Framing the Debate: Use of Family Remittances for Housing Finance

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The objective of this paper is to provide CGAP´s Working Group on Housing Finance for the Poor with a framework for exploring how to facilitate the use of family remittances for housing. This paper addresses the potential of these funds for financing housing solutions, what has been learned and where to look for lessons. Finally, it poses questions and areas for research, and recommends where to start.

The Importance of Remittances for Developing Countries

In 2005, developing countries received at least US$167 billion in remittances (see Table 1 for regional distribution), an increase of 73 percent from 2001. Over 50 percent of this increase went to China, India, and Mexico. Although most of these flows originate in developed countries, South-South remittances represent between 30 and 45 percent of the flows reaching developing countries (World Bank 2006).

The impact of remittances on regional and national economies is enormous. Worldwide, in 2004 official estimates placed remittances at nearly the same level as foreign direct investment; moreover, remittances have grown faster than either private capital flows or official development assistance during the past decade. The top 19 remittance-recipient countries receive at least 10 percent of their GDP in remittances (World Bank 2006). In many small developing economies, remittances are greater than total exports. Furthermore, their countercyclical nature can provide economic stability in times of hardship. At the household level, remittances can not only increase but smooth consumption, thus providing social insurance. These flows can also increase savings and investments in education, health, and small businesses. In developing countries, remittances have been associated with decreased poverty levels (Page and Adams 2003, Gupta et al. 2007).

However, the benefits from migration and remittances come at a cost: families suffer from disintegration; economically active people leave their home countries; governments postpone key decisions on poverty reduction because of dependence on remittances; and countries may suffer from inflation. The net impact is hard to estimate.

Even though remittances can have an income redistribution effect given that many reach poor households, these flows do not necessarily reach the poorest (Kapur 2005). According to recent estimates, at least in Latin America, the overall impact of remittances on inequity and poverty has been "quite modest" (Fajnzylber and López 2007). Rather, remittances are creating new patterns of exclusion and inclusion (Serageldin et al. 2004). Finally, remittance flows cannot become engines of development without an enabling environment fostered by appropriate policies, which improve access to social services and financial institutions, among other issues (Orozco 2007, 2006).

Remittances and Housing

In developing countries, increasing the investment in housing by poor households has the potential to leverage the positive impacts of remittances by increasing family assets and overall quality of life. Nevertheless, remittances alone cannot solve endemic problems in the housing sector; they must be seen mainly as an alternative means of payment (Doyle 2007).

The current impact of remittances on housing for low-income households is unclear. Field observations suggest that these households have higher quality homes and home ownership rates than those not receiving remittances (Kapur 2005, Parrado 2004, HFHI 2007). On the other hand, according to Fajnzylber and López (2007), remittances received by these households seem to have a “limited impact” on housing investment in Latin America.

Better data are needed to draw a clearer picture on the use of remittances for the financing of housing by poor households. Current data do not appear disaggregated by income level, for example. Aggregated data suggest that 10 percent of the remittance-receiving families invest a portion of their total income in savings and investments, through mechanisms that include mortgages. Usually these families have bank accounts, which suggest that they are not poor (Orozco 2002, 2006, 2007). Other aggregated data indicate large variability in the percentage of remittances that families invest in housing (e.g., 0.7 percent in El Salvador (UNDP 2005), 16 percent in Indonesia (ADB 2006)). Regarding potential demand in Latin America and the Caribbean, housing investment products are among the most attractive financial products for receivers and senders of remittances originating in the U.S. (Bendixen Associates 2006), and likely from other parts of the world too.

What Has Been Learned

The number of mortgages backed by remittances is still low (Doyle 2006). Remittances are more likely to be used for home improvements than for home purchases, and they are likely to be carried out without the involvement of formal financial institutions. Emphasizing the use of remittances for investment in progressive building, as opposed to the purchase of complete homes, has greater potential for reaching poor transnational families and may encounter fewer implementation barriers (see below; Doyle 2007, HFHI 2007). Furthermore, given that the likelihood of sending remittances drops over time, at least among Latino immigrants residing in the U.S. (Suro 2003), products that require shorter periods of payment may make greater sense (Doyle 2007).

In order to increase investment of remittances in housing, the following barriers need to be addressed (Chaffin et al. 2005; Doyle 2006, 2007; Gómez 2007; Jaramillo 2005, 2007; Mulrooney 2007; Olivares 2005):

- Related to target families: low financial literacy among transnational families and low capacity “to make ‘smart’ housing investments”; distrust of formal financial institutions, especially those in their home countries; remittances intended for housing used for other purposes; in the case of home purchases, deciding in whose name to register the property; lack of collateral or a guarantor needed to apply for a loan.

- Products offered: shortage of appropriate financial products for poor transnational families; shortage of useful strategies and tools for promoting financial and housing products among these families; poor quality control of construction financed with remittances. (These barriers may be related to low availability of information about the nature of the demand.) In addition, providers perceive risk in offering financial products to transnational families.
- Loan application process: gathering information for evaluating risk, and legal and logistic issues render this process complicated, requiring extensive paperwork and involving prerequisites that vary by country of origin. Requisites may include a legal representative in the country of origin and sending payments to that country instead of paying directly in the country of destiny.
- Coordination among players: insufficient coordination among governments, private sector and civil society organizations involved in housing finance and remittance transfer at the national and transnational levels. Increasingly, however, money transfer operators are attempting to partner with microfinance institutions to target housing finance.

