

Finance for low-income housing and community development

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SUMMARY: Over the last 15 years, there has been much innovation in finance to support housing and community development for low-income groups – even though most governments and official aid agencies have paid little or no attention to this. Most of these schemes had savings as an important component. For some schemes, and for many households, savings is the only source of investment finance, as incomes are too low or uncertain to ensure loan repayments. Many of the largest and most effective financial schemes have been cases where the resources and capabilities of low-income households have combined with the efforts of supporting local NGOs and local governments. Even where local governments lack capacity to provide financial support, they have important roles in allowing improvements in informal settlements, helping allocate land for low-income housing and being flexible in the application of standards. International funding agencies would get a much greater development return on their funding if they developed the capacity to support these kinds of local grassroots–local NGO–local government partnerships.

1. In addition to the 20 papers on this topic in the October 2007 and April 2008 issues of *Environment&Urbanization* that are listed on the back page, a further 19 papers on the topic have been published in earlier issues of the journal – and these can all be accessed on-line at no charge at <http://eau.sagepub.com/>. These include Ferguson, Bruce and Jesus Navarrete (2003), "A financial framework for reducing slums: lessons from experience in Latin America", *Environment & Urbanization* Vol 15, No 2, October, pages 201–216; also Malhotra, Mohini (2003), "Financing her home, one wall at a time", *Environment & Urbanization* Vol 15, No 2, October, pages 217–228; Frank, Daphne (2004), "A market-based housing improvement system for low-income families – the Housing Incentive System (SIV) in Ecuador", *Environment & Urbanization* Vol 16, No 1, April, pages 171–184; Stein, Alfredo with Luis Castillo (2005), "Innovative financing for low-income housing improvement: lessons from programmes in Central America", *Environment & Urbanization* Vol 17, No 1, April, pages 47–66; and Boonyabanha, Somsook (2005), "Baan Mankong; going to scale with 'slum' and squatter upgrading in Thailand", *Environment & Urbanization* Vol 17, No 1, April, pages 21–46.

I. INTRODUCTION

IN MOST URBAN areas in high-income nations and many middle-income nations, good quality, legal housing is expensive. Most of it would not have been built without mortgage finance; middle-income households, and even most upper-income groups, need mortgages in order to buy it, or long-term finance in order to build it. In most cities in Africa, Asia and Latin America, low-income households cannot afford legal housing or good quality housing. They either rent (usually in poor quality overcrowded dwellings) or buy or build in illegal settlements. They cannot get conventional housing finance because their homes are in illegal settlements and they lack the income or formal documentation that housing finance agencies require.

However, there has been much innovation in finance to support housing, infrastructure and community development for low-income groups over the last 15 years.¹ Much of this works in informal settlements, supporting negotiations for land tenure security, house construction and improvements, and often improved provision for water and sanitation. Most schemes combine savings, loans and subsidies. During these 15 years:

- State programmes have become less concerned with direct provision of housing and more interested in working with finance to enable greater choice for beneficiaries.
- Microfinance for housing became a significant part of the microfinance portfolio of lending opportunities, although mostly for house improvements and extension.
- Financial deregulation has increased the number of agencies interested in providing mortgage finance in a number of countries, and these are available to a larger section of income groups.
- Innovative approaches using savings and loans to transform low-income neighbourhoods have demonstrated impact at scale.

II. THE THREE KEY SOURCES OF HOUSING FINANCE

The role of savings

IT IS OFTEN assumed that low-income households cannot save for housing, as all their income is needed for consumption – or if they can save, it is only sufficient for community-managed emergency funds or small loans for livelihoods. But many case studies show the importance of savings for shelter investment by low-income groups. Low-income individuals often start savings to provide a fund they can draw on to help cope with emergencies or illness – and this develops into savings for housing too. This is especially so if they have a local savings scheme to which they can contribute,

This Brief of the October 2007 and April 2008 issues of the journal *Environment&Urbanization* is based on the editorials from these two issues and draws on the papers therein. (The papers are listed on the back page, with details of how to obtain electronic copies of individual papers or the whole issues). This summary, produced with the support of the Royal Danish Ministry of Foreign Affairs (DANIDA) and the Swedish International Development Cooperation Agency (Sida) allows the journal's main findings to reach a wider audience.

2. See the paper by Mtafu A Zeleza Manda on Malawi, and Anna Muller and Diana Mitlin on Namibia listed on the back page.

3. See the paper by Shaaban A Sheuya listed on the back page.

4. See the paper by Arif Hasan listed on the back page; also Hasan, Arif (2006), "Orangi Pilot Project: the expansion of work beyond Orangi and the mapping of informal settlements and infrastructure", *Environment&Urbanization* Vol 18, No 2, October, pages 451–480.

