining housing microcredit with government subsidies to help the poor. In essence, these MFIs fear – with good reason – that involving politicized government housing agencies will dilute the willingness to pay of households on microcredit. Historically, the MFI industry has grown out of a rejection of grants and subsidized credit for rural development and the principle that only market-rate credit can sustainably finance micro-business (Robinson, 2001). Housing, however, is a ‘merit good’ in which the public sector inevitably retains some responsibility.

The ABC direct-demand housing subsidy programs of Latin America are an example. These programs function best when market-oriented second-tier government housing finance institutions control and administer the subsidy (such as the National Housing Bank in Costa Rica and SHF in Mexico) rather than social housing bureaucracies.

Another approach is that of the Kuyasa fund of Cape Town, South Africa. This organization makes loans to families that have received a government housing subsidy that allows them to increase the size of their unit from an average of 23–54 m² (Unitus/Lehman Brothers, 2007; Mills, 2007).

For many reasons, mortgage credit and housing subsidies are easier to ramp up than housing microfinance. Nurturing market-rate housing microcredit – particularly the capacity of microfinance lenders in this new realm – takes more time. Governments also tend to adopt the rhetoric of microfinance, but undermine its power for scale by channelling credit through public housing agencies at heavily subsidized rates. Such subsidization risks contaminating the housing-microfinance market and the growth of a sustainable housing microfinance practice. Examples include FGTS in Brazil and FONHAPO and many state government housing institutes in Mexico. Not surprisingly, neither Brazil nor Mexico has a significant housing microfinance industry.

Notwithstanding, housing microfinance has both a commercial market-rate application and a socially-defined mission when joined with public subsidies (in the form of grants that complement market-rate microcredit and households' savings). Subsidizing the interest rate, however, creates numerous policy and program dilemmas.

Recommendation 7. Create and strengthen institutions for finance and development of land parcels and communal infrastructure for low/moderate-income groups

Building the structure of the individual house is only one aspect of the low/moderate-income habitat challenge. Acquisition of land parcels and communal infrastructure and services is equally if not more important. Community-based housing finance has a special role to play in this regard. This practice can take various institutional forms. In Mexico, CEMEX – one of the three largest cement producers in the world – has a program to lend to low-income neighbourhoods in order to pave local streets. The loan goes to the group, and individual households repay their pro-rated share.⁴ Such commercial community-based housing finance for communal infrastructure has begun to spread to microfinance institutions, such as *MiBanco*⁵ in Peru, which also lends to groups of households

for street paving. In both cases, group repayment rates for this communal infrastructure are excellent.

In Karachi, a sophisticated citizen-sector organization – Saiban – has acquired land parcels, organized, financed, and provided the internal infrastructure for over 60,000 people (Ferguson, 2008a, 2008b). The process to apply for and buy a lot is handled on-site and involves minimal paperwork. Saiban offers a flexible payment schedule consisting of a down payment of 20–40% (about US\$175) of the total price. Households pay the remaining amount of US\$525 in monthly instalments over 100 months. The resulting payments of US\$5.25 dollars per month are affordable even to the lowest-income households and virtually none drop out of the process. Saiban keeps ownership of the lot until the last payment, after which it delivers full legal title to the families. Saiban has also worked with commercial banks to offer mortgage finance to those earning US\$3 per day and upwards.

The initial infrastructure is minimal – partly to discourage speculation – and consists of communal water supply, a soak pit for sanitation, and public transport from private suppliers. The remaining infrastructure – including underground sewerage, piped water, electricity, and paved roads – is extended incrementally as instalment payments are made. Saiban develops the infrastructure internal to the subdivision including underground sewer and water pipes, electric poles and wiring, and internal paved roads funded by the monthly instalments from purchasing households. The relevant government agencies develop external infrastructure including trunk sewer lines, sewage treatment plants, bulk water and electricity supply, and access roads. In order to discourage speculation, Saiban requires that a poor family stay at a reception site for up to two weeks to demonstrate need. On making the down payment at the end of the two-week waiting period, the family gains possession but not title to the plot, which is delivered to the family on payment of the final instalment (for a similar scheme in Hyderabad, Pakistan, see: Van der Linden, 1997). In addition, Saiban arranges for a wide variety of other services. Perhaps most important, Saiban transfers a clear title to the lot when households make the final payment on their land and ensures public safety in its settlements through agreements with local police (usually, not to intervene) and others.

Various types of public-private partnerships have potential for providing basic communal infrastructure and services to the poor.

Recommendation 8. Provide technical assistance to financial institutions for HMF along with appropriate funding mainly from domestic sources but also from international groups with experience across countries and regions

The *GmbH (2005)* survey of 25 Latin American MFIs found that appropriate funding is the main factor necessary to increase their housing lending. *Magowan (2008)* details the characteristics of such appropriate funding. More and better funding can certainly help in many instances.

With some frequency, however, declarations of lack of appropriate funding indicate deficits in the know-how, information systems, and business alliances necessary to engage in low-income home lending. Packages of funding and technical assistance from international sources with experience in a range of countries have an important role to play in supporting housing microfinance. Such international support can disseminate important innovations. As capacity develops, this funding and technical assistance best comes mainly from local sources.

Conclusions

Affordable housing finance markets will grow exponentially as 90% of the net increase in world population of 4 billion people by

⁴ http://www.cemex.com/su/cs/su_ca_so_hi_ph.asp.

⁵ Source: interview with *MiBanco* manager, Jesus Ferrera.

2050 is projected to reside in the urban areas of developing countries. The bulk of these people will earn low to moderate-incomes and construct their homes progressively. Hence, finance for incremental housing has a huge potential market. The bulk of such incremental housing finance now occurs informally. The micro-finance industry and has recently entered this market by introducing small home improvement loans as a niche product largely to their existing clientele, although on a miniscule scale relative to demand. The expansion of incremental housing finance to scale requires a number of fundamental innovations. These include broadening its institutional base, offering a wide variety of products beyond small housing improvement loans, joining serial small credits with other components of the affordable housing value chain, partnerships among financial institutions and homebuilding materials suppliers and developers, and improved funding.

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