Where to Look for Lessons Learned

Relatively few initiatives have specifically tackled the use of remittances for housing finance. Most involve mortgages and are concentrated in Latin America. Among them:

- Sociedad Hipotecaria Federal: with financial support from the Inter-American Development Bank, this Mexican government agency has created a mortgage program to help Mexican immigrants in the U.S. and Canada to invest in new or used houses in Mexico. The program provides long-term funding to three financial intermediaries (including Su Casita) and offers mortgage insurance, among other services. By September 2005, SHF had given 525 mortgages. This program does not specifically target the poor (their average loan is US$55,000), but it has fostered coordination between several government agencies and the private sector, and has implemented mechanisms to work out legal and logistic issues (Olivares 2005). Such mechanisms may not be transferable to countries with inadequate financial systems, Gupta et al. 2007).
- Mi Vivienda (a government program in Peru) and Banco Solidario (a private bank in Ecuador) also have mortgage programs targeting middle-income transnational families. Several banks in India also offer housing loans for improvements and purchase to nonresident Indians (NRI).
- Construmex: this program was created by CEMEX in 2001. It offers credit to Mexicans living in the U.S. for buying, building, and improving homes. Construmex offers financing of up to US$50,000 for purchasing a new home and up to US$8,000 for construction materials. Monthly payments can be made at Mexican consular offices and 800 access points of a money transfer operator. In addition, Construmex offers a list of 4,000 certified distributors of building materials in Mexico. This program has served 8,000 families (CEMEX 2007, 2008).
- Housing fairs: government agencies in alliance with private businesses from El Salvador, Colombia, and Peru have organized fairs in the U.S. to promote housing solutions among immigrants.

- On a small scale, local organizations (such as Habitat for Humanity in El Salvador) are accepting proof of remittances as an income source in qualifying for home mortgages.

Microfinance institutions are also offering products to transnational families, mainly linked to home improvements:

- International Remittance Network (IRNet®), developed by the World Council of Credit Unions (WOCCU), distributed US$300 million in remittances through their members in eight LAC countries and Kenya. A portion of their clients have remittance-backed credits for home improvements and purchase (Sasuman 2005).
- ACCION International is currently running small pilot projects, through local partners, in seven LAC countries, which among other financial products provide microcredits for home improvements (ACCION 2007).

Questions and Areas of Research ,

CGAP's Working Group on Housing Finance for the Poor should consider these questions and areas of research:

- Demand: what amount of remittances are poor transnational families investing in housing and in what types of solutions (e.g., home purchase and improvements)? How do preferences for financial products and housing solutions vary by demographic characteristics (income, urban/rural, ethnic group, country of origin, country of destiny, age, sex, number of years abroad, banking practices)? What segments of the demand are not being satisfied? What is the size of each segment?
- Supply: only a few initiatives have intentionally channeled remittances into housing solutions. Are their efforts reaching the poor? Are they offering the desired products to this population? What lessons have been learned by these initiatives that can help overcome the above-mentioned obstacles? How transferable are these lessons, given the differences in financial systems and other factors? What other initiatives exist? How should suppliers design their products in order to reach additional segments of poor transnational families?
- Delivery channels: what strategies and institutions are appropriate to promote and deliver housing solutions and financial products to transnational families? (A system that offers information about housing solutions and financial products from multiple sources in a given country could increase market efficiency). How can microfinance institutions based in countries of origin offer their services in those countries as well as in countries of destiny? How can immigrants pay for housing products in their countries of destiny?
- Scale and sustainability: what kinds of financial products directed to poor transnational families are cost-effective and can reach scale?
- Community remittances: associations of migrants send donations to their countries of origin. How can these collective remittances be used more effectively to improve the infrastructure in poor neighborhoods?
- Policies and alliances: what local and national policies are needed to build a housing market that serves poor transnational families? What types of local, national, and international alliances are needed to offer these products? What intersectoral alliances are necessary? Participants in these alliances include national and local governments,

for-profit or non-profit money transfer operators, and construction contractors from both business and not-for-profit sectors.

Where to Start?

Collecting information and generating knowledge will help in three areas. First, it will help suppliers design adequate products and promotion strategies for different market segments. Financial products must increase access to housing solutions, emphasizing home improvements over purchase of complete homes. Second, new information and knowledge will help low-income transnational families to choose among products. Finally, governments will be better equipped to devise policies that improve market efficiency and support these families in their efforts to secure decent homes.

Table 1. *Worker Remittances to Developing Countries (US$ billions)*

	2001	2005	Change (%) 2005–01
South Asia	19	32	67
East Asia & Pacific	20	43	114
Middle East and North Africa	15	21	41
Europe and Central Asia	13	20	53
Sub-Sahara Africa	5	8	72
Latin America	24	42	74

Source: World Bank 2006:88.

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