Expanding Microfinance for Housing

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The purpose of this article is to briefly describe microfinance for housing: the institutions involved, typical loan products, the constraints on its expansion to more meaningful scale, and the greater role it might potentially play in relieving the shelter problems facing the poor, especially the urban poor.[1]

1.0 What is Microfinance for Housing?

Microfinance for housing (MFH) is a subset of microfinance, designed to meet the housing needs of the poor and very poor, especially those without access to the banking sector, including to formal mortgage loans. MFH is designed for low-income households who wish to expand or improve their dwellings, or to build a home in incremental steps, relying on many small loans. MFH differs from formal mortgage lending in two key ways: the loans are smaller and shorter term, but more importantly they are usually not collateralized by the property. MFH clients generally cannot qualify for formal mortgage loans, for a variety of reasons, including low income, informal sources of income, lack of land title (although some microfinance institutions make this a precondition) and a dwelling that does not meet formal building standards. Relative to micro enterprise loans - namely working capital and fixed assets loans to micro entrepreneurs - MFH loans are, in some cases, somewhat larger and of longer duration. Finally, however, housing and micro enterprise loans may sometimes be indistinguishable. First, many micro businesses are conducted in whole or in part from the home, and secondly, many micro lenders have learned that some portion of their loans are being used for housing.

2.0 Who Offers MFH?

The institutions that offer MFH that were surveyed for this MicroNote are listed in Table 1. There are many other institutions, some of which are noted in *Housing Microfinance: A Guide To Practice*, and some of which are included in other tables or in the discussion. MFH is offered by a wide variety of institutions, including MFIs (microfinance institutions), banks, NBFIs (nonbank financial institutions), cooperatives, credit unions, and NGOs. A major distinction can be made between financial institutions whose main product line is micro enterprise loans (MFIs, banks and NBFIs) and institutions whose main purpose is improving the shelter situation of the poor. These are discussed in turn.

Micro Finance Institutions. The MFI group from Table 1 includes **BRI** (Bank Rakyat Indonesia), **SEWA** (Self Employed Women's Association), the **ACCION** network in Latin America, **UML** (Uganda Microfinance Limited), Fundacion, and **FAMA** (Fundacion Para el Apoyo a la Microempresa. **K-Rep**, which offers construction loans for low income housing, and **Jamiibora**, whose main concern is improving the live of slum dwellers overall, would also be included here. Many of the microlenders in the Accion network are banks.

Micro Housing Lenders. The second group, whose primary focus is improving shelter, are often NGOs or NBFIs that have evolved from housing NGOs as "sister" financial institutions conducting the savings and lending operations. This group includes **Kuyasa**, **SPARC**, and **NACHU** (National Cooperative Housing Union) and its housing cooperative members. SEWA and SEWA Bank provide a "sister" example, and although it is a micro lender, SEWA Bank has included housing lending for well over a decade.

There are also several network NGOs providing low income housing solutions, including **Habitat for Humanity** (HFH) and **CHF International**. These groups use business models that seek to offer affordable pricing to the end customers, relying on both sweat equity and continual capital inflow from donations. This model has a strong technical assistance component for the construction of the house. One key challenge for these business models is to achieve financial

[1] This article was prepared under contract to Development Alternatives Inc. for submission to the United States Agency for International Development (USAID). We wish to acknowledge the excellent assistance of Catherine Johnston of DAI and Sashi Selvendran of USAID. Our methodology is first of all, to summarize key findings from an overview published in 2004. See Daphnis, Franck and Bruce Ferguson, eds., *Housing Microfinance: A Guide to Practice*, Kumerian Press, 2004. The MicroNote draws in particular from chapter 3, Alejandro Escobar and Sally Merrill, "Housing Microfinance: The State of the Practice". Second, in order to update this information, we have carried out brief surveys of selected institutions involved in MFH; ACCION surveyed selected institutions in Latin and Central America, while the Urban Institute addressed institutions in Asia and Africa. The views expressed here are not necessarily those of USAID.

