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Singapore Institute of Planners

Investing in Neighbors:

Private Financial Institutions and Slum Upgrading

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Panel D4: Wednesday, September 26, 2007

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Private Finance & Urban Slum Upgrading

Context:

- Six billion people will be living in towns and cities by the year 2050; two billion expected to be slum dwellers (UN Habitat);
- Global poverty will be concentrated in cities that lack physical infrastructure, social and economic services, and political governance;
- Need to create and implement new community-driven models that empower marginalized communities – as few replicable approaches are in place.
- Need to sensitively adapt models to the national/local contexts.
- Need to identify more sustainable sources of finance and link them to processes that are endorsed by local political structures.

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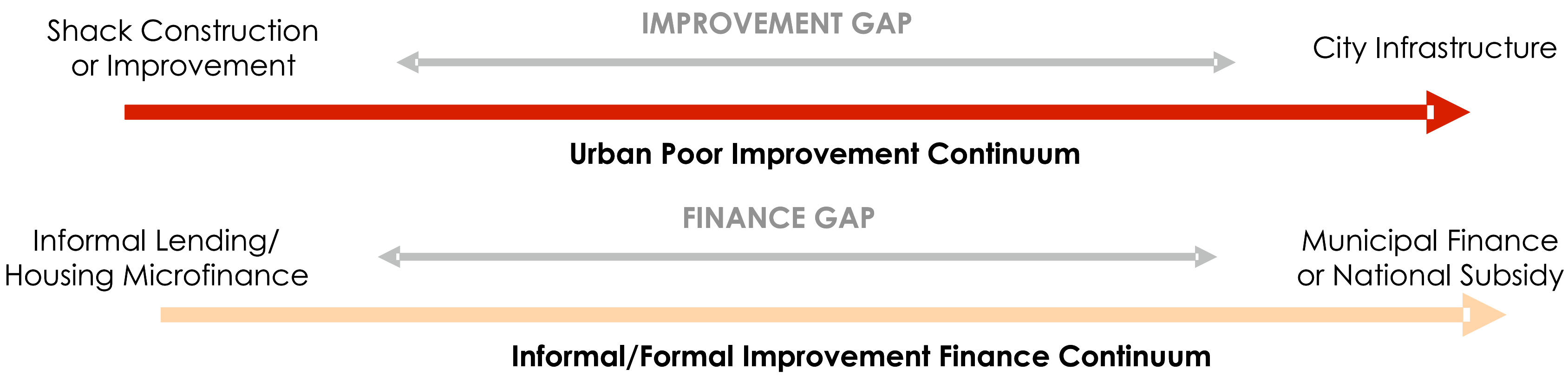
Continuum for Improvements and Finance In Poor Communities

Without available financing, many of these essential, basic improvements may not get made.



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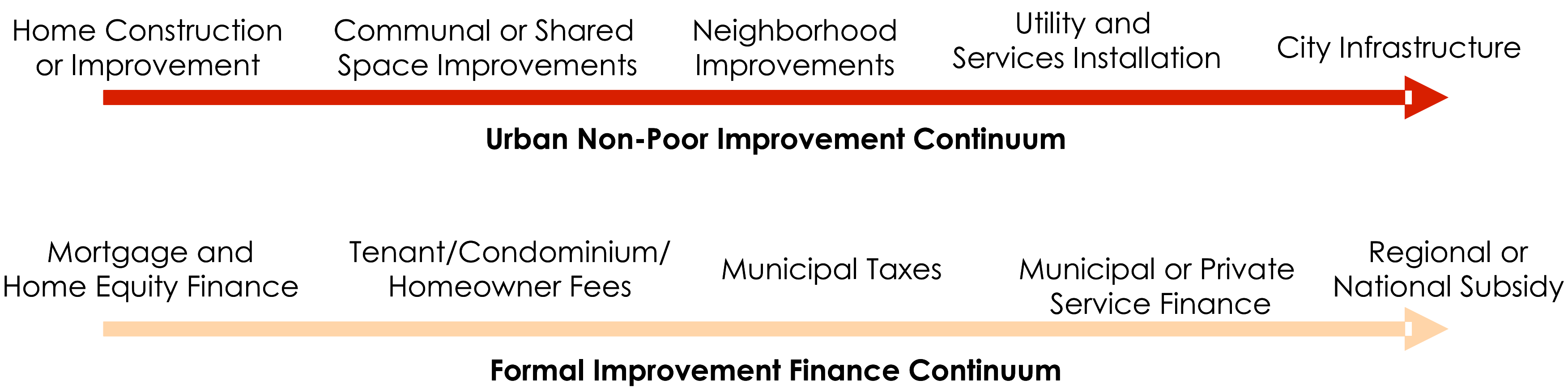
Continuum for Improvements and Finance In Non-Poor Communities

