CIVIS

Shelter Finance for the Poor Series

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Shelter Finance for the Poor Series Synthesis

Series Introduction

From shacks in the shantytowns of Lima, Peru, to tin-roofed mud huts in the slums of Gujarat, India, insecurity of tenure and uneven income streams force the poor to build their homes tentatively, one wall at a time. Yet the poor lack access to financial institutions and financial products tailored to the way they build. This, despite the fact that in so many developing cities around the world a majority of the population lives in slums—60 percent of Nairobi's population, 82 percent of Lima's population—and that most housing is built informally and progressively.

The Cities Alliance launched the Shelter Finance for the Poor Initiative to focus on the still nascent practice of financial institutions providing housing finance to poor clients on commercially viable terms. These loans are distinct from mortgages in that they are typically not for the purchase or construction of new units, but rather for home improvement and progressive building. They are being offered as a new product line largely by a generation of microfinance institutions that built their success on providing working capital loans to the urban poor, and are now looking to expand and diversify their products. To date, few of these experiences had been viewed through the prism of scale and sustainability. This is the framework applied to five case studies examined under this initiative: Mibanco in Peru, SEWA in India, FUNHAVI in Mexico; a wholesale fund facility in Ecuador, and the enabling environment for shelter finance in Kenya. This synthesis paper identifies emerging policy recommendations on taking housing finance for the poor to scale.

The objective of the Series is to look at shelter financing in practice through the prism of scale, sustainability, and outreach to the poor, and learn about best ways to encourage and promote this emerging practice.

Introduction

This paper makes three central points:

I) There is strong demand from poor people for housing finance services tailored to the way they build.

II) Lessons are emerging in large part from microfinance institutions building on earlier successes with working capital loans, and innovating with new housing loan products.

III) The large potential for achieving scale and sustainability can be realized if financial institutions, governments, and donor agencies work in concert.

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"There is strong demand from poor people for housing finance services tailored to the way they build."

Box 1. The Five Cases in the Shelter Finance for the Poor Series[1]

- Mibanco, Peru. A commercial regulated bank, Mibanco is Latin America's second largest microfinance institution with over 70,000 active clients, profitable and in operation since 1972. Half of its clients are women. Mibanco launched Micasa (my home), its home improvement loan program in the middle of 2000, initially as a pilot through four branches. Within 12 months, Micasa had 3,000 active clients, an outstanding portfolio of US$2.6 million, and was profitable, generating almost $16,000 a month in incremental net income.[2] It anticipates that these loans will grow to 50 percent of its overall portfolio within the next five years. Mibanco is part of the ACCION network of 27 financial institutions in Latin America and Africa.

- FUNHAVI, Mexico. FUNHAVI is a non-governmental organization focused on a single loan product: housing microfinance loans. Affiliated with Cooperative Housing Foundation, an international network of housing finance institutions, FUNHAVI has been in operation since 1996. As of October 2001, it had 1,300 active clients of whom approximately 40 percent are women, an outstanding portfolio of $1 million, and was operationally sustainable and moving towards financial sustainability.

- SEWA Bank, India. SEWA Bank was established as a cooperative bank in 1974, with initial share capital contributions from 4,000 members, all very poor women belonging to the Self-Employed Women's Association, a registered trade union. The bulk of SEWA Bank's capital comes from member savings. As of January 2002, the Bank had 3,700 loans with a portfolio of almost $1 million outstanding in home improvement and infrastructure loan products. This amounts to 40 percent of SEWA Bank's total portfolio.

- Ecuador. This case looks at the early experience of a demand-led subsidy program funded by the Government of Ecuador and the Inter-American Development Bank to involve non-bank financial institutions and private commercial banks in providing financial services to poor, low- and middle-income households.

- The Policy Framework, Kenya. This case analyzes the legal, regulatory and policy framework for housing finance loans in Kenya, to understand the barriers faced by financial institutions that have been trying to provide this service for some time with limited success, and to extrapolate policy issues and recommendations that are applicable to many developing countries.

[1] It is important to note that the cases were not selected a priori as "best practices", but were selected by their networks as those with experience worth documenting, and those willing to subject themselves to public scrutiny, irrespective of the final analysis results. Full case studies as well as summary notes are accessible on www.citiesalliance.org.