Table 1: Institutions Contacted for this MicroNote

Latin America and Central America		Asia and Africa	
Mibanco (Peru)	Bank	SEWA Bank (India)	Cooperative Bank
Banco Solidario (Ecuador)	Bank	SPARC (India)	NGO
BancoSol (Bolivia)	Bank		
Finamerica (Colombia)	NBFI	BRI (Indonesia)	Large MFI
Sogesol (Haiti)	Pilot phase	UML (Uganda)	MFI
Integral (El Salvador)	Bank	Kuyasa (South Africa)	NBFI
El Comercio (Paraguay)	Financial institution	NACHU (Kenya)	Apex for Housing Coops
Fundacion (Santo Domingo)	MFI	Jamiibora (Kenya)	Foundation
Compartamos (Mexico)	Pilot phase	K-Rep (Kenya)	Bank
FAMA (Nicaragua)	MFI,	PRIDE (PRIDE Tanzania)	MFI

FINCA and **PRIDE** are major international networks of microfinance institutions that are thinking of initiating housing lending, and their branches in several countries have recently done so. A recent research project undertaken by FINCA revealed that their clients often use a substantial percentage of their loans for home improvement. To better track the performance of these different segments, FINCA is considering the introduction of housing microfinance products. Similarly, PRIDE is examining the potential for adding housing loans to their product line and acknowledges that some of the money it lends for micro enterprise goes into housing.

sustainability and reduce the dependence on subsidies. HFH is undertaking a strategic reorientation in an effort to increase scale and outreach, focusing on microfinance products such as home repairs/improvement, expansion, and land purchase/titling

3.0 Loan Products, Underwriting, and Funding

Loan Products. As noted above, MFH loans are used for home improvement, incremental building, new construction, at-home production and storage, or home purchase. Accordingly, they differ greatly in value and term. Table 2 illustrates loan terms for selected institutions.[2]

Clearly, loan sizes and terms vary considerably across institutions.

- Based on ACCION's data, home improvement loans in Latin America and the Caribbean typically are short to mid-term loans from 3 months to 36 months, although many institutions offer a wider range of terms up to 60 months or more.
- Average loan size in the Latin American region for 2005 was US$2,800 and ranges from $900 to $3,500.
- Interest rates are in some cases below those for working capital loans and vary greatly from one market to another (for example 24% to 36% per annum is typical).
- Fixed interest rates are the most common; however, BancoSol diversified its housing loan products to include a variable rate product for loans with terms of 36 months or more.
- In Asia, SEWA and Grameen offer up to 10 year loans, but the typical loan is generally of shorter duration, usually 1 to 3 years.
- Housing loans are almost always to individuals, while micro loans may be group-based.

Underwriting. Institutions rely on a variety of additional means to increase the probability that the loans will be repaid, including mandatory savings over a specified period, mandatory membership in savings groups, co-signers, and previous success with one or more micro enterprise loans. Whereas underwriting for a microenterprise loan rests in large part on the institution's assessment of the income stream that is derived from a micro enterprise, not all MFH borrowers may be entrepreneurs, and thus underwriting generally includes a variety of approaches to reducing credit risk. Because South Africa has a credit bureau, Kuyasa is able to undertake a full credit assessment and history. Fortunately, a number of emerging markets are in the process of establishing credit bureaus, which are especially important to microenterprise and housing institutions.

Funding. Table 3 illustrates funding sources for various institutions that offer MFH. Institutions that are registered as banks rely on demand deposits, while NBFIs seek savings accounts. Importantly,

[2] This table is derived from our surveys, from *Housing Microfinance: A Guide to Practice*, and from Franck Daphnis, "Housing Microfinance: Current Issues, Opportunities, and Challenges", a presentation made at the World Bank Housing Finance Conference, March 2006. A "linked" loan refers to the requirement that the borrower must have already successfully completed a microenterprise loan. Housing technical assistance usually refers to construction planning and/or implementation assistance, but for groups like SEWA and Jamiibora, non-housing types of assistance may be offered.

