Overview: - Financing for the urban poor

*The way housing and urban infrastructure are financed is a topic of renewed debate and a source of creative innovation, write **Chris Williams**, Political Advisor, and **Nicholas You**, the Special Advisor on Policy and Strategic Planning, both in the Office of the Executive Director at UN-HABITAT. Here they examine financing in Africa, Asia and Latin America, where the demand for shelter and basic services far outstrips supply, and where most urban populations live in slums.*

In an era of neo-liberal economics predicated on market-led growth, interest in financing reflects recognition of the limits of public expenditure. It also reflects the failure of public planning and delivery systems to keep pace with rapid urbanization. It further reflects the initiatives of non-State actors to increase the supply of housing and infrastructure in the absence of adequate public intervention.

The shift in emphasis from public to private sources of finance raises questions about the role of the State in housing and urban development and, by extension, about the future policies of international development cooperation agencies and financial institutions.

Most member States in the developing world experienced in the 1970s an economic and political crisis that led many to implement structural adjustment policies in the next decade. Governments devaluing their currencies to promote exports, eliminated price supports, aligned their economies with global markets, cut public expenditures on social services, privatized state-owned enterprises, and liberalized financial markets. National housing corporations in many countries either collapsed or scaled back operations. Public expenditure on housing dropped, as did public investment in urban infrastructure. By the 1990s, public finance for housing and urban infrastructure was all but eliminated, save ad hoc programmes of development cooperation agencies and NGOs designed to minimize the social consequences of structural adjustment.

The advent of rapid urbanization coincided with economic crisis and structural adjustment. First in Latin America, then in South and Southeast Asia, and more recently in Africa rural-urban migration combined with population growth to increase the size of cities. Urbanization without requisite economic growth resulted in urban unemployment; urbanization without public services resulted in inadequate shelter, water and sanitation; urbanization without economic growth and public services resulted in the urbanization of poverty and slums. Municipal authorities barely capable of meeting their payrolls, were vulnerable to corruption, unable to collect revenues, or plan, let alone finance the burgeoning housing and service needs.

The demand for services in the absence of public supply created two types of innovation and corresponding sources of finance: Private entrepreneurs who saw in slums a business opportunity and urban poor organizations keen to improve their living and working conditions. The entrepreneurs built shacks without services for rent, or provided unofficial services (water, credit, sanitation, electricity, security, etc.). Rates were calibrated on capacity to pay, small unit provision, high unit cost, and on high volume. The organized poor mobilized savings and acted collectively or individually to secure land, build homes, and gain access to services. Micro-finance institutions emerged to offer credit to entrepreneurs and the organized poor. Rather than rely on public finance, slums generated investment, fostered rent-seeking opportunities and offered a source of cheap labour to industry, upscale residential neighbourhoods and the central business districts.

The combination of structural adjustment, rapid urbanization, weak municipal planning and services, and a distinct slum economy has created conditions for radical changes in the formal private sector – and hence, a new source of finance for housing and urban infrastructure. The banking sector and private utility companies are two important examples of finance. The flip side of structural adjustment has been that banks have grown in number with the advent of market liberalization, privatization and related financial sector reforms.

While many banks have confined lending to traditional, higher-income markets, others have diversified lending to reach rapidly growing urban populations, building upon precedents set in slums by entrepreneurs and urban poor organizations. Innovation of this kind has been accelerated by competition among banks for traditional, higher-income markets, the lucrative business of micro-finance, and downward pressure on interest rates. Primary mortgage institutions have also emerged especially in countries with established domestic capital markets that can subscribe to debt instruments as a source of long-term financing so essential for housing finance.

For private service providers, structural adjustment has had unanticipated consequences in countries with rapidly expanding urban populations. Privatized utility companies see in slums a large, untapped market—a population of slum dwellers who pay more per unit cost of service than higher income households. By working with entrepreneurs and urban poor organizations, private utilities are developing innovative systems to extend their services to slum dwellers and the urban poor.

The shift from public to private sources of finance for housing and urban infrastructure in cities of Africa, Asia and Latin America would suggest that governments no longer have a significant role to play in financing human settlements development. On the contrary, the role of the State has never been more pertinent. Only government policy, public investment and municipal planning can ensure financial sector reforms that translate into private investment in affordable housing and basic services.

Government legislation on pension funds, for example, can create a source of long-term capital and trigger institutional investment in debt instruments to finance municipal infrastructure and/or mortgage facilities. Targeted public investment is also crucial. It is estimated that 30 percent of the cost of home construction is made up of expenditure in water and sanitation. By dedicating public expenditure to infrastructure, the State can spur massive private investment in housing—a volume of shelter hundreds of times greater than could be constructed by government funds. Municipal planning is a pre-requisite for mainstreaming private investment, particularly approaches to planning that build upon, rather than exclude the dynamism of the slum economy and the integral role it plays in urban development.

The change in the way affordable housing and urban infrastructure is financed at country level has significant implications for development cooperation. Official development assistance will never finance the massive housing and service deficit in cities in Africa, Asia and Latin America, nor should it.

The accumulated savings and purchasing power of urban poor and the capital housed in pension funds and among private investors as well as dedicated public investment constitute sources of finance that make official development aid pale by comparison.

The future of development cooperation is to channel funds in ways that accelerate the actions of local actors to harness these sources of finance. This includes a combination of targeted technical assistance and credit enhancements, equity investments, and bridging finance that preferably can build local capacity and leverage multiple sources of finance.

It also involves creative partnerships between multilateral and bilateral development agencies and international finance institutions geared toward fast-tracking investment for infrastructure.

More fundamentally, development cooperation will require coming to terms with the social and economic consequences of rapid urbanization and addressing urban poverty by drawing on the potential of innovations in financing.

Commitments on shelter finance, Habitat Agenda, 1996

Paragraph 47 of the Habitat Agenda commits member states to:
"… strengthening existing financial mechanisms and, where appropriate, developing innovative approaches for financing the implementation of the Habitat Agenda, which will mobilize additional resources from various sources of finance – public, private, multilateral and bilateral – at the international, regional, national and local levels, and which will promote the efficient, effective and accountable allocation and management of resources, recognizing that local institutions involved in micro-credit may hold the most potential for housing the poor."

Paragraph 48 of the Habitat Agenda commits member states to:

(a) [Stimulating] national and local economies through promoting economic development, social development and environmental protection that will attract domestic and international financial resources and private investment, generate employment and increase revenues, providing a stronger financial base to support adequate shelter and sustainable human settlements development.
(b) [Strengthening] fiscal and financial management capacity at all levels, so as to fully develop the sources of revenue.
(c) [Enhancing] public revenue through the use, as appropriate, of fiscal instruments that are conducive to environmentally sound practices in order to promote direct support for sustainable human settlements development.
(d) [Strengthening] regulatory and legal frameworks to enable markets to work, overcome market failure and facilitate independent initiative and creativity, as well as to promote socially and environmentally responsible corporate investment and reinvestment in, and in partnership with, local communities and to encourage a wide range of other partnerships to finance shelter and human settlements development.
(e) [Promoting] equal access to credit for all people.
(f) [Adopting], where appropriate, transparent, timely, predictable and performance based mechanisms for the allocation of resources among different levels of government and various actors.
(g) [Fostering] the accessibility of the market for those who are less organized and informed or otherwise excluded from participation by providing subsidies, where appropriate, and promoting appropriate credit mechanisms and other instruments to address their needs.

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