



human settlements

Department:
Human Settlements
REPUBLIC OF SOUTH AFRICA

Department of Human Settlements

HUMAN SETTLEMENT SECTOR : DEVELOPMENT FINANCE REVIEW

Strategic Analysis, Conclusions and Recommendations

Presentation to the Financial and Fiscal Commission

11 October 2011



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This document provides an outline of a presentation and is incomplete without the accompanying oral commentary and discussion.

Contents

Structure of the Presentation

1. Strategic Analysis

- Scoping the Housing Need
- Defining the Human Settlements Response
- Identifying Development Finance Product Options
- Testing Alternative Development Finance Scenarios
- Strategic Implications for Development Finance

2. Proposed Development Finance Strategy

3. Institutional, Statutory and Financial Implications

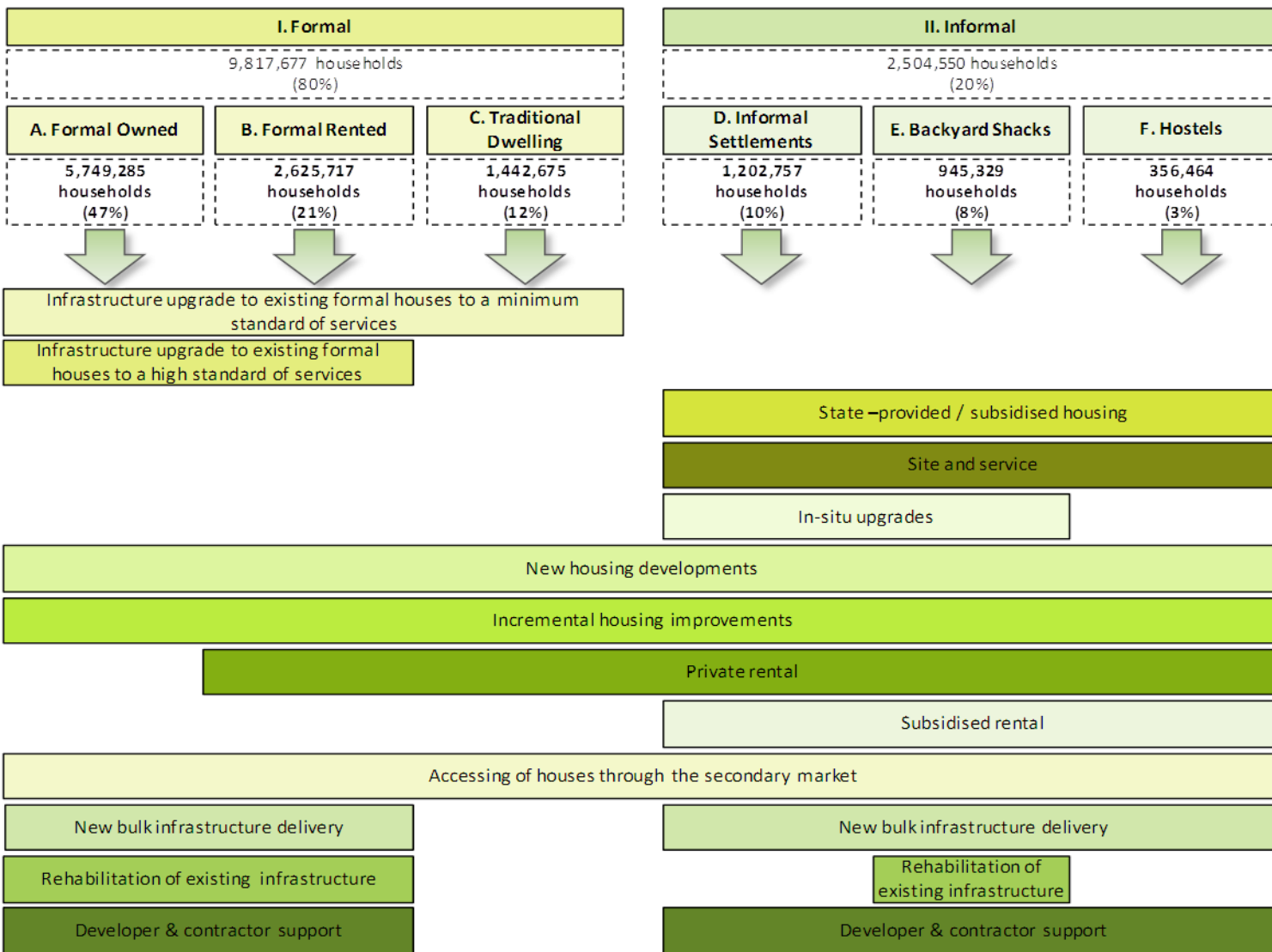
Contents

- 1. Strategic Analysis**
2. Proposed Development Finance Strategy
3. Institutional, Statutory and Financial Implications

Strategic Analysis

Defining the Human Settlements Response

- Indicated here are the range of human settlements responses generally applicable to the identified housing needs
- These include a range of current as well as proposed or under-utilised options



** Note that the current assignment does not deal with social and economic infrastructure nor tenure and related issues that are critical to the delivery of sustainable human settlements