5. See the paper by Sophie Mills listed on the back page.

6. See the paper by Anna Muller and Diana Mitlin listed on the back page.

7. See the paper by Mtafu A Zeleza Manda listed on the back page; also D'Cruz, Celine and David Satterthwaite (2005), "Building homes, changing official approaches: the work of urban poor federations and their contributions to meeting the Millennium Development Goals in urban areas", *Poverty Reduction in Urban Areas Series, Working Paper 16, IIED, London, 80 pages.*

8. See the paper by Sophie Mills listed on the back page.

9. See the paper by Sarah Stavrakakis with Ruth McLeod and Kulandei Francis listed on the back page.

10. See the paper by Tova Maria Solo listed on the back page.

11. See the paper by Allan Cain listed on the back page.

12. See the paper by Gilberto M Llanto listed on the back page.

13. See the paper by Alfredo Stein and Irene Vance listed on the back page.

as in the community-managed savings groups that are the foundation of so many federations of slum and shack dwellers.² Savings may support housing improvements outside of any housing programme, as shown by a study in two low-income settlements in Tanzania.³ Renters and would-be owner-occupiers also helped to finance construction with advance rent payments to their landlords (who owned the structures), once settlements became more established.

In Pakistan, household savings have financed the development of infrastructure in over 300 predominantly low-income settlements. Here, financing takes place within a technical support programme from the Pakistan NGO, the Orangi Pilot Project–Research and Training Institute. This is an example of a financial model that uses domestic savings and has a capacity to go to scale once residents are convinced of its value.⁴ One key to its success is keeping down unit costs, so what is provided matches what low-income households can afford. Case studies from South Africa and Namibia also show the benefits of savings programmes – some residents choose to finance improvements through savings rather than taking up loans that they may be entitled to. In South Africa, the Kuyasa Fund offers small loans (often placed within the rubric of microfinance) for shelter improvements. Savings is required prior to loan release and 65 per cent of members only use their programme for savings.⁵ In Namibia, many households within the Shack Dwellers Federation of Namibia prefer to use savings rather than loans to finance the extension of infrastructure from communal to on-plot facilities (for instance, from community to individual taps and toilets). This avoids the risk of not being able to meet loan repayments for those with low and irregular incomes.⁶ In this instance, and also in Malawi, savings is more than simply a means of financing shelter improvements; as in the case of the affiliates of Shack/Slum Dwellers International, community-based savings groups are the core organizing "glue", which help individuals save and which hold local organizations together, enabling them to build the trust and confidence needed to identify collective priorities and implement development projects together.⁷ Savings is widely acknowledged to offer benefits in other cases, as in the examples of the Kuyasa Fund⁸ and IVDP,⁹ although the orientation tends to be on the financial rather than the development process, and hence the benefits are less comprehensive.

In some countries, it is difficult for low-income individuals and groups to get a bank account. They have to form their own savings institutions because no local bank or other institution will support them. In many low-income areas, there are no banks; and where there are, they often only provide accounts to those with formal employment or proof of income and relatively high incomes – and they often have high charges. Not having a bank account implies not only difficulties in saving, but also many other problems and additional costs in making payments (for instance, to utilities or service providers) and in sending and receiving money.¹⁰

Microfinance for house improvements

A growing number of microfinance agencies offer small loans for housing improvements. They usually offer finance only to individual households living on land sites with reasonably secure tenure, and they enable dwelling investment that usually entails adding a room, or an improved roof and/or floor, toilets and/or bathrooms. Shelter microfinance emulates many aspects of enterprise-oriented microfinance and is often embedded within the same agencies. In *KixiCrédito* in Angola, housing finance is offered to those households that have been successful in enterprise borrowing; a second stage is the extension of shelter lending to other specific groups under alternative terms and conditions.¹¹ The Kuyasa Fund in South Africa offers small loans for housing improvements and expansion; these help low-income households that have already benefited from state intervention through a housing capital subsidy programme that provides a plot with legal tenure, services and an initial dwelling. In both cases, the rapid development of loan programmes illustrates the scale of demand for borrowing for housing within low-income settlements. In the Philippines, there is also this combination of state housing programme and loans for housing improvements. The government programme, Development of Poor Urban Community Sector Project, supports local authorities for site development and improvement with housing loan provision along with microenterprise finance.¹² A comparable model has been implemented in various Central American countries. Here, local authorities coordinate the upgrading of low-income neighbourhoods and a range of local institutions offer loans to households to improve their homes. In some cases these can be combined with state subsidies. In every case these loans blend with family savings and self-help efforts, and this blending has demonstrated its effectiveness in many places, as long as the unit costs of housing and infrastructure construction or improvement are not too high.¹³