[2] Henceforth, all dollars, unless otherwise indicated, are US dollars.

I. Demand for Housing Finance is Strong

In 2030, there will be an additional 2 billion poor people living in urban areas, as the world is urbanizing at a rate unprecedented in history. It is estimated that there are currently some 840 million slum dwellers—without a significant shift in policy approaches, this figure will double within the next 20 years, with the bulk of this urbanization of poverty occurring in Africa and Asia.[3] Demand for housing and housing finance will increase, as illustrated by the following examples:

- **Peru** Eighty-two percent of the 8 million people living in greater Lima are classified as poor. At least half of poor households and 60 percent of the poorest households express a strong desire to expand or improve their home within the next 12 months. Only 10 to 15 percent are borrowing from formal or informal sources.[4]

- **Indonesia** In 2000, the country's urban population of 85 million already represented 40 percent of the total. By 2010 it will represent 50 percent, with 120 million people. Annual projections for housing needs for the next 10 years are approximately 735,000 new units and an additional 420,000 in need of improvement. An estimated 70 to 80 percent of all housing in Indonesia is constructed informally and incrementally, with minimal access to formal financial markets.[5]

- **Morocco** Two surveys found that 88 percent of households have or are planning a productive activity in the home, and more than 83 percent of households are willing to take a loan to finance their home improvement projects. Ninety-two percent of urban and 94 percent of rural households constructed their own homes without access to formal finance.[6]

Poor urban residents identify their most important needs in order of priority as (i) lack of jobs, (ii) inadequate housing, and (iii) water supply.[7] Lack of access to formal sources of finance and household credit is emerging as one of the most significant obstacles to the reduction of urban poverty, hampering not only the improvement of shelter conditions, but also local economic development.

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II. Emerging Financial Sector Responses

Innovations in providing shelter loans on commercial terms to poor people are emerging largely from private financial institutions, many of which originated as microfinance institutions. These institutions are a heterogeneous set of players comprising private commercial banks, credit unions, non-bank financial intermediaries, housing finance companies, and non-governmental organizations. Their basic lending methodology has been to offer small working capital loans, and reward good repayment behavior with access to increasingly larger and longer-term loans. The clients of the early

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3 Gelbard, Haub and Kent, 1999.
4 Brown and Garcia, 2002.
5 Indonesia: Housing Microfinance Project Concept Note, 2002, World Bank.
6 Davis and Mahoney, 2001.
7 African Population and Health Research Center, 2002.

"The few impact evaluations conducted of shelter finance point to positive results for the poor."

Box 2. The Clientele

Maria, a market vendor living in a poor barrio south of Lima built on "invaded" land, borrowed 2,000 soles ($571) from Mibanco over 12 months for her home. For more than five years, Maria had been saving what she could out of her monthly income of $150 to buy the bricks needed to convert the walls of her two-room home from particle board and to add rooms on the back of the house for her children. She applied for the Micasa loan so that she could finish buying the materials and pay for the construction labor. In applying for the loan, Maria consulted with friends and neighbors to find a contractor with a good reputation. However, when the contractor started building, he realized that the soil on Maria's lot was unstable and needed significant reinforcement to support the weight of the new walls. To cover the additional construction costs, Maria borrowed from family members and a local moneylender. Seven months after taking her Micasa loan, Maria now has encased her original two rooms and kitchen in brick and has installed a cement floor. The walls of the new rooms are complete, but they still lack a roof and solid flooring. Maria has repaid her family members and the moneylender and has five payments left on her Micasa loan. When she finishes repaying her existing loan, she plans to take another to continue work on the additional rooms and begin replacing the tattered zinc and wood panel roof.

Brown and Garcia, 2002.

generations of such institutions are investing significant portions of their longer-term and larger loans into home improvement.