Strategic Analysis

Identifying Development Finance Product Options

Range of Alternative Development Finance Products		Cost per HH (Rands)	Whether or not existing
A1	Project-based basic services connections to minimum standard in existing formal and rural residential areas	11,941	Yes
A2	Project-based basic services connections to high standard in existing formal residential areas	28,770	Yes
A3	In-situ upgrades of informal settlements (site proclamation and service only)	18,776	No
A4	Site and service to accommodate new demand and de-densification requirements	30,040	No
B1	Existing Housing Subsidies for ownership (Project linked RDP incl. services site)	150,000	Yes
B2	Existing Housing Subsidies (informal settlement upgrading)	30,000	Yes
B3	Market-based mortgage backed housing for ownership	254,167	Yes
B4	Market based FLISP subsidised mortgage backed housing for ownership	0	Yes
B5	Subsidy supported secured lending for primary & secondary market housing for ownership	200,000	No
B6	Subsidised residential rental	250,000	Yes
B7	Market-based residential rental	250,000	Yes
B8	In-situ upgrades of informal settlements - infrastructure + top structure incentive	115,613	No
B9	Site and service and top structure incentive to accommodate new demand and de-densification requirements	125,793	No
B10	Small scale rental in existing areas (including upgrade infrastructure for increased density & investment incentive)	32,694	No
C1	Rehabilitation and replacement of existing infrastructure	41,170	Yes
C2	Support primary & secondary market housing transactions through un-secured lending	32,599	Yes
C3	Mortgage Insurance at existing product specifications (HH Income R3,500 to R10,000)	10,000	No
C4	Mortgage Insurance at reduced product specifications (HH income R3,500 to R10,000)	28,500	No
C5	Bulk infrastructure for new housing developments	8,133	Yes

Strategic Analysis

Testing Alternative Development Finance Scenarios

Scenario 1 - Expanded Status Quo

Current sector policy and financial instruments remain but expanded to better meet demand

However this scenario fails to resolve current distortions and market failures which contribute to the “housing gap”

Scenario 2 – Shift the Walls

Eligibility of the capital subsidy is expanded to include households earning up to R7,000 pm & mortgages are made available to households earning less than R7,000 pm

However this scenario is likely to increase current distortions and market failures and overtime to extend the “housing gap”

Scenario 3 – Government Retail Lending

Government assumes the role of retail lender via DFI's or Agents providing mortgages and other secured lending products to households to whom the private sector is reluctant to lend

Results in substantial loan repayment “moral hazard” to the State, as a result of its direct link to retail lending.

Moreover, the regulatory and institutional requirements for the government to establish a retail housing loan capacity is such, that it mitigates against pursuing this option.

Strategic Analysis

Testing Alternative Development Finance Scenarios

Scenario 4 – State Rental

Government provides affordable rental accommodation, through either social housing institutions or other agents, building, owning and operating the stock

This scenario also results in substantial rental payment “moral hazard” to the State as a result of its direct link to state funded rental accommodation.

Scenario 5 – Break Down the Walls

Comprises a redesign of the current capital subsidy, in order to directly finance services sites and to provide a subsidy for the top structure that is directly linked to a personal contribution by the household. Access to credit is enhance by the subsidy/savings contribution

This scenario also results in substantial private / household contribution and lowest direct cost to government – but this is dependent on shifting to a strong emphasis on household delivery (through insitu upgrading and incremental approaches to housing delivery) and redefining the state’s role away from the provision of fully-subsidized housing units towards a focus on access to well located land and basic services.

Strategic Analysis

Testing Alternative Development Finance Scenarios

Assessment of alternative development finance scenarios ...

	Scenario	Total Development Finance Required (1)	Total Cost to State*	Total Private / HH Investment	No of HHs targeted for assistance – housing (2)	% of HH assisted - housing	No of HHs targeted for assistance – services (3)	% of HH assisted - services
		R'm	R'm	R'm	#	%	#	%
1	Expanded Status Quo	952,623	725,343	146,383	4,623,205	62%	2,848,961	100%
2	Shift the Walls	965,310	765,232	144,298	4,623,205	71%	2,848,961	100%
3	Fill the Gap (Govt Retail Lending)	1,140,803	967,218	199,143	4,623,205	41%	2,848,961	100%
4	Fill the Gap (State-Funded Rental)	1,299,252	1,040,072	136,724	4,623,205	61%	2,848,961	100%
5	Break Down the Wall	716,522	547,146	169,376	4,623,205	83%	2,848,961	100%

Notes:

1. The total development finance requirement includes all costs including bulk infrastructure and rehabilitation of infrastructure, but excludes contractor / developer support and payment guarantees as well as any land assembly subsidy.
2. Number of households targeted for housing assistance includes all households in informal circumstances as well as provision for secondary market activity.
3. Number of households targeted for infrastructure only includes households already in formal or traditional circumstances required either basic or higher levels of service.

Strategic Analysis

Strategic Implications

Overall, the scenario analysis reveals that ...