Group lending for housing

A third source of finance for housing is the collective process of group lending. This is generally for more than just housing and includes loans that fund investments in land and infrastructure. In Namibia, the Shack Dwellers Federation and its support NGO, the Namibia Housing Action Group,

14. See the paper by Anna Muller and Diana Mitlin listed on the back page.

15. See the paper by Gilberto M Llanto listed on the back page.

16. See reference 1, Boonyabancha (2005). See also the ACHR website, www.achr.net.

17. See reference 1, Boonyabancha (2005). See also regular updates on the work of CODI available in English from CODI, 912 Nawamin Road, Khet Bang Kapi, Bangkok 10240, Thailand or downloadable from www.codi.or.th; this includes CODI (2008), *CODI Update: 50 Community Upgrading Projects*, Community Organizations Development Institute, Bangkok, 75 pages.

18. See the paper by Shaaban A Sheuya listed on the back page.

19. See reference 4, Hasan (2006).

20. See the paper by Sophie Mills listed on the back page.

21. See the paper by Allan Cain listed on the back page.

22. See the paper by Tova Maria Solo listed on the back page.

have developed a model that includes regulatory reform, land purchase from local authorities, the extension of infrastructure provision and dwelling construction. This model is affordable to some of the lowest-income citizens as the housing component of the loan does not have to take place immediately and land and service costs can be paid off first.¹⁴ For the Malawi Federation, a sister to the Namibian Federation, group loans were taken to finance the construction of identical dwelling units for the development of housing on 222 plots in Lilongwe. The political impact of these units has been considerable; the national government was sufficiently impressed by the speed and competence of federation members in their construction that it provided the federation with more than 3,000 housing plots. In most of Lilongwe, where there is no provision for sewers, the loan amounts have also been sufficient to pay for the cost of skyloos (elevated pit latrines).

In the Philippines, the Community Mortgage Programme is an example of state support for collective loans. Here, credit for purchasing land is available to groups of low-income households facing eviction from land on which they are illegally settled.¹⁵ In Thailand, an innovative state-financed programme (the Community Organizations Development Institute) has put in place community networks able to manage many aspects of the development process at a local and city level, as well as providing loans available to communities for supporting upgrading or new house construction. Here, the move in the level of intervention from neighbourhood to city level has been important in enabling finance to be used to transform options for some of the lowest-income and most disadvantaged citizens, and for supporting community organizations and local governments to work collectively to address diverse needs and interests across the city.¹⁶ Citywide networks of community organizations work with local authorities in participatory planning and allocate both subsidy and loan finance. This enables the planning process both to prioritize the settlements most in need of upgrading and to consider how finance can help support local environmental improvements for the benefit of all.¹⁷

III. THE RANGE OF DIFFERENT AGENCIES DRIVING CHANGE

THESE THREE DIFFERENT financing strategies for housing – savings, microfinance and group lending – reflect the differences in local circumstances and in the agencies that are engaged with this process. In some cases, the key agent is the people, managing as best they can – as in the case from Tanzania.¹⁸ In Pakistan, for the investments in sanitation and drainage made by communities, the key agent is also the people, but in this case supported by an NGO, the Orangi Pilot Project–Research and Training Institute. This NGO provides technical assistance, catalyzing sanitation investments by showing how the unit cost of good quality provision can be brought down to one low-income communities can afford.¹⁹ In the case studies from South Africa and Angola, the key agencies are microfinance providers, which in both cases emerged from the work of conventional urban development NGOs, Development Action Group²⁰ and Development Workshop.²¹ This highlights a tension for NGOs seeking to provide new shelter options for low-income households, because the organizational demands for providing financial services are very different from those for advocacy. In these cases, in Angola and South Africa, two distinct organizations have developed. These experiences suggest that it is difficult to manage a microfinance agency and an advocacy-oriented NGO within the same organization. Over time, both organizations have divided into two although, in both cases, the newly created microfinance agencies collaborate closely with their “parent”.