These financial institutions describe their clients as the economically active poor in the informal sector. They are largely serving their existing poor clients with this new loan product, and most provide housing loans as a reward for good past performance on microenterprise loans. As illustrated by the following examples, institutions devise their own indicator for client poverty levels:

- Mibanco's clients' incomes hover around and below the poverty line. The poverty line indicator of gross national income per capita was $175 per month in 2000.[8]
- FUNHAVI in Mexico serves clients who earn between two and eight times the local monthly minimal wage of $125. Less than 1 percent had accessed formal finance prior to borrowing from FUNHAVI.[9]
- SEWA Bank's clients are all poor self-employed women—predominantly street vendors, laborers, or home-based workers. In 1998, an estimated 76 percent of SEWA borrowers had annual household incomes below $415 and half of these had annual incomes below $276.[10]
- Ninety-five percent of the clients of CARD, a commercial bank in the Philippines were earning below the poverty line, with a weekly income not exceeding $13.[11]

The few impact evaluations conducted of shelter finance point to positive results for the poor. An evaluation of Plan International's Credit for Habitat

[8] Brown and Garcia, 2002.
[9] Daphnis, Tilock, Anderson and Fulhauber, 2002.
[10] The Center for Urban Development Studies, Harvard University Graduate School of Design, March 2000.
[11] Ibid.

programs in Bolivia and Guatemala showed that clients invested their $200 to $800 loans in roofing, walls, floors, tiling, water, sewage and electrical connections, and additional rooms. Seventy-eight percent of clients said that home improvements improved family health.[12] Clients with Grameen-financed homes, equipped with Grameen's construction standards of cement pillars and sanitary latrines had 50 percent fewer incidences of illnesses than those without Grameen houses. Their houses suffered far less structural damage during the devastating floods of 1987 and thereafter, compared with non-Grameen homes.[13] An impact assessment of SEWA Bank's slum-upgrading program that included progressive housing loans, reported increases in literacy (school children enrollment), productivity (increase in number of working hours), income, health (lower incidences of illness and thus lower health expenditures), and increased marriage opportunities, higher status, and respect in the community for women borrowers.[14] In sum, housing finance loans serve poor households, and help them improve their livelihoods.

Housing Loan Terms, Conditions, and Service Delivery Innovations

The most significant finding in terms of achieving scale is that housing finance loans are in essence a variant of well-honed working capital loan products innovated by microfinance institutions. The product is distinct from mortgages in that it is typically used for housing *improvement*—a sturdier roof, walls, floors, or a water, sewage or electrical connection, latrine installment, or an additional room—rather than to purchase or build a new home. It is a variant of the working capital loan technology with the following distinctions: longer terms, larger amounts, lower interest rates, adapted loan appraisal techniques, and no differentiated collateral or service delivery channel, as illustrated by the examples below:

- Mibanco's housing loan product differs from its microenterprise loan in the following four ways: a lower annual interest rate, longer terms (up to 36 months compared with 24 months), slightly larger ($916 on average compared with $500), and also available to a new client group of low-income salaried workers such as bus drivers and school teachers. In terms of similarities, it relies on the same informal collateral of household assets and co-signers used for microenterprise loans, despite the mass land-titling program that has taken place in Peru. Mibanco found that land titles are expensive to use as guarantees, and that poor clients do not want to use title as collateral for a less than a $1,000 loan. Mibanco uses the same staff to provide housing loans and, similarly, does not couple loan services with technical assistance or construction advice to clients. Engineers found no qualitative differences between the homes of Mibanco loan clients and those of other institutions that tie construction advice and assistance to their borrowers' loans.
- SEWA Bank's housing products do not diverge significantly from its microenterprise loans, and in fact most of the latter can be used for housing as well. The housing loans are longer-term (60 months compared with 35 months) and cheaper (14.5 percent per year compared with 18 percent) than microfinance working capital loans. Just as for microenterprise loans, clients are required to save for at least 4 to 6 months if the loan is non-collateralized, or provide informal collateral such as household assets, jewelry, or co-guarantors. SEWA prefers that the assets backing the loan be registered in the woman's name. The product is provided by the same staff who handle all of SEWA Bank's other loan and savings products.
- FUNHAVI's only product is home improvement loans. Loan terms range from 6 to 36 months but average 20 months, loan amounts range from $500 to $2,500 and average $1,600. Co-signers serve as the guarantors. Part of the loan is issued as vouchers to purchase construction materials from specified wholesalers. FUNHAVI earns 11 percent of its revenue from purchasing construction materials at wholesale prices and selling them to clients at retail prices. In contrast to the service delivery model of Mibanco and SEWA Bank, FUNHAVI requires that all borrowers purchase materials from suppliers it specifies and receive construction

[12] Plan International, 2001.
[13] The Center for Urban Development Studies, Harvard University Graduate School of Design, March 2000.
[14] Daphnis, Tilock, Chandy and Fulhauber, 2002.

assistance that it provides.

- CARD Bank's (Philippines) average housing loan amount is $349 compared with its average microenterprise loan of $103. Microenterprise loan terms range from 25 to 50 weeks, compared with 50-week housing loan terms. Housing loans are available to clients with a solid repayment record with CARD, and with a minimum year-and-a-half savings record.
- Grameen Bank's (Bangladesh) loans are available to its clients with a good repayment track record, and loans are available for a range of activities from home repair to home construction or land purchase. Loan amounts and terms are larger than for the microenterprise loans, interest rates are lower, and a member must provide legal documentation of land ownership when a house is to be built. While borrowers are responsible for the design of the house, it must meet minimum Grameen health and safety standards, such as having a pit latrine.[15]

To summarize, the key finding is that there are more similarities than differences in terms of the basic principles underlying original microfinance working capital loans: loans remain uncollateralized, savings remain important, women have a significant presence in the loan portfolios, and *formal* land title (distinct from tenure *security*) is not important for institutions to offer this variant of a housing loan product. Also, the basic lending methodology rewards clients' good repayment performance by providing access to longer-term and larger loans. Adjustments to the lending methodology are essentially variations of microfinance institutions' tested financial product. One of the variations is that many of the institutions offering this product undertake a quick assessment of the intended construction proposal to minimize the risk of unfinished construction, and several are training their loan officers in construction pricing and techniques to better assess and monitor housing improvement loans. In Mibanco's experience, adding a home improvement loan product was easier than originally anticipated. This finding is perhaps the most important one in terms of inspiring more retail microfinance institutions to start adding this product to their existing mix of services for poor clients.

Growing Portfolios

Although most microfinance institutions have only recently begun to offer housing loan products, the number is increasing. A study funded by the International Finance Corporation (IFC) identifies 141 institutions providing shelter finance loan products to the poor.[16] And while the scale of operations is still small given its newness, it represents a growing portion of the portfolios. Among the 27 financial institutions in the ACCION network, 7 have housing portfolios totaling almost 10,000 active clients and $20 million in outstanding balances. Housing loans account for approximately 7 percent of BancoSol's portfolio in Bolivia. They represent 6 percent of Mibanco's current portfolio, but are expected to grow to as much as half in a few years. The percentage of Grameen Bank's portfolio in housing loans is 6.7 percent, with a total dollar portfolio of more than $620 million. Grameen disbursed 317 housing loans in its first year (1984) and by November 2002 had disbursed 556,600 housing loans.[17] As of February 1999, CARD's total amount of loans outstanding was $2.2 million, of which 18.4 percent were housing loans.[18] For these institutions, and for the majority entering this market, housing loans are a growing segment of the portfolio.

Financial Sustainability

At this point, it is difficult to make a firm assessment of the profitability of housing finance to the providers, especially given the novelty of these loans as a specific product line. While many financial institutions recognize that an increasing proportion of their loan portfolios are being invested in housing, very few maintain disaggregated portfolio data. The Cities Alliance case studies of Mibanco in Peru, FUNHAVI in Mexico, and SEWA Bank in India are the first to use an analytical framework of scale and sustainability to assess housing finance loan products. Although the sample is small, these three case studies indicate that financial institutions can provide this service on commercially viable terms.

[15] The Center for Urban Development Studies, Harvard University Graduate School of Design, March 2000.
[16] Escobar, 2002.
[17] The Center for Urban Development Studies, Harvard University Graduate School of Design, March 2000; Grameen Bank Monthly Update, November 2002.
[18] The Center for Urban Development Studies, Harvard University Graduate School of Design, March 2000.

- **Mibanco** The institutional impact of Micasa after 12 months has been positive, with almost 3,000 clients, a high-quality albeit young portfolio, with the portion at-risk greater than 30 days of only 0.6 percent. Micasa broke even on a cash-flow basis, including the initial investment in adjusting the management information system within nine months, and, if performance continues at present levels, is expected to generate a return on loan portfolio of between 7 and 9 percent, compared with its overall return on loan portfolio of 3.4 percent.
- **FUNHAVI** After six years in operation, FUNHAVI is operationally self-sufficient and moving towards full financial sustainability.
- **SEWA Bank** SEWA Bank is profitable and has been in every year since 1998, with small operating losses reported in 2001. It has had a correspondingly positive return on assets except for 2001. It should be noted that these figures include SEWA Bank's total portfolio, since the portfolio was not disaggregated for housing loans, which account for an estimated 40 percent of the total portfolio.