- **An effective mix of products addressing different target segments performs best** in respect of overall cost to society, reduced cost to the state, the mobilisation of private / household funding and the number of households accessing support.
- **This approach (suggested by Scenario 5) is premised on a fundamental shift from current policy** and critically **requires the phasing out of the current subsidy regime** in order to reduce distortions and substantially increase the contribution of households themselves and the private sector in the delivery of affordable housing.
- This is **necessary in order to reduce market distortions** caused by the subsidy housing product **which both inhibits household responsibility and contribution**, and also undermines **the willingness and ability of the private sector to supply/invest in affordable housing**.
- However, **it will need to be phased-in and managed carefully to avoid unacceptable levels of informality** in low income areas.
- These approaches **maximise the impact from available funding and enable funds to be redirected** into new infrastructure delivery and the rehabilitation and replacement of the existing aging and often inappropriate infrastructure platform.
- **Critical supply constraints** such as land assembly and reduced housing product specifications **must also be resolved**.
- **It is important that the overall equity / transformational agenda not be forgotten**. To this end **land intervention** is important in order to secure poorer households good access to the amenities and opportunities of cities and towns. Appropriate **support for emerging contractors and developers** is also essential.

Contents

1. Strategic Analysis
- 2. Towards A Development Finance Strategy**
3. Institutional, Statutory and Financial Implications

Towards a development finance strategy

- **There is no single solution or financial intervention** that can be applied to meeting the human settlement needs of South Africa - **a range of responses are required.**
- **Development finance capacity within the human settlement sector must be sufficiently robust to accommodate a variety of approaches** within a broad overall direction and to accommodate changes in approach without huge disruptions to DFI capacity or financial services available to lower income households.
- It not proposed that a single scenario be selected to inform the required DFI institutional capacity, but rather there should be a focus on a broad approach within which a range of choices can be made over time. **The institutional and financial framework should then be structured so as to allow for this flexibility.**
- **Change carries a cost and delays implementation and must only be done where it adds value.** Any changes to the current arrangements must be planned and implemented in a considered manner over a medium to longer time frame (next 3 to 10 years).

Proposed development finance strategy

Key principles of the broad approach to be adopted are :

- **The current subsidy regime should be phased out over time.** There are a number of options as to how to do this.
- **The state should actively encourage and support households to take responsibility for meeting their own housing needs.** The state could fulfill a number of roles including for example providing access to well located land and basic services, incentivising household and private sector responsibility and investment, etc.
- **In order to assist households to meet their housing needs, all income groups should have access to finance.** The state should support private sector lending.
 - **Access to mortgage backed loans should be facilitated** through state interventions for example securitisation, equity support or cost subsidy interventions.
 - Consideration should be given to enabling **first time home buyers to access an additional subsidy linked to personal savings.**
 - **Equity and debt funding should be made available to micro lenders** to increase the reach that this form of finance currently has.

In the implementation of these interventions the state must at all times support responsible borrowing and lending by both households and the credit providers who should continue to be regulated by the national credit regulations.

- **Both state rental and social housing are excessively expensive for the State and cannot be sustained at the required scale. Commercial** (corporate and small scale rental) **and household landlords** (rental accommodation on existing properties) **are providing substantial supply but often not at the appropriate scale or quality.** Accordingly the state should **stimulate corporate and household investment in affordable rental stock to appropriate specifications.** This could be undertaken through reducing regulations, making available subsidies, tax incentives, property tax rebates or rewarding suppliers of rental stock once investments have been made to required specifications with a capital incentive.

Proposed development finance strategy

- **The existing Infrastructure networks must be rehabilitated and maintained so as to ensure that households already connected into infrastructure services access efficient, cost effective services and that these existing platforms support critical increases in residential densities.** In addition new infrastructure platforms should be created so that new housing can be delivered.
- **The secondary market should be actively supported.** Transactional efficiency should be enhanced, titling backlogs eradicated and restrictions on the re-sale of subsidy housing lifted. In addition, to the extent necessary the availability of loan finance to support secondary market housing transacts must be enhanced through selected government interventions.
- **Human settlement development must be undertaken within a clear spatial/economic plan for the area.** Municipalities must be required to develop a human settlement development plan clearly indicating land allocation for lower income and affordable housing, the development of bulk services and public transport interventions. **Intervention in the urban land market , within the context of this plan, should be supported and must ensure more equitable access to urban opportunities to poorer urban households.**

Human settlement strategy-Proposed Strategy: Key Programme Elements

- 1. Infrastructure**
- 2. Household-led housing delivery**
- 3. Formal housing delivery (ownership)**
- 4. Rental housing delivery**
- 5. Rural housing**
- 6. Redevelopment/replacement of hostels**
- 7. Secondary housing market activity**
- 8. Contractor/Developer support**

Human settlement strategy-Proposed Strategy

Infrastruc- -ture



Overall Approach

- Municipalities are responsible for the development and ongoing maintenance of municipal basic services
- The infrastructure component should provide explicitly for the ongoing rehabilitation of the existing infrastructure platform, additional bulk infrastructural capacity, basic service backlog eradication and new housing delivery
- Municipalities must be able to operate on a sustainable basis and should be explicