Role of UN-Habitat in Finance: ERSO and SUF Programme Lessons Learned Options for the Future

Report to CPR Working Group on ERSO
20 September 2010
Global Need: Housing and Infrastructure Gap

- UN-Habitat estimates that over 1 billion people live today in substandard conditions, lacking access to:
  - Clean water
  - Sanitation
  - Adequate bathing or cooking facilities
  - Clean, comfortable, safe homes
- The problem is most acute in emerging and frontier economies of the Global South
- This adversely affects families, communities, economies, public health and the environment

Closing the Global Housing and Infrastructure Gap

- In Global South communities, family or group savings can cover between 5%–20% of the cost of bringing water, sanitation, roads, utilities and better housing to a community
  - Savings alone will not close the gap
  - Government home building programs alone have not closed the gap
  - Reliance on private sector mortgage lending has not closed the gap
- What has UN–Habitat’s recent finance experience shown about how we might close the gap?
  - Principles and lessons learned
  - Options for the future
- We welcome your ideas and input
Executive Summary on ERSO: Principles and Lessons Learned

ERSO positive principles
- Effective to run a first loss, early stage investment fund
  - $3.6 m fund stimulating $625m in investment in 6 pilots
  - Facilitating structures with major IFI’s like IFC, KfW, IDB
  - In 16 countries in Asia, sub-Saharan Africa, Latin America
- Guarantees are highly cost-efficient for donors
- Guarantee structures and scaled PPP investment programs have broadest impact in host countries

Key lessons learned
- Need financial expertise to run a lending program
  - A separate fund management structure (like UNCDF) would be optimal
  - Can combine grant and early stage lending
  - Will provide transparency and quality needed for donors, investors and host country partners

Executive Summary on SUF: Principles and Lessons Learned

SUF Positive Principles
- Guarantees attract private sector lending to well–designed slum upgrading projects
- Best projects are: toilet blocks, market stalls, community kitchens, bringing informal housing to code, neighborhood paving and lighting
- Effective when combined with muni government and community input and savings

Key lessons learned
- Expensive to implement program alone and from scratch
  - $5.5 m to LFF’s will support $14 m total investment in 4 countries
- Close partnership with municipalities is the most efficient delivery mechanism
- Need financial structure safeguards to prevent diversion or ineffective application of funds
- A formal fund structure combined with an expert credit team would help to manage grants as well
Executive Summary
Next Steps in Evaluation

- ERSO Programme
  - SMC meeting October 2010 in Spain
    - Review of proposed final ERSO pilot with IFC, KfW, SIDA et al.
    - Advice to ED on lessons learned
    - Attendance by external evaluator (to be selected by M&E after TOR and public advertisement posted this month)
    - Chairman of CPR, Chair of G77, China and all SMC members have been invited

- SUF donors meeting October 29th in Nairobi
  - To be followed by formal evaluation of SUF programme

- Evaluation reports mid–November to December

- UN–Habitat Management Response following

- Executive Director’s Report to Governing Council for April 2010 meetings

Background: UN-Habitat in Housing and Project Finance

- What types of pilot programs have been tried?
  - Revolving loan fund program (ERSO)
    - 6 pilot loans of different types
  - Local market credit enhancement (SUF programme)
    - 6 Local Finance Facilities in 4 countries
  - Grants (SUF programme)
    - Multistory building construction and reconstruction
    - Seeding a MFI
    - Grants to community funds

- Who is the target population served?
  - In emerging markets, 70th to 85th income deciles
  - In frontier markets: from 30th to 85th income percentiles
  - The poorest of the poor cannot borrow unless and until their income generating capability is increased
Lending Experience: ERSO

- ERSO experimental revolving loan fund
  - Reviewed over 40 project proposals since 2008
  - Closed 5 pilot loans to local housing lenders and apex organizations from July 2009–March 2010
- Final pilot being structured for target closing by April 2010
  - Global Micro Housing Facility with IFC, KfW, SIDA, Cities Alliance, UNCDF
- Opportunities to increase impact in water:
  - Water hookup finance pilot with IDB, ProCredit
  - WOPS and water plant upgrade finance review with IFC, KfW and USAID

Lessons Learned from ERSO

- Standalone loans (UN–Habitat only) have low volume impact
  - Can show effectiveness of partnership between local lenders and municipalities
  - Example: DFCU (125 homes plus infrastructure)
- Muni loans to aid area development projects produce greater impact and strengthen local governments
  - Depend on local governments to execute
  - Example: Azania (2800 homes plus infrastructure)
- Loans to apex NGO’s also have greater impact
  - Lengthening tenor of micro housing loans
  - Especially effective as part of a capital structure development strategy
  - Examples: HFH Nepal; Prodel (broadening national programs)
Lessons Learned from ERSO

*Public-private partnerships* with local banks and IFI’s produce **even greater impact**
- Need donor guidance and government support to focus on reaching down to 85th percentile
- Example: AMAL: 30,000 units

*Guarantee programs in PPP format with IFI’s produce the greatest impact most efficiently for donors*
- Example: Pending proposal with IFC, KfW, SIDA, Standard Chartered Bank
- Supporting expansion of micro housing and community project lending to MFI’s in 15 countries in SSA, Asia

*Offering long term secondary finance supported by guarantee* is more effective than direct interest rate subsidy (as in early ERSO loans)

Lessons Learned from ERSO

*Sustainability*
- Present ERSO structure (branch of operating division) not optimal
  - Does not attract sufficient donor funding
  - A struggle to operate internally
- Better to use formal fund structure with separate, transparent fund accounting (like UNCDF, NMI, World Bank or IFC Trust Fund, etc.)

*Goal should be:*
- To make small but catalytic investments in housing and infrastructure finance
- To stimulate involvement of IFI’s and private sector
DFCU Bank, Uganda: ERSO Loan

- **COMMUNITY DEVELOPMENT PROJECT FINANCE** with government and private banking and private bank takeout mortgage finance
- **Partners:** Ministry of Land, Housing and Urban Planning, Tororo Municipality, DFCU Bank, Kasoli Housing Association
- **Loan type:** Institutional loan to DFCU for construction finance and then lending to end-users mortgage finance
- **Land:** Government land under trusteeship of Tororo Municipal Council currently occupied by 125 families.
- **Developmental aim:** Developing 125 secure tenure houses in Kasoli, Tororo Municipality
- **Housing stock design:** Ministry of Housing
- **Project Team:** DFCU Bank, Ministry, Tororo Municipality, Kasoli Housing Ass’n

AZANIA Bank, TZ: ERSO loan

- **MUNICIPAL LOAN for peri-urban development**
- **Partners:** Azania Bank; Mwanza Municipal Council (MMC)
- **Project type:** Development of area presently occupied by low-income families informally near the lakeside in Mwanza to create mixed use, formally titled site and services development
- **2800 total plots**
- **Land:** Development by the Mwanza Municipal Council.
- **Target Group:** 700 middle income and 2100 lower income sized plots. National government compensates current inhabitants and they are offered first refusal rights to formal plots
- **Type of transaction:** ERSO loan to Azania for physical land survey and provision of water, electricity in Phase 1
Habitat for Humanity Nepal: ERSO loan

- **Partners:** Habitat for Humanity International Nepal, NGO
- Habitat for Humanity International
- **Project type:** Community development loan to HFHI to be onlent to 11 credit cooperatives/village banks, which will lend the funds to *Save&Build* groups of 12-18 people for incremental building/renovation
- **Target Group:** low-income dwellers
- **Number of units created:** 885 houses built/upgraded with potential program expansion to 1,765 in total
- *Save&Build* methodology allows every family benefit in cycles of saving and borrowing
- Potential future expansion to other HFHI affiliates

Programa de Desarrollo Local (PRODEL), Nicaragua: ERSO loan

- Created in 1993 with SIDA funding and support to finance infrastructure, housing and micro-finance products throughout Nicaragua
- To date approximately 100,000 families have benefited from Prodel activities
- $500,000 Working Capital Loan to Prodel to finance:
  - Infrastructure development,
  - Secondary lending to local MFI’s
  - Support microfinance housing loans in up to 16 small to medium-sized regional cities in Nicaragua and Central America
- Ongoing advice to augment capital structure
Affordable Mortgage and Loan Corporation, Palestine: ERSO Loan

- **SCALE PRIVATE SECTOR CONSTRUCTION and long term IFI-FUNDED MORTGAGE FINANCE PROGRAM**
- **Partners:** Palestine Investment Fund, OPIC, IFC, Bank of Palestine, Cairo Amman Bank, DFID, Aspen Institute’s MEII, CHF International, and World Bank Technical Assistance
- **Project type:** Large-scale affordable housing programme providing up to 25-year fixed-rate and 5-year adjustable-rate mortgage financing
- **Target Group:** Low to middle-income Palestinian public sector workers, teachers, nurses.
- **Number of units:** 30,000