Moving to Scale

The potential for scaling up housing finance for the poor is reinforced by the following converging developments:

- **Product innovation in housing finance by a generation of microfinance institutions** that has understood delivery of other financial services to the same clientele, and that is institutionally and financially stronger now than 15 years ago. When Mibanco decided to offer its Micasa housing finance loans in August 2000, it had already established itself as one of the largest microfinance institutions in Latin America with nearly 70,000 active clients, an outstanding portfolio of $45 million, and net income of $1.2 million. It could thus demonstrate positive results on the Micasa housing portfolio within the first 12 months.
- **Product innovation in community-led low-cost housing construction,** engineered by community-based organizations such as SPARC in India, and the South African Homeless People's Federation, where poor communities are building homes at a significantly lower cost than comparable houses in the local market.
- **Joint ventures between housing institutions and financial institutions,** as illustrated by Intermediate Technology Development Group (ITDG), an international NGO and NAHECO, a group of community-based organizations, working together in Nakuru's informal settlements in Kenya, where ITDG has developed a low-cost house and NAHECO provides business and housing loans towards acquisition of these homes.[19]
- **Entry of traditional commercial banks and credit unions** who find that the longer terms, larger amounts and, at times, some form of collateral backing the loan are closer to their comfort zone than traditional

"Although most microfinance institutions have only recently begun to offer housing loan products, the number is increasing."

[19] Brown, Tilock, Mule and Anyango, 2002.

> "*Governments play a unique role in creating an enabling policy and regulatory environment for finance institutions that would like to provide housing finance services for the poor.*"

microenterprise loans. Examples include Banco del Desarrollo in Chile, Capital Bank in Haiti, and Banco Caja Social in Colombia.

- **Governments seeking solutions to chronic housing problems**, and a dearth of public finance to perpetuate the social housing model of subsidy provision for each fully constructed unit. This is in addition to disenchantment with the limited scale and mis-targeting of such efforts.
- **Entry of private developers**, such as Argoz in El Salvador, which is subdividing privately owned urban plots of land located on the outskirts of San Salvador and other urban centers, leasing with an option to buy individual lots to low income families, providing long-term financing, and providing limited advice to families and the new settlements on obtaining access to basic services.[20]
- Most importantly, **client demand for services** and **demonstration that they are creditworthy** and a potentially profitable large segment of the population.

III. What Role for Governments and Funding Partners[21] to Assist this Emerging Industry?

A key point to note is that microfinance methodologies and the financial innovations discussed in this note were, and continue to be developed largely by *private sector* institutions, often without national and local government or external donor support. This section outlines some policy recommendations to governments and funding partners about how best to leverage their comparative advantages to support sound financial institutions in order to reach scale and sustainability in delivering housing finance services to the poor.

Recommendations to Governments on Setting the Policy and Regulatory Framework

Governments play a unique role in creating an enabling policy and regulatory environment for finance institutions that would like to provide housing finance services for the poor. Demand for such services will be severely constrained if the poor are not allowed to build, or live in fear of their homes being razed to the ground; and the same holds true for supply of services if financial institutions are restricted by legal constraints or fail to innovate because there is no competition in the market. Policy debates regarding the enabling environment for microenterprise finance focus on the financial services legislation and regulation adopted by the national government. Issues such as minimum capital requirements, depositor protection, usury laws, degrees of intermediation allowed, ownership structures, and institutional soundness and sustainability are seen as the key policy levers available to governments to influence and control the development of the sector. All of these issues are relevant for housing finance. But in

[20] Ferguson and Haidar, 2000.

[21] The term "funding partner" is applied to a broad category of organizations such as bilateral and multilateral aid agencies, private philanthropic foundations, social venture funds, and private investors, among others, that provide funds to microfinance institutions.

addition, the enabling environment also encompasses issues that affect poor people's ability to buy land, obtain legal rights to that land, and build a home upon it.[22] Specifically, governments should focus on the following steps to set the proper policies:

1. Set a conducive macroeconomic financial and regulatory framework for housing finance. Macroeconomic stability and sound financial sector policy remain important preconditions for the development of sound and sustainable financial institutions, and this is as true for those focused on the poor. Bolivia set a precedent that enabled the rapid growth of sustainable microfinance—closing down competing state-run banks operating on an unequal playing field, removing interest rate ceilings, and regulating providers after their formative stage when regulations are appropriate.[23] Kenya illustrates how over-regulation has stunted the development of housing finance despite there being a relatively mature set of interested microfinance institutions.[24]

2. Recognize that poor people build their houses incrementally, and set policies and regulations in accordance. Building codes and financial laws are often based on the assumption that people acquire homes through purchase of a fully constructed unit. For example, in Kenya, building codes were designed for the construction of complete homes, thus making progressive building illegal, despite it being the most common form of home construction for the poor. These codes limit the poor's demand for financial services—they fear that their out-of-code structures will be destroyed and so prudently limit investment in them. The Kenyan Banking and Building Societies Act explicitly forbids financial institutions from lending for plots of land with no or partially constructed housing on it. The Governments of Indonesia and South Africa, on the other hand, have developed comprehensive housing policy strategies that support commercially based housing microfinance programs as one of the tools for housing finance expansion.

3. Recognize that the poor value access to credit more than its cost. As the growing portfolios of microfinance institutions are attesting, the poor are voting with their feet and their message is loud and clear—access to quality and efficient financial services is more important than cost. In turn, microfinance institutions have demonstrated that competent financial institutions can provide financial services to the poor at scale and on commercial terms. Interest rate ceilings or subsidies, or "debt forgiveness" policies, by national governments distort overall financial sector policy and constrain the development of viable institutions that can operate at scale. The Donde Act in Kenya, which regulates loan terms and conditions with the intent to make loans more affordable to poor households, is having the opposite effect with banks reducing their lending to higher risk populations, and investing in safer treasury bills instead. The case of Ecuador, where the government is providing a one-time subsidy to poor families for home improvement, raises the question of whether these subsidies are not in fact stifling the emergence of private sector responses to demand as illustrated by Mibanco, Sewa Bank and FUNHAVI.

The poor are able to service their loan payments since housing is a productive asset for them—30 to 60 percent of housing finance clients are engaged in a home-based income-generating activity. A survey of clients participating in SEWA Bank's slum upgrading program reported a 35 percent average increase in weekly earnings due, in large measure, to loans for home improvements and water and electrical connections.[25]

4. Provide land, basic infrastructure, and social services to the poor and the poorest. To the extent that governments have funds to expend, it is better to invest these scarce funds into areas that do and perhaps always will require subsidies—making land available to the poor, servicing it with basic infrastructure such as water, electricity, and roads, and building and servicing social infrastructure such as schools and health clinics. Also, there may be necessary exceptions to the rule of unsubsidized credit when reaching out to the very poorest who are perhaps better served with welfare programs.

[22] Brown, Tilock, Mule and Anyango, 2002. While this section draws heavily on the Kenya case study in this Series to illustrate points, the examples and points can be generalized to many countries around the world.
[23] See Rhyne, 2001, for more information on the Bolivian Government's role in mainstreaming microfinance.
[24] Brown, Tilock, Mule and Anyango, 2002.
[25] The Center for Urban Development Studies, Harvard University Graduate School of Design, March 2000.

5. Provide secure tenure for the poor. Improving tenure rights is key to increasing security and stimulating improvements in housing and living standards. Households are willing to invest over 30 percent of their income to acquire land, build, or improve their homes.[26] Conversely, they will not spend more than 15 percent of their income on shelter without some assurance regarding security of occupancy as owners or renters. Governments should provide tenure security, if as an intermediate step towards ultimately providing full legal titles. There are many examples of intermediate tenure systems that led to increased investments in housing,[27] such as the Ahmedebad Municipal Corporation granting slum dwellers 10 years security of tenure. As has been mentioned earlier, financial institutions providing housing finance loans do not rely on formal collateral such as land title to back their loans. Despite the significant land-titling program in Peru, which issued 4 million deeds in four years, Mibanco only uses mortgages for loans higher than $5,000, because of the high cost and poor clients' reluctance to use title as collateral for loans that average less than $1,000.

Recommendations to Funding Partners

These recommendations are aimed at funding partners on how best to use their resources to support forward-thinking governments and financial institutions in providing sustainable housing finance to the poor at scale.

1. Policies

Work with and support those governments that seek to promote an **enabling macroeconomic, financial policy,** and regulatory framework for housing finance, as discussed above.

2. Institutional Partners

Select a few financial institutions with a proven track record to partner with, placing emphasis on financial sustainability and portfolio quality as key criteria for selection. It could be argued that the most important factor for the creation of microfinance industries in Bangladesh, Indonesia, and Bolivia was the power of demonstration by Grameen Bank, Bank Rakyat Indonesia, and Bancosol respectively—they spawned industries in their nations and inspired action abroad. As a strategic choice, there is more to be gained by investing limited funds in a select few potential winners and demonstrating impact than spreading resources indiscriminately across many. Nothing spreads like success.

3. Instruments

Provide medium-term capital to financial institutions. Financial institutions offering shelter finance loans need access to longer-term sources of capital than currently available in most developing country capital markets to improve the match between their asset and liability term structures. One example of an initiative addressing this issue is the Community-Led Infrastructure Finance Facility (CLIFF). CLIFF is a new finance facility of the Cities Alliance designed to increase the access of poor communities to medium-term sources of capital.

Provide funds for building institutional capacity, not just for on-lending. Grants or cheap funds should be applied towards initial start-up costs, operating expenditures for a limited time, and knowledge dissemination. ACCION International is planning to pilot a housing microfinance loan product through several affiliated institutions, and then disseminate the results throughout its network of 27 institutions in 21 countries to scale up the experience, with some funding from the Cities Alliance.

Avoid conditions on funds that can (inadvertently) reduce ability to experiment with housing finance. Funding agreements with microfinance institutions often restrict support to microenterprise loans, and restrict institutions from providing a wider array of services to their poor clients in response to client demand. Practitioners are urging their funding partners to assist in building their institutions and their capacity to deliver a wide array of financial services to the poor, and to not pre-determine or restrict the service mix they offer.[28]

[26] Ibid.
[27] Durand-Lasserve, Fernandes, Payne and Smolka, September 2002.
[28] Brown, Tilock, Mule and Anyango, 2002; Franck Daphnis, CHF International, presentation on FUNHAVI at World Bank, March 2002.

4. Knowledge

Support applied research and its dissemination. Many international funding partners work in multiple countries and are well placed to transfer knowledge. Practitioners have identified these topics as knowledge gaps:

- More analysis of the profitability of this product line to make the case for its commercial viability—this is essential to stimulate the entry of more institutions;
- The range and forms of security of tenure that microfinance institutions can use in lieu of mortgage guarantees for the provision of housing loans;
- The points of intersection between mortgage finance technology and microfinance lending technologies to improve product offerings and to reach a wider segment of poor populations;
- The necessity and cost-effectiveness of providing technical/construction assistance to poor clients;
- The links between housing finance institutions and local and national government initiatives—what public sector/municipal-level service provision can help support and facilitate the development of housing for the poor, and of housing finance institutions that enable them to do so;
- And perhaps most importantly, incentives to promote construction of *affordable* housing for the poor by private builders, to reap the benefits of specialization and economies of scale, that will in turn stimulate financial service provision.

Conclusion

Preliminary analysis of the emerging housing finance industry for the poor is demonstrating the same lesson that microfinance has taught us: the poor are reliable clients who are willing to pay the full cost for *cost-effective* services tailored to their needs. Pioneer financial institutions are continuing to build on their strengths and innovate with new product offerings such as shelter finance to retain and expand their clients. The initial round of innovations in this area is likely to come from the existing generation of microfinance institutions. But with proven success, as is happening with the commercialization of microfinance, they will be paving the path for a whole new set of players—commercial banks, mortgage finance companies, private builders and others who typically shy away from poor people. It is our hope that they will soon be vying side by side for poor people's attention and purchasing power.

“...the poor are reliable clients who are willing to pay the full cost for cost-effective services tailored to their needs.”

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