Table 2: MFH Loan Features and Underwriting Requirements

Loan Feature /Institution	SEWA Bank	Grameen Bank	CARD	ADEMI	FUNHAVI	Kuyasa Fund	ACCION Latin America
Loan Size	$333 average; $4,444 max	$100 - $600	$359	$4000	$3000	$700	$300 to $3,500
Maximum Term	120 months	120 months	12 months	36 months	20 months	24 months	120 months
Security	1 yr savings; 2 co-signers	5 co-signers	5 co-signers	Collateralized	2 co-signers	6 months savings	Mostly co-signer
Savings Required?	Yes	Yes	Yes	No	No	yes	No
Linked or Stand Alone	Linked	Linked	Linked	Stand alone	Stand alone	Stand alone	Stand alone
Time with Organization	1 year minimum	2 years minimum	1.5 years	Not required		Not required	Not required
Gender-based?	Women only	Mostly women	Mostly women	No	No	Mostly women	No
Land Ownership	Not required	required	required	Not required	Not required	required	Mostly not
Housing Technical Assistance	Assistance for Illiteracy	No	No	No	Yes	No	Mostly not

Table 3: Sources of Funds

Type of Funding	Banco Sol	SEWA Bank	SPARC	CARD Bank	BRI	Grameen Bank	Mibanco	NACHU	Kuyasa	FAMA
Mandatory Savings		X	X	X		X			X	
Deposits	X			X	X	X	X	X		X
Commercial Credit	X		X				X		X	
Donor Funds		X	X	X		X			X	X
Foundation Funds		X	X	X		X			X	X
Public Funds		X	X							
International Finance Corporation						X				
Credit Enhancement			X						X	

Lines of credit from commercial banks and other financial institutions are increasingly important. PRIDE Tanzania receives commercial lines of credit from the National Microfinance Bank and Azania Bankcorp, both in Tanzania. In other cases, the commercial borrowing is facilitated by credit guarantees. SPARC pioneered the use of a credit enhancement to provide a partial guarantee for a loan from a major international bank in India; SPARC has continued in this approach and currently receives assistance from USAID's credit enhancement mechanism, the DCA (Development Credit Authority). Many of the shelter-focused institutions receive a fair amount of grant and donor assistance in an attempt to make their products more affordable. Kuyasa, as one example, is not yet commercially self sufficient, although it claims to be aiming toward this status; among its sources of funds is a line of credit from a major Pan-African Bank, which is similarly guaranteed by a USAID DCA credit enhancement.

the table illustrates another type of distinction that can be made among institutions offering MFH: (1) microfinance institutions that fund themselves on strictly commercial terms, at market rates, and (2) those that are also subsidized through various combinations of donations, grants, and donor or government funds. Many large microfinance institutions, such as BRI and the ACCION network in Latin America, are self sufficient. Grameen, in contrast, has always received some level of subsidy from donors and foundations.[3] Subsidy funding may take the form of infusions of capital or funds to increase liquidity. K-Reps shareholders, for example, include the IMF, Shorebank, the African Development Bank and two commercial banks based in the Netherlands. Finally CARD, the Center for Agricultural and Rural Development, includes the CARD NGO and CARD Bank, with the goal of providing a group of mutually reinforcing institutions.

4.0 MFH: Demand and Supply

Housing Lending in Perspective. The potential "effective" demand for MFH – that is, loans to households who have the ability to service them as opposed to the need of low income families for shelter - is assumed to be very large. There have been a few efforts to understand customer demand for MFH; for example, **SEWA Bank** began providing housing loans over a decade ago after a customer survey indicated a significant proportion of microenterprise loans were used for housing purposes and other lenders have conducted similar market research. No widespread or definitive study of demand has been undertaken, however. Tentatively, we offer three conclusions:

- There has been significant growth in housing lending by institutions who were already offering housing microfinance, in response to customer demand;
- the number of institutions now offering MFH has been growing steadily, similarly, in response to customer demand;
- overall, however, housing microfinance remains a relatively small portion of the microfinance industry and is still far from reaching a scale that approaches potential demand.