Global Micro Housing Facility Pilot

- Possible final ERSO investment on or before April 2010 – to be reviewed by SMC in October, 2010
- **Initial participants:**
  - IFC (co-lead in guarantee facility)
  - KfW (co-lead in guarantee facility)
  - SIDA (guarantee support; TA)
  - Cities Alliance (policy linkage)
  - UN–Habitat (investor through ERSO program, participation in structuring)
  - UNCDF (MFI network, TA)
Global Micro Housing Facility
Potential Virtual Fund Structure

Donors - $10 m coverage of 4-5 defaults
Guarantee or through Trust Fund

IFC/KfW - $50 m
Maximum guarantee amount
Pari Passu with Standard Chartered up to [70%]

Standard Chartered Bank - $75 m
bears [30%] loss exposure
pari passu with IFC, KfW

- Pillar 3 team develops
  eligibility criteria, monitors performance
- Bank extends loan to MFIs
- MFIs extend loans to clients and take x% of risk

Micro Housing clients

Reimburses SCB for defaulted MFI loans pro Rata
- Select MFIs
- Extend guarantee for x% of each MFI loan
- Reimburse SCB when First Loss Fund has been depleted

SUF Experience, Lessons Learned

- Designed and funded 6 Local Finance Facilities
  - 4 are functioning
  - 2 (in Indonesia) are sustainable in long term due to close association with municipalities

- Grants made under SUF programme
  - To launch urban poor funds and an MFI
  - To pay for construction projects (Tawlat, Mavoko)

- Lessons learned
  - LFF’s are sustainable when closely linked to municipalities
  - Community groups cannot manage large construction projects without extensive external help
  - Savings and lending alone are not enough to finance new building for low income communities
  - Lack of financial plan stymied Mavoko project
  - Urban poor fund grants must be supervised
Where do we go from here?

- We have had preliminary discussions in house
- We are not yet ready to make a recommendation
  - Need time to reflect
  - Need opinions from evaluation and from country experts
- But wanted to share thinking at this stage
- Ask for your input
- And come back for further dialogue

Where do we go from here?

- Option 1: Eliminate finance programs at UN-Habitat altogether
  - Would remove programs causing controversy in the past with Governing Council, CPR and donors
  - But also removes chance to
    - Benefit from lessons learned
    - Use expert financial team now assembled

- Option 2: Design new UN-Habitat finance program in fund format
  - Independent structure like UNCDF–UNDP relationship
  - Would build on programs carried out to date
  - But may not be a comfortable fit for UN–Habitat
    - Would require separate structure, budget, administration
    - Would require full financial transparency on portfolio performance
Where do we go from here?

- **Option 3: Partnership option**
  - Create partnership between UN-Habitat and new specialty fund located outside UN-Habitat
    - Would preserve value of work done to date
    - Would provide a more expert and robust platform for lending activities.
    - Would accept current ERSO portfolio
    - Would allow for ongoing collaboration between financial services team and WSIB, Global Division and RTCD
    - Would need careful exploration to assess potential new platform

Where do we go from here?

- **Partnership and Partnership Fund Examples**
  - **UN Capital Development Fund (UNCDF)**
    - Discrete fund with ED reporting to head of UNDP as the fund’s managing director
    - Focus on Microfinance and Local Government
  - **Norwegian Microfinance Institute**
    - PPP supported by Norway and 4 private sector investors
    - 2 funds plus TA facility through NorAd
    - Focus on Microfinance
  - **Cities Alliance**
    - Focus on housing and urban infrastructure and slum upgrading
    - Could link with WB or IFC Trust Funds
Homes, Neighborhoods, Happiness

- Homes and neighborhood infrastructure relate to many MDG’s
  - Health and education
    - Clean water cuts infectious disease risk
    - Less crowding reduces infection, AIDS, TB
    - Cement floors cut disease, improve health and school and work attendance
  - Economic development
    - Construction work a great economic stimulator
  - Gender
    - Women clean, cook, and run businesses from the home
- Can we work together in some way to get more improvement to more homes and neighborhoods?
- Thanks for your attention and your support