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Leveraging investment into low-income housing

Tags: Investment, Housing, Land. Case Study

With around 1 billion urban residents living in informal settlements, there is an urgent need to reconsider how development is delivered. This challenge is not just mobilising sufficient finance. It requires rethinking how urban development is structured to create an investment environment where all available resources and capabilities can be mobilised. In a new in-depth study found **here**, ICED outlines how community finance organisations can help to overcome barriers to private-sector involvement in the development of informal settlements.

Research[1] highlights the provision of affordable housing, including for the lowest income groups, as an overlooked opportunity for developers and investors willing to think more creatively about the housing market. There are a number of areas where collaboration between private and community sector organisations could enable development of affordable housing, utilising the networks and resources established by community finance bodies. Beyond community finance the involvement of regional development banks and municipal authorities to underwrite urban development is an area that requires further elaboration. Key to meeting the scale of housing demand is blending the resources of state, community and private sector stakeholders.

One possible opportunity to engage private firms is through the joint development of land for housing development. In many cities of the global South, the development of high-value land in central locations is frustrated by unclear ownership or planning conditions, occupation of sites by informal settlement and the costs associated with resolving disputes to allow development to progress. Where there are multiple layers of ownership and occupation, as found in many informal settlements, it becomes very difficult to negotiate separately with land owners, 'structure owners' who build and rent shacks illegally and tenants. In the Mukuru informal settlement, Nairobi some 92 per cent of residents are tenants and are paying between Ksh 1,500 – 2,000 (US$15 – 19) per month in rent. In large settlements this level of rent income from informal housing can present strong resistance to developers.

Some SDI federations collectively own or control land in commercially valuable city-centre locations. Community groups however, lack the capital to develop their land holdings and are interested to identify potential partnerships for mixed-use land development. Private firms can develop high-yield commercial or residential property on community land in return for capital to develop affordable low-income housing and safeguard space for informal trading opportunities alongside offices and retail.

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[1] McKinsey Global Institute. 2014. *A blueprint for addressing the global affordable housing challenge*. Available: http://www.mckinsey.com/global-themes/urbanization/tackling-the-worlds-affordable-housing-challenge

An alternative approach is through the capitalisation of Urban Poor Funds. As outlined in Section 2, household savings have been pooled to capitalise revolving funds at a city and national scale. These have often been supplemented with public finance and development assistance. Low-income communities can obtain loans from these revolving funds to finance housing, infrastructure and public goods, with interest rates below those offered by commercial lenders.

Box 4: Kinawataka Market Upgrading, Uganda
Kinawataka Market forms part of an informal settlement in the eastern part of Kampala. To improve the environment and performance of the market UPFI was used in 2015 to fund the construction of a sanitation unit to serve the market vendors as well as residents of the adjacent settlement. Negotiations with city authorities secured the release of land and technical support for the communal facilities, which were constructed and managed by the community. The UPFI loan will be repaid over six years using projected revenue from the sanitation unit. The project provided a precedent for partnership working with the city council and has contributed to a wider programme of upgrading in Kinawataka.

To date, the Urban Poor Funds have not sought to attract private finance. However, there are opportunities to secure satisfactory risk-adjusted returns through blended finance. In Malawi, for example, the Mchanga Fund is a revolving fund established by the Malawi Homeless People's Federation and the Centre for Community Organisation and Development (CCODE), primarily to provide housing microfinance. Between 2003 and 2011, it supported 1,583 members (99.5 per cent of whom are women) to obtain loans valued between MWK 70,000 – 140,000 (US$496 - 993). The household also contributes in 'sweat equity' and building materials. Interest is charged at the rate of 12 per cent per annum on reducing balance accrued monthly.[2] The recovery rate exceeds 85 per cent. From the perspective of low-income households, this rate offers a significant improvement over conventional mortgage finance, as the commercial financial sector is often a high-cost lender: the interest rate on loans is 17.5 per cent for owner-occupied houses, 22.5 per cent for commercial premises and 24.5 per cent for other personal or business purposes. Moreover, borrowers from these formal institutions are required to be salaried employees who can produce a pay slip, which excludes many prospective applicants.[3] Capitalising Urban Poor Funds could therefore be attractive to impact investors, allowing them to obtain a market returns while reaching an under-served sector.

The Mchanga Fund in Malawi has provided housing loans to 1,583 people who live and work in the informal sector. It offers an interest rate of 12 per cent per year, compared to 17.5 per cent for commercial banks. Recovery rates exceed 85 per cent.

Most organised communities have a detailed understanding of the local political context and experience of mobilising large numbers of people to engage in, for example, co-production of service infrastructure with local authorities. These constructive relationships mean that communities may be able to negotiate credit guarantees, subsidies or other contributions from the state that can improve risk-adjusted returns from Urban Poor Funds. For example, federations in India and Namibia secured interest rate subsidies for housing loans; federations in Brazil, India and South Africa secured capital subsidies for land development projects; and federations in Kenya, Malawi, Sri Lanka, Zambia and Zimbabwe secured direct land allocations for projects that received investment finance from Urban Poor Funds.[4] In other cases, bespoke services could be linked to a specific development opportunity, for example, to enable the kinds of inner-city mixed-use mixed-income developments mentioned above.

Further Opportunities for leveraging investment into low-income housing

There is strong demand for affordable housing in urban centres that meet the needs of low income communities. Private investment in this sector has been limited by the perceptions of difficulty in delivering schemes and extracting value in contexts where there are established informal settlements. This opportunity can however be realised through collaboration between community and private developers. Grassroots groups

[2] Houston A. 2010. *Housing Support Services for Housing Microfinance Lending in East and Southern Africa: A Case Study of Centre for Community Organisation and Development / Malawi Homeless People's Federation / The Mchenga Urban Poor Fund*. Centre for Affordable Housing Finance in Africa. Johannesburg, South Africa. Available from: http://housingfinanceafrica.org/app/uploads/CCODE-case-study2.pdf?x77297
[3] Manda MAZ, Nkhoma S, Mitlin D. 2011. *Understanding pro-poor housing finance in Malawi*. International Institute for Environment and Development. London, UK. Available from: http://pubs.iied.org/pdfs/10596IIED.pdf
[4] Mitlin D. 2008. *Urban Poor Funds: development by the people for the people*. International Institute for Environment and Development. London, UK. Available from: http://pubs.iied.org/10559IIED/

often have ownership or access to city centre sites that they lack the capital to develop. Organised communities also have local knowledge and capacity to navigate through the complex politics of informal settlements.

There is a range of private-state- community partnership routes to invest in housing that include the joint development of schemes and capitalising Urban Poor Funds. By blending finance and delivery capacity, cross-sector partnerships offer the potential to produce housing and mixed-use development at scale. To advance collaborative approaches the model needs to be developed to demonstrate how housing is produced to be affordable to low income communities and how developer risk is identified and mitigated in order to capture the interest of business. To address this challenge the following recommendations are made.

- Map opportunity sites by identifying land holdings of organised communities interested in housing joint-ventures with private sector. Use the data to broker discussions and new partnership approaches.

- Develop the delivery model focusing on affordability, risk assessment and mitigation. Drawing from evidence of existing schemes, demonstrate how risks have been managed and how this practice could be extended to other contexts.

- Improve access to capital finance. Engage regional development banks and national housing banks to identify whether there are opportunities to establish city level loan guarantees that would enable blending of public, private and community funding for housing development.

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