Table 4 offers some figures on MFH portfolios. It is illustrative to look at the recent record of ACCION's network in Latin America. For those institutions offering MFH, loans, ACCION's network achieved a notable advance over the past 3 years, as the housing portfolio jumped from US$38 million in December 2002 to US$117 million in December 2005, an annual compounded growth rate of 49%. For the same period, the growth rate for home improvement loans (which is the primary housing microfinance product) was 51%. By the end of 2005, home improvement lending represented 62% of the housing portfolio of ACCION's network, the remaining 38% being mostly mortgage backed loans or loans linked to government programs, which are usually directed towards somewhat higher income groups.

Those who have been in the business of home improvement lending for more than 5 years, such as **Mibanco** and **BancoSol**, have continued to experience significant growth. BancoSol's total housing portfolio reached 35% of its total portfolio and Mibanco's reached more than 15%. In both cases, home improvement lending makes up around 50% of the housing portfolio. Putting these figures in perspective, within the ACCION Latin American network, however, the aggregate total housing portfolio of all ACCION affiliates is still only 8.7% of total portfolio, which is comprised primarily of working capital credit. The home improvement portfolio (taking out mortgage lending) relative to the total portfolio of ACCION's network worldwide is 5.4 and represents 2.3 percent of total active customers.

SEWA Bank also notes that housing loans have grown rapidly – 55 % in 2005. SEWA continues to maintain a special focus on housing loans, as many low income clients use the house for conducting their business. For **BRI**, although MFH represents only 1 percent of BRI's total portfolio, the magnitude is very large ($85.6 million) as compared with many other lenders, as BRI is one of the world's largest micro lenders, with a total portfolio of over $8 billion. **UML** in Uganda introduced a pilot housing loan project in 2004, and launched the product in 2005. It has already grown to represent 10.6 percent of UML's portfolio. UML feels that its housing lending is limited by lack of medium-term funds. Similarly, **Kuyasa** reports that demand for MFH is very high and it is only lack of access to sufficient funds that prevents faster growth. Kuyasa's new housing lending was over $1 million in 2005, and expectations for 2006 are $1.7 million.

[3] Muhammad Yunus, founder of Grameen Bank in Bangladesh, received the Nobel Peace Prize for 2006, an award which has led to much greater awareness of the microfinance sector. It has also sparked debate about the virtues and drawbacks of strictly "for-profit" commercial microlenders and those who seek to improve affordability by utilizing grant funds or funds obtained at below market cost.

Table 4: Micro Institution Portfolios and MFH Loans

Institution	Total Portfolio 2005	Total MFH Loans	Percent in MFH Loans	% Home Improvement in MFH Loans
ACCION Network offering housing loans	$624,324,129	$116,784,223	18.7%	62%
ACCION Total Network	$ 1,340,000,000	$116,784,223	8.7%	60%
Mibanco	$206,729,374	$30,864,706	20%	50%
BancoSol	$130,106,032	$45,083,923	35%	50%
SEWA	$5,415,555	$1,638,812	27%	80%
BRI	$8,572,000,000	$85,300,000	1%	na
UML	$11,325,366	$1,223,204	10.8%	na
Kuyasa Fund	$2,970,000	$2,970,000	100%	50%

The Supply of MFH: Why Offer MFH? From the perspective of the microfinance industry, the goal of MFH may be primarily to strengthen the institution's business both by expanding its customer base and fostering higher customer loyalty via multi-product financial services. Newcomers to housing within the ACCION Network are also committed to making housing microfinance an important part of their product portfolio such as **Sogesol** (Haiti) currently in pilot phase, **Compartamos** (Mexico) which plans to start a pilot by early 2007 and **El Comercio** (Paraguay), which plans to increase MFH stemming from the results of its successful pilot for house improvement product (Cherogara)

Grameen Bank in Bangladesh also recognized the customer demand for MFH some years ago, and began offering housing loans as "rewards" for successful completion of micro enterprise loans. Grameen recognized the emotional attachment that customers have to their homes for being both the family's shelter and their key asset; thus, MFH builds stronger emotional bonds between the customer and the lending institution, which impacts favorably on the customer loyalty and life time value to the institution. Similarly, **BRI** initiated a study in 2001 in order to determine customer demand for housing loans and the implications for its branches and staff. As a result, MFH has now been solidly introduced by BRI, an institution that takes pains to test and develop its new products and train its regional and branch managers in the new products.

For HFIs concerned primarily or solely with improved shelter and urban development, the entire aim of MFH is to improve the housing of lower income households, to provide loan products to meet the needs of incremental building and home improvement, and to provide an improved base for at-home provision of products and services. **The Kuyasa Fund** in South Africa falls into this category as do the housing co-op members of **NACHU** in Kenya.

Finally, in some cases funding for low income housing is just one part of a broader effort to improve the lives of slum dwellers. **SPARC** in India, for example, seeks to provide assistance for broad efforts in provision of basic infrastructure, multi-family housing, slum upgrading, and informal settlement regularization. It is this latter goal that is now increasingly being designed and piloted by both governments and donors, particularly UN-HABITAT. Finally, **Jamiibora** in Kenya is now introducing housing development into its broad-based efforts to improve the overall well being of slum dwellers; Jamiibora contends that some slum upgrading efforts in Kenya have failed to improve the lot of the very poor, and that land purchase and greenfield construction for these slum and pavement dwellers may be a better answer.

In sum, the major suppliers of MFH include:

- MFIs primarily focused on enterprise loans, that respond to demand from their customers for housing loans and thus develop specific loan products for housing microfinance;
- MFIs that recognize that work and business activities often take place in the home, and that their micro enterprise loans are frequently used for these housing purposes; and
- NGOs and other groups dedicated to shelter, especially those that have evolved to include a sound financial structure or sister financial organization, so that saving and borrowing activities are formalized.

In all three categories, the demand for micro housing loans is apparently growing rapidly. The constraints on its growth are discussed below.

5.0 Constraints to the Expansion of MFH

Has MFH been "over-hyped"? Can MFH be a scale product or will it remain relatively "boutique"? What are the issues in increasing scale? Issues in the supply of MFH and constraints on its growth are discussed here.

Barriers to MFH at the Individual Institution Level

- Lack of awareness of how to implement housing loan products among MFIs;
- Need for increased commercial financing for both MFI and shelter-focused institutions. MFIs should not need to choose between supplying microenterprise loans and as opposed to micro housing loans. MFH may be viewed as risky compared with micro enterprise loans. Shelter focused institutions, many of whom rely on grants and donor assistance, need assistance in designing financially sustainable models. Microenterprise lenders need to obtain sufficient funds so that they are not be forced to make a choice between supplying micro enterprise loans as opposed to micro housing loans;
- Shelter-focused NGOs without an effective financial arm, are too often relegated to a project-by-project approach and the supply of grant funds, and thus fail to achieve scale.

Some Solutions to Institutional Barriers

- Provide technical assistance to help institutions develop housing loan products;
- Demonstrate to MFIs the profitability of housing loans and product diversification;
- Assist housing NGOs and foundations build financial management skills and capacity to engage in housing lending. **Jamiibora**, for example, is just in the process of taking this step;
- MFI friendly regulatory framework, including not setting interest rate ceilings;
- Train loan officers, add multi-product officers and specialists, improve operational efficiency to allow loan officers more time for the credit evaluation process needed in housing.

Barriers to MFH in the Financial Sector.

Major constraints for scaling up housing finance may include:

- A weak financial sector and very limited mortgage finance sector;
- Scarcity of liquidity for most or all segments of the market;
- Asset-liability mismatch. As microloan products are generally fixed rate and short-term for small amounts, institutions have difficulty accessing longer term funds at a fixed rate, given the interest rate risk and duration mismatch;
- A lack of linkages between microfinance institutions, commercial banks, mortgage lenders, and capital market institutions, such as pensions and insurance companies.
- Lack of secondary market financing from capital markets;
- Lack of a conducive regulatory framework for micro lenders that would help strengthen MFI profiles and enable them to obtain lines of credit;
- Legal constraints on borrowing in foreign currencies;
- Lack of resources to hedge currency risk where foreign borrowing is permitted for microfinance institutions.