Myriad public, private, and public-private financing schemes available to cities in developed countries for community improvements.



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Basic Premises:

1 - Many recent efforts at slum upgrading have been promoted and implemented by local and national government agencies through defined programs that respond to locally identified needs (i.e., land titling, water services, subsidies). Local political interest/commitment plays a key role in achieving results.

2 – Widespread poverty among slum dwellers impacts the “bankability” of slum communities.

3 – Massive investment in basic infrastructure services is required to provide a decent standard of living in slum communities – far beyond the resources available from the public sector. Private finance will be required to fill this large gap.

Others……..Importance of NGOs, etc.

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Challenge: How to develop private financing mechanisms for slum upgrading that would incorporate a type of group/community approach .

Loan products would probably be oriented in the following manner:

- Client or capital consumer be a group of at least two individuals or households that are currently unserved or underserved; but that can feasibly be "banked" using microfinance loan criteria.
- Use for which the consumers wish to access the finance product be either singular (e.g. one well for a group, road) or multiple (individual house connections to a water main).
- Form of the capital be appropriate to the terms for which the consumers have capacity (typically, modest principal at shorter terms), to the expenses incurred by the provider for originating, monitoring, and servicing (usually resulting in higher interest rates than commercial bank loans), and to the costs of the end use (such as design and construction or land purchase fees).
- Provider of loan services be a microfinance institution, private commercial bank or other source of funding.

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Phnom Penh, Cambodia Water Supply Authority

Accomplishments:

Rapid expansion of its water supply and improved services to urban poor communities.

- Water distribution from 280km of piping in 1993 to 1,400km by 2006.
- Water treatment from 65,000m^3 to 235,000m^3 daily.
- Unaccounted water losses from 72% in 1993 to 8% in 2006.
- Service operation increased from 10 hours per day to 24 hours per day.
- Connections have gone from 27,000 in 1993 to 147,000 in 2006.
- Water coverage of 82% achieved in Phnom Penh.

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Challenge:

Phnom Penh Water Supply Authority wanted to increase access to water services to its urban poor → high connection fee in the form of an upfront payment (~$100) was the critical issue, not the usage/costs of water.

Solution:

Connection fund of US$260,000 was created within the Authority with loan resources from the International Development Association (IDA) of the World Bank; implemented as a loan fund with sliding subsidy component for individual users.

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Finance Mechanism:

- Initially in 1998, Authority provided loans for water connections with repayment in 10 installments and connection made after the first installment (8.5% p.a.). Limited success due to inadequate outreach.
- Improved outreach and longer term repayment approaches improved connections in succeeding years.
- By 2004, a direct household subsidy was introduced to address some households' inability to connect to the water system and their continued need to purchase high priced water from vendors. Subsidies ranged from 30% to 100%. Subsidy decisions were made in consultation with community leaders and through defined eligibility criteria.
- Sliding subsidy was started to reward households with low consumption; in effect, cross subsidizing poor households.

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Lessons Learned:

- Households are willing to pay for basic services (water, etc.).
- Requires financial discipline in terms of initial savings and repayment.
- Relatively low cost per household (~$100) enabled scalability (14,000+ households).
- Sustainability appears to be linked to continued donor funding at concessional rates.
- Active engagement and involvement of community residents achieved through NGOs and Authority staff; with an emphasis on communication and education.

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Community Mortgage Program – Philippines

The Community Mortgage Program (CMP) is a national government program for squatter communities on public and private lands to gain access to land ownership, basic infrastructure and subsequently house construction. Started during the Aquino administration (1986-92) and represented a major housing policy shift from the production of middle income housing towards urban poor shelter needs.