The success of collective loans requires strong local organizations. In the cases noted above, in Malawi, Namibia and the Philippines (Community Mortgage Programme), professional support agencies provide advice on the technical aspects of development and offer other kinds of assistance. In part, this is required because these housing development programmes have to work with local authorities, which means working with all their building, land use and infrastructure regulations. In Malawi and Namibia, the local grassroots organizations are networked through federations that enable them to visit and learn from each other. The formation of federations also helps pressure the government to agree to regulatory reforms that reduce development costs (for instance, smaller plot sizes and less expensive infrastructure requirements). Politicians are reluctant to be seen to ignore the demands of mass movements; and may believe that regulatory reforms are a relatively low-cost route to respond to citizen demands. There is little evidence of the commercial sector in these case studies, although in the broader field of microfinance, there is considerable interest shown by formal financial institutions in some Asian and Latin American nations.²² The growth in experience in microfinance for housing has shown the commercial sector that there is a viable market at least in some nations and cities, which can be served by financial institutions or through their collaboration with microfinance agencies. This is important in supporting many lower-income households with relatively secure tenure of their housing plot to improve their homes, but it does not address the needs of the lowest-income groups who are landless.

IV. THE ROLE OF THE STATE

THE STATE IS rarely the driving force behind shelter finance initiatives but it still has a powerful influence on whether low-income groups can get good quality housing. First, it influences land markets and the possibilities for land tenure regularization in informal settlements. Land regularization and the extension of infrastructure and services to what were previously illegal settlements may provide a very good context for providing loans for upgrading.²³ So too may the allocation of land sites to community organizations formed by the urban poor, as highlighted in the case in Malawi mentioned above. Obviously, this process (and any state-managed resettlement), influences the location of low-income settlements and the degree of spatial and/or social inclusion for such settlements. Second, the state's many rules and regulations regarding land use, infrastructure and buildings, and the ways these are applied, influence housing and land prices and availability, and thus whether lower-income groups can get or build legal housing. The extent and application of regulatory systems influences the scale of illegality associated with shelter provision in informal settlements. In Namibia, far more low-income households were able to take part in official legal housing developments when the Slum Dwellers Federation negotiated lower and more flexible building and infrastructure standards. In Malawi, the low-cost housing required the Malawi Federation to negotiate to get approval for the use of traditional materials.

Third, state programmes for services or for social protection may reduce costs or increase incomes,²⁴ and so increase the amount that low-income households can spend on or save for housing. Any shelter finance project that addresses tenure and service needs has to come to an accommodation with the state, even if microfinance programmes providing individual housing loans for dwelling improvements can avoid this.

The state is involved in housing provision in most nations, although the scale and nature of this involvement varies greatly. Even in a very low-income country such as Malawi, there have been a range of government housing policies, although few programmes at scale. The involvement of the state in shelter initiatives reflects the importance of housing to citizen well-being; but the nature of their involvement also reflects the politicization of housing provision as politicians seek to control and gain from the allocation of housing and land tenure. Political elites often manipulate the allocation of housing finance programmes to address their political interests; for instance, housing finance in Brazil under the Collor administration was used to secure political support in Congress.²⁵ In the Philippines, the inadequacies in conventional state housing programmes have encouraged a shift to more market-oriented strategies following the failure of credit subsidies and high rates of default on government loans. What is evident in many contexts is the lack of state support for programmes oriented towards the lowest-income residents.

One key role of the state is to provide the supervisory and regulatory framework for the financial sector. In large part, it was the failure of the state and self-regulatory frameworks that explains the sub-prime crisis in the USA. Loans were given out and sold on in a complex set of financial markets designed to increase the availability of mortgage finance. However, the risks related to such loans were inadequately assessed and/or not fully taken into account. The subsequent problems have been both loan defaults by individual families and related repossession, and the international credit crunch as banks refuse to lend to each other due to fears of bad debt. However, as shown in the papers in these two volumes of *Environment&Urbanization*, there are many positive experiences where loans have been manageable at the household level and the loan-giving bodies continue to be viable organizations. Given the body of knowledge about successful lending to low-income households, why haven't governments and international agencies sought to create an appropriate framework of support and regulation?

In most urban contexts, shelter finance alone can never address the problems faced by the lowest-income groups because the gap between what they can afford and the cost of the cheapest "good quality" unit with infrastructure and services is too high. The case studies noted above emphasize the need for an approach that includes opportunities for tenure security, the upgrading of services and the improvement of dwellings. This is clearly seen in the case study from Angola and the dual roles played by *KixiCrédito* and by Development Workshop, the first providing finance and the second developing new models for land development and lobbying for pro-poor land policies. Another important aspect is a real dialogue between the state and low-income households, so that the limited resources and capacities of each can be combined to maximum effect. For instance, in urban areas in Pakistan, the official bodies responsible for providing water and sanitation were not able to meet needs in informal settlements – but with the introduction of a new model by OPP–RTI, which provided for a realignment of citizen and state contributions, they have been able to provide the "external" water pipes, sewers and drains into which community-managed and financed "internal" pipes, sewers and drains can integrate.²⁶

23. See the papers by Alfredo Stein and Irene Vance and by Florencia Almansi and Andrea Tammarazio listed on the back page.

24. See the papers by Mike Muller and by Nicola Jones, Rosana Vargas and Eliana Villar listed on the back page.

25. See the paper by Marcio M Valenca listed on the back page.

26. See the paper by Arif Hasan listed on the back page.

V. INTERNATIONAL FINANCE FOR LOCAL INITIATIVES

VERY FEW OFFICIAL aid agencies support housing finance initiatives. In part, this is because they do not support urban initiatives. But, in part, it is also because of the challenges these agencies face in finding ways to enable flexible locally managed finance to respond to neighbourhood and city-level initiatives while maintaining the required accountability to the governments that provide their funds. Some international NGOs have long supported housing finance initiatives. For instance, housing finance has been central to the work of the UK-based charity, Homeless International, and it came under pressure to find alternatives to grant finance to allow its funds to increase the scale of their impact. Homeless International has developed guarantee finance to enable organizations in Africa and Asia to obtain loan finance from local banks. It has also developed another financial mechanism to support housing, the Community Led Infrastructure Financing Facility (CLIFF). This is a capital fund provided through Cities Alliance, on which their partner organizations can draw to allow them to increase the scale and scope of their housing initiatives – for instance, by providing bridge financing for large redevelopment programmes, or allowing larger, more ambitious upgrading programmes. This was tried first in India, working with the Alliance of the National Slum Dwellers Federation, *Mahila Milan* and SPARC and this received financial support from the UK Department for International Development and the Swedish International Development Cooperation Agency (Sida). A similar facility is being developed to support low-income housing initiatives in Kenya and the Philippines.²⁷

Another example of an international fund supporting housing for low-income groups is the International Urban Poor Fund, managed by Shack/Slum Dwellers International/SDI and IIED. This provides small grants throughout the SDI network of slum/shack dwellers federations to catalyze local initiatives in secure land tenure and basic services. It finances urban poor funds that have been set up by national slum/shack dweller federations and supports community-led advocacy to advance grassroots solutions. Its contribution lies as much in the flexibility of the funds and the locally determined allocations as in the scale of its support. Many of the initiatives it funds receive only US\$ 20,000–40,000, but the federations make this go much further than conventional development agencies can as it is combined with the resources and capacities of the federation, the locally negotiated support (often from local government) and the care with which the federation uses the funding.²⁸

VI. CONCLUSIONS

IT MIGHT SEEM inappropriate to highlight the importance of shelter finance in low- and middle-income nations, given the crisis in the USA and other nations where large numbers of low-income households cannot repay loans. But this crisis does not suggest that financial markets cannot serve low-income groups or that low-income households cannot manage credit. Rather, it highlights the fact that financial services must take account of the vulnerabilities and limited repayment capacities of low-income households. Financial services for low-income groups need to be developed with these groups as they are best able to assess their repayment capacities and develop effective systems.²⁹ The design of such services needs to take into account the difficult choices faced by low-income households in generating savings, as they struggle to balance potential income gains (microenterprise borrowing), expenditure savings, investments in capacities and relationships (education, marriage) and investments in assets (including housing). Financial services need to have the flexibility to support this complexity.

The examples given above show how far external funding can go if it can support local processes driven by local organizations that make maximum use of such funding. International agencies could do much more with their monies if they were willing to relinquish more decision-making powers and more financial control to local organizations formed by, and accountable to, the urban poor. The many case studies of schemes that provided low-income groups with access to finance also show impacts that go far beyond what was financed – for instance, new community capacities and new relationships between low-income groups and government or financial institutions. Looked at from the other way, external finance, if provided effectively, can multiply and deepen the self-help activities of low-income neighbourhood associations.

27. See the paper by Ian Morris, with Kim Mullard and Malcolm Jack listed on the back page.

28. See the paper by Diana Mitlin and David Satterthwaite listed on the back page.

29. For a discussion of this, see the paper by Florencia Almansí and Andrea Tammarazio listed on the back page.

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