Increasing competition among mortgage lenders in the upper and middle markets has lead some lenders to begin to look downmarket for portfolio expansion and market share. Latin America and South Africa offer examples of links between commercial banks and microfinance institutions. A major bank in India – ICICI – now securitizes MFI portfolios. Lines of credit help supply liquidity to the micro lender, who is best suited to perform the outreach, underwriting, and servicing in low income communities, while the “formal” sector bank may be better suited to raise funds. Regulation of MFIs is also important, providing more assurance of the viability of the MFI to banks offering lines of credit. The regulation needs to be MFI friendly, however, as too onerous capital requirements, for example, will defeat the intended purpose.

Barriers to MFH at the Policy Level: The Shelter Policy Context

Demand for, and supply of, MFH seem inextricably intertwined in the shelter policy context.

Numerous problems face a country’s ability to supply low income housing, infrastructure, urban land, and proper land titles. However, ***MFH cannot take place in a shelter policy vacuum, most especially without regard to tenure security***. Lack of access to urban land, scarcity of government-supplied infrastructure, government failure to provide timely planning and zoning, and inadequate land titling and registration processes are all major depressants to both supply and demand of MFH. This is nowhere more evident that in the proliferation of urban slums and in the seeming inability of governments to prevent the squatting that leads to major slums.

Tenure Security. From the demand perspective, it is a phenomenon recognized worldwide that households will spend to improve housing if they have land with a sound title. Similarly, lack of infrastructure and a permanent dwelling inhibit incentives for households to improve their own shelter situation. Lack of title and lack of effective title registration systems are serious problems in almost all emerging markets, and in some, these barriers inhibit demand for formal sector mortgage finance as well as MFH. From a supply perspective, many institutions will not lend unless the borrower has adequate title. Note that unlike formal sector mortgage finance the title is not always required; however, demand for MFH is understandably inhibited if a household fears being bulldozed or otherwise relocated.

Without sufficient land and without government supplied infrastructure, low cost housing is especially limited. If the housing supply constraints are extremely serious, housing prices quickly become out of reach of low income households. Often, the middle class “outbids” lower income households for housing actually intended for lower income groups.

6.0 MFH Potential in Slum Upgrading and Shelter Provision.

How Can Microfinance for Housing Make a Difference? The low income shelter problem continues to defy solution from a wide variety of approaches. UN_HABITAT has estimated that one-sixth of humanity – 1 billion people – live in slums.[4] Slum upgrading is now the focus of many national governments, mega-cities, donors, and international organizations, with major efforts being made by UN-HABITAT via SUF – the Slum Upgrading Facility, Cities Alliance, USAID and many other donors. Slum upgrading, however, has its own pitfalls, especially in the context of severe shortages of both housing and serviced land. So-called "rent seeking" behavior results in higher income households simply buying out the lower income groups that the slum upgrading program was designed to assist, while the targeted households often move and once again begin the slum and squatting process. For this reason, Jamiibora's planned housing project will be greenfield, to avoid the turnover process experienced in some of Kenya's slum upgrading programs. Historically, this has been a classic failure of sites and services programs.

What role can microfinance for housing play in this difficult environment? That the private sector, and individual low income households need to play a bigger role - and can play a bigger role - in housing themselves, is now widely accepted. However, MFH is hardly a panacea for lower income groups, especially given the problem of reaching meaningful scale. And, most importantly, MFH needs to be built into a context where its usefulness can be maximized. MFH will be more effective when combined with policies that increase the incentives of households to make the maximum possible inputs into solving their own housing problems. Major synergies can emerge when MFH is combined with secure land title, and basic infrastructure provision in order to maximize household incentives to save and to borrow. Where feasible, government subsidies can greatly assist, but only if provided in a manner that does not conflict with the financial incentives.

Thus, if the problems of land supply, land title, and infrastructure are being addressed with government help, then MFH can potentially play a significant role in supporting the housing portion of the shelter equation. Next, the question should be placed in the context of effective demand: what type of dwelling is involved and what are the affordability constraints of the would-be borrowers? If the stated goal is a *modest dwelling including basic infrastructure*, the ability of MFH to help address the affordability gap could be meaningful for modest income households. It could be somewhat helpful for lower income households. However, MFH could only be supplemental for the poorest of the poor, as they will not have the resources to afford an adequate loan and would need an intervention of public or donor funds to supplement private funding via MFH. Nevertheless, even small loans could be used to upgrade simple dwellings.