Mechanism:

Provision of long-term, highly subsidized loans to individuals living on squatted lands.

Major Accomplishment:

Financed solutions for 106,000+ families (1991-2001)

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Key Elements/Processes:

- Formation of community association (CA) by residents;
- NGO, local government or national government agency as community organizers and loan originators;
- Sales agreement negotiated between CA/NGO and landowner;
- Long-term highly subsidized government credit program → with generally poor repayment record;
- Community-based, individual loans in stages → (1) lot acquisition, (2) basic infrastructure, and (3) housing construction or upgrading;
- Program financed mostly land acquisition → minimal slum upgrading;
- Savings component served as the trigger to financing;
- Financed acquisition of existing squatter communities or off-site parcels.

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Constraints to Scalability:

- Lack of consistent national government political commitment to a program that put it in conflict with business elites;
- Bureaucratic and slow processing of CMP pipeline projects and lack of transparency in funding decisions;
- Decentralization of the shelter sector to local administrations did not translate into greater efficiencies – often the opposite, as local government housing agencies lack technical capacity;
- Financial resources were limited to government sources (pension funds);

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Lessons Learned:

- Many NGOs require technical assistance to develop their institutional capacity to organize slum communities and originate viable projects;
- Many NGOs lack sufficient funding to sustain their core operations during long project cycles;
- Rising market prices for developable land in urban centers were beyond the financial scope of the urban poor and required deep subsidies in order to finance slum upgrading projects;

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Mibanco – Peru

- Since April 2007, Mibanco began offering a new line of credit titled “urban upgrade”; a loan product designed for self-organized communities looking to bring in water, sewage, electricity, road, and sidewalk networks.
- Loan can cover <90% of the project costs (with a 10% down payment but no mortgage guarantee requirement) for 6 months to 5 years at 25% interest rate.
- Project costs range from US$10,000 to $160,000;
- Total value is divided into individual loans for each community member with Mibanco’s usual requirements for other microfinance clients being applicable;
- Funds are disbursed directly to the project provider (i.e., the contractor, installer, etc.);
- Loan approval comes only after technical plans are completed and signed off on by the local government.

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Genesis – Guatemala

- *Genesis Empresarial* of Guatemala is a microfinance leader in Central America, and has been a sustainable, independent institution for 10 years.
- The Infrastructure and Community Service Loan is a facilityct that provides individual loans for community electricity, potable water, and other basic infrastructure needs.
- In 2000, Genesis had 7,800 active clients borrowing US$120-450 individually at 21-30% nominal rates for 1-4 year terms; $2.4 million infrastructure portfolio.
- Detailed analysis of each member’s payment capacity is made in order to assess the total community loan.
- Loans are administered through groups of four to twelve families, and group guarantees along with one group member's property fulfill collateral requirements.

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CEMEX Calle Digna – Mexico

Key Elements:

- Linked with the CEMEX Patrimonio Hoy home improvement program; private sector and community residents have incentivized local governments to upgrade public infrastructure.
- Calle Digna allows organized community partners to make weekly payments for public improvements (cement and other materials) to their neighborhood streets.
- The city government pays a matching amount that includes the costs of labor and engineering.
- CEMEX loans the building materials so that construction can begin 18 weeks after the community members begin making weekly payments.

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Elements for Improving Access to Community Services and Upgrading Slums

- Using credit as a means to afford better quality services and spread costs over a longer period of time;
- Recovering costs for users and revolving these resources back into other improvements.
- Reducing the cost of housing and infrastructure through appropriate technology, modifying construction standards, and/or through "sweat equity".
- Strengthening community organizations to increase their capacity to improve conditions and to negotiate with external agencies.

(Excerpt from Mitlin & Satterthwaite, Empowering Squatter Citizen)

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Elements for Improving Accessing to Community Services and Upgrading Slums

- Structuring investments to cover incremental, progressive improvements.
- Share costs where possible with other actors.
- Focus on supporting "bottom up" community-driven approaches that are reflective of local needs and capacities;
- Local government agencies responsible for urban development, infrastructure and housing need to play an enabling role.
- Careful use and targeting of government subsidies;