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Overseas Private
Investment Corporation

Challenges in Affordable Housing Delivery

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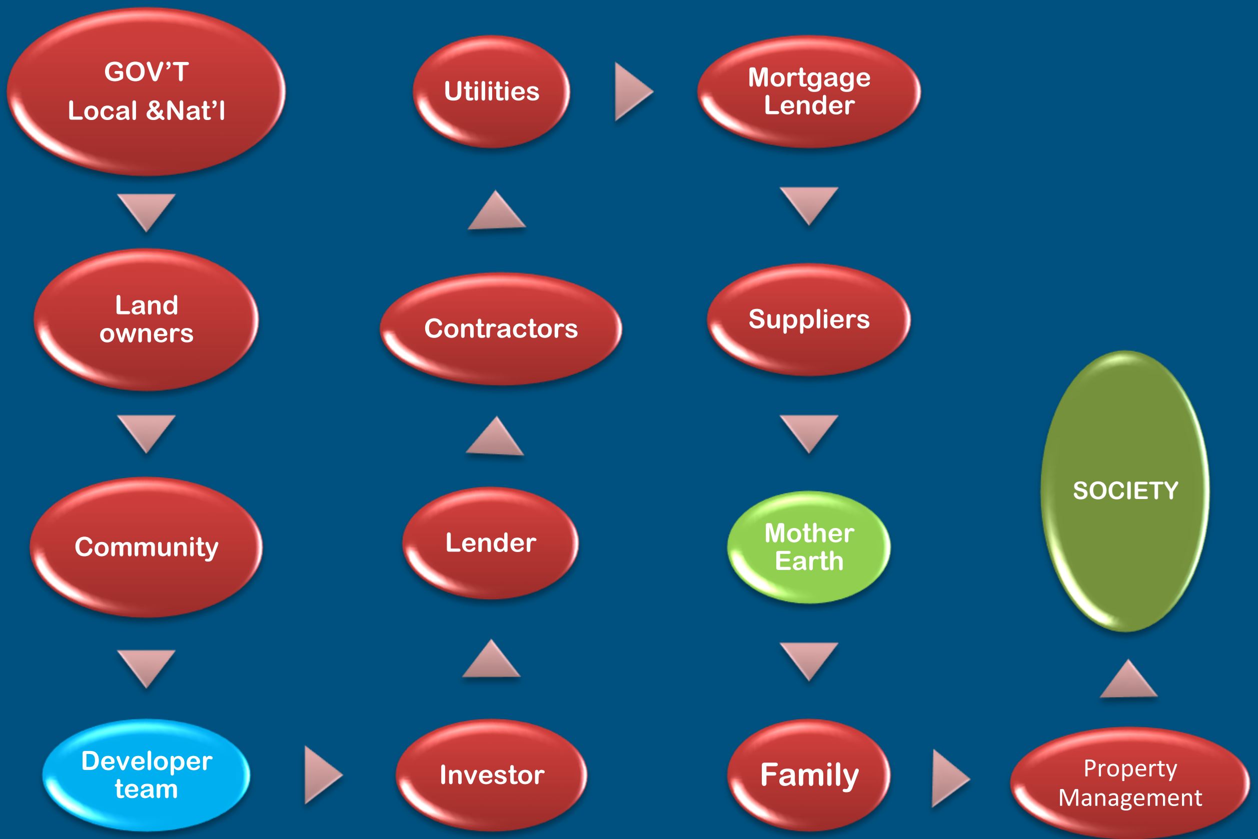
Outline

1. Quick view of housing ecosystem
2. Ecosystem weakness in emerging markets - systemic
3. Housing developer/builder capacity limitations – private sector
4. Financing limitations – banks and DFIs, long term capital
5. Case study in Honduras and lessons learned
6. Suggestions for better success

Value Chain Model



Systemic barriers to affordable housing development

Public policy must be coordinated to support supply *and* demand concerns

Supply barriers

- ✓ Coordination between national and local governments impeded by politics and competing mandates – lack of institutional continuity on which investors and beneficiaries can rely
- ✓ **Lack of affordable land in and near city centers with access to services, jobs, schools**
- ✓ Lack of financial incentives (e.g. tax) for builders of entry-level product
- ✓ **National affordable housing initiatives that are not supported with budget resources for long term implementation**
- ✓ Lengthy and costly zoning, permitting and entitlement processes
- ✓ **Public policy (subsidies) often focused on ownership rather than rental**

Demand barriers

- ✓ Informally employed do not have access to standard mortgages
- ✓ **Lowest income families cannot save for downpayment to purchase or commit to long term debt obligation**
- ✓ Lack of long term debt vehicles to finance mortgages or income property investment
- ✓ **Limited programs to subsidize monthly rent or mortgage costs for lowest income families**
- ✓ Low acceptance of "social" housing given poor location and quality
- ✓ **Apparent unwillingness of families to accept alternative building tech that would be lower cost and more sustainable**

Private Sector Limitations

The sheer scale of need requires mobilization of more and *different* capacity

Operational Capacity

- It is very difficult to efficiently deliver large scale housing in unpredictable macro environment
- Lack of market data to plan
- Investment in technical innovation is limited in this sector
- Municipal utility capacity cannot keep pace with rapid development
- Affordable housing competes with more profitable segments
- Tendency not to differentiate product among sub-markets, "one-size-fits-all" mentality
- Overall lack of professional housing developers specializing in affordable
- Community sustainability must be considered and accounted for in development plan – not normal role for builders

Financial Capacity

- Better cost management and budgeting is required
- Assumption that low prices means low profit margin (not true) means builders avoid this segment without gov't offtake
- Lack of liquidity among developers and contractors to take on large scale projects
- Local banks not familiar with project finance structure which limits access for small/medium builders
- Sector viewed as high risk for equity and debt providers
- Lack of market transparency and unpredictable processes causes delays and creates hidden cost that is difficult to budget for.

Financial Sector limitations

We are seeing more attempts to adapt microfinance models to lowest income housing needs – live/work developments, incremental construction, micro-utilities – but they are not easy to finance

- **Local currency, affordable mortgage loans** are still very difficult to obtain, given high interest rates and lack of local sources of long term capital.
- **Downpayment subsidy programs (eg Panama, S. Africa)** have been very effective at attracting large numbers of entry level buyers to new homes.
- **Tax credit and specialized bond** instruments (Malaysia, Panama) have succeeded in attracting long term investment into the mortgage sector.
- Directing investment from **pension funds** into mortgages and housing projects through regulatory effort requires very prudent management and credit infrastructure. Efforts to develop instruments suitable for pensions in Africa are underway.
- **Micro-finance and incremental, participatory funding** for housing construction is an interesting approach that may be challenging to scale. Partnerships with community organizations are key for these programs.
- **DFIs have had limited success in project finance for housing** given the lack of qualified developer/builders. **India, Mexico and Brazil** are examples of some successes, but also significant failures with over-building and macro-economic volatility.
- **Private equity firms** have invested in middle income housing, and beginning to invest in rental housing, but very limited interest in true entry-level projects. Return expectations are higher than achievable in social housing sector.
- **Social impact funds** present new opportunity to match low return expectation with affordability target and social goals. Will need to overcome concerns about housing sector risks, lack of experience with those investments.

OPIC Case Study:
Castaños de Choloma
Honduras

Typical neighborhood in Choloma

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The Choloma Valley – highest risk area in Honduras

- Goal was to address both Supply and Demand issues – build houses and provide lease/purchase financing
- Included live/work units. 37 – 42m
- Development plans included drinking water, waste treatment, power, roads, security, community services
- Well located – near San Pedro Sula and town of Choloma
- Income target 2-3X minimum wage (~$200 per month)
- Other value added – home owner’s association, small business support, neighborhood watch, daycare, sports fields, playgrounds
- 3,500 houses planned

The elementary school

The U.S. Government's Development Finance Institution

Lessons we are applying today

- House price $13,000, payable over 25 years with $150 deposit
- 1,800 units built and occupied
- Very strong safety record in the community, strong commitment by developer to maintain community
- USD payments not sustainable after GOH delinked lempira from Dollar – trying to convert to local currency
- Lease purchase program deemed “ineligible” for homebuyer subsidies
- Roof remediation required (inadequate insulation) added developer cost
- Significant payment delinquencies developed
- Discussions with housing ministry are ongoing

- Inexperienced homebuyers did not understand their contract or their obligations.
- 25 year payment plan did not show equity build up quickly enough
- Continued commitment of developer in the community was key to sustainability
- Must have a local currency financing plan
- Subsidy program must be established and transparent
- Quality cannot be sacrificed for cost
- “mini-communities” within the larger development were key to develop sense of ownership and connection
- The school was critical glue for community and attraction for new residents
- Security was paramount for community sustainability in high risk region

Our affordable housing strategy

Support high quality developers	Find companies that are doing it right and encourage them to push affordability further.
Catalyze long term funding	Provide long term financing for entry level rental developments; actively encourage local pensions and insurance companies to invest in mortgages.
Mixed income projects	Cross- subsidize lower income housing with middle and upper middle, using models from developed countries.
Resource efficiency	Energy, water and other efficient uses of resources are necessary for long term affordability. Actively encourage new technologies to achieve this.
Community sustainability	Builders must build more than houses – and ensure that a completed development contains what is needed to succeed as a community.
Credit enhancement	Use our guaranty to credit enhance instruments to attract new investors to the affordable housing sector.
Urban, accessible	Large scale housing projects outside of city boundaries are not sustainable without long term access to jobs, schools, health care, shopping and social networks.

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