Broad-based Shelter Programs with Private, Public, and/or Donor Involvement. MFH has been discussed thus far in a somewhat narrow context - that is, loans to individual borrowers, and for the most part, to improve single family housing. The majority of MFIs provide direct loans to individual borrowers and much of MFH lending is as a stand alone product, not necessarily connected to slum upgrading or green fields housing programs. However, there are also groups that focus on the supply side, for example, working with developers, providing multi-family low income housing, providing construction finance, and providing infrastructure. In our sample, **SPARC** has led the way in this regard, and SPARC's leaders continue to look for ways to increase scale, as well as to provide land and basic services. In the case of **K-Rep**, construction finance is the focus. In the case of **Jamiibora**, there are plans to provide very modest income housing – outside the slums of Nairobi - for which members can offer sweat equity and ultimately purchase or rent. Jamiibora's approach is "holistic", addressing issues of income generation, education, health, and insurance for the very poor.

Should Microfinance Institutions participate in Government Programs? ACCION notes that part of the growth in MFH lending has been fueled by government programs channeled through the microfinance industry. The "Techo Propio" program of the Peruvian government's Mivivienda fund target lower income families and complements the original Mivivienda product which tended to reach higher low to middle income segments. Techo propio showed a potential for success in mortgage loans for affordable houses, with 10,000 customers. However, many microfinance institutions prefer not to rely on government programs mostly due to the risk of being interpreted by end customers that the loans do not need to be repaid and also due to bad experiences dealing with the additional bureaucratic procedures associated with these programs. For example, when residents learned that funds for the Hanna Nassif slum upgrading effort in Tanzania had been provided by the Ford Foundation, there was massive default. It may also be costly for MFIs to comply with the bureaucratic procedures associated with these programs.

7.0 What Can Policy Makers and Donors do to Reduce Constraints on MFH?

Three types of barriers were discussed above: decisions by individual microfinance institutions, the ability of the formal financial sector to help address constraints on liquidity, and failures of overall urban housing policy. In the context of these constraints, there is an immense amount that government policy makers and donors can continue to do to increase the involvement of the private sector, including MHF institutions.

Expanding the Number of MFH Institutions. Policy makers and donors can play a huge role in the process of expanding MFH. First is assistance in publicizing MFH in order to bring more micro institutions into this field. Demonstration projects, toolkit materials,

[4] UN-HABITAT, Human Settlements Financing Division, SUF Brochure: A Guide to Working with the Slum Upgrading Facility.

From the learning obtained about the barriers of getting to scale, we can draw a number of policy implications:

- Private sector actors, including banks and regulated microfinance institutions, have demonstrated their ability to deliver tailored housing products for mid-level economically active poor segments, if the regulatory framework allows free decision about loan product features conditions and credit methodology, particularly about product pricing.
- In particular, housing microfinance based on progressive building fills a critical need for the non-indigent poor and is commercially viable, when done correctly. There are examples of successful housing finance programs that do not rely on any government subsidy and came from private sector innovation growing out of an institution's deep understanding of its clients.
- Government subsidies on the other hand play a critical role in making infrastructure available for the low income households (very poor economically active and the non-economically active), and can be especially effective when done in partnership with private sector actors. Successful government initiatives in low income housing, again, are those that strategically use subsidies to encourage private sector participation.
- As noted above, land titling is a crucial issue: although not all lenders require title, studies are now showing that households are reluctant to improve their units without secure tenure.

training, and technical assistance can help the process.

Improving Formal Sector Mortgage Markets will Assist MFH. A first step is to link formal sector mortgage lenders with MFIs that can benefit from lines of credit. Improving the primary mortgage market, and especially increasing competition, will assist in incentives for these linkages. Second, assist formal sector mortgage lenders to increase their own access to liquidity and longer-term funds through development of secondary market funding capacity; at the simplest level this involves the legal framework for mortgage-backed debt, such as mortgage bonds, and legislation permitting capital market institutions to hold a reasonable proportion of their assets in this form. Alternatively, or in addition, strong microfinance institutions can be assisted in obtaining funds directly from the domestic capital market through bond issuance; as discussed below, credit enhancements can assist this process by sharing risk with the MFIs and providing some comfort to the market.

Improving Microfinance Regulation. Regulation can play an important role. Central banks in a number of emerging markets are establishing regulatory regimes tailor-made for MFI. Regulation and supervision of micro MFI necessitates that they have a prudent and sound capital base as well as transparent reporting and auditing procedures. Both will greatly facilitate lines of credit. For example, **PRIDE** in Tanzania is soon to be registered under the Central Bank's new guidelines for micro institutions and is now undertaking a major reorganization under this regulatory framework, dividing itself into the PRIDE NGO, and PRIDE Microfinance Corporation (MFC). This will begin at the end of 2006 or beginning of 2007. Funding is being sourced from the National Microfinance Bank and other banks in Tanzania and from donors and other sources internationally. PRIDE has specifically stated its interest in microfinance for housing. PRIDE MFC will offer small MFH loans; funding will consist of short-term resources, largely savings deposits. In contrast, the NGO will provide larger housing loans ($20,000 for example).

Credit Guarantees. Credit guarantees can be used in many ways to expand both middle market and low income MFIs or HFIs –from commercial banks, formal sector mortgage lenders, and pension and insurance funds – via guarantees. USAID, IFC, OPIC and others all utilize guarantees to leverage funds and provide financial sector incentives to kick-start a process that should be viable in the long-run. USAID's DCA has been widely used to leverage funds, including in the mortgage market context. IFC may introduce a secondary mortgage market development scheme – the Mortgage Funding Trust - into a number of African countries to kick start the capital market funding process for local institutions. Guarantees could also assist with swaps for interest rate risk or foreign exchange risk to address the issues in fixed vs variable rate lending and borrowing in foreign currency.

Comprehensive Shelter Policies. The discussion in section 6.0 above emphasized the importance of placing MFH in the context of a comprehensive shelter policy,

Azania Bankcorp in Tanzania supports low income lending in a number of ways, lends both directly to micro lenders, including PRIDE, and indirectly via low income housing initiatives, such as the **UN - HABITAT/TWLAT** project. Azania is now the bank facilitating this HABITAT project. In order to implement this project, the Tanzanian Women Land Access Trust (TWLAT) was established by Habitat to assist low-income women to purchase their own home. TWLAT will act as the intermediary between Azania Bank, which has agreed to house a $100,000 guarantee from Habitat, and the women that will be borrowing money from the bank to participate in the project. Houses have been designed for different price ranges, but the intention is for each unit to have 3 bedrooms so that the owner can rent out a room for income generation.

including title, and infrastructure. As mentioned, the **UN-HABITAT SUF** is one key initiative – SUF is described below along with an example from Tanzania. The central objective of the SUF is to mobilize domestic capital for slum upgrading by facilitating links among local actors and by packaging the financial, technical, and political elements of upgrading and low income housing development so that they can attract domestic commercial finance. Along with national and municipal governments, NGOs, and CBOs (Community Based Organizations), SUF's partners include banks, mortgage lenders, MFIs, and institutions making up domestic capital markets. MFH can play an important role in this context, if, as discussed above, the land, title, and infrastructure issues can also be addressed. SUF is now being piloted in Ghana, Kenya, Tanzania, Sri Lanka, and Indonesia.

Viable Structures for more Complex MFH. Finally, it should be noted that the projects that involve building multi-family housing, such as those of SPARC and UN - HABITAT/TWLAT, clearly complicate the process and the role of MFH relative to single family housing. Construction finance must first be secured, and then a number of issues may arise concerning the legal framework of ownership, condominium and coop law, and whether the project's status is for purchase, rent, or rent-to-purchase. Again, policy makers can be of assistance in helping design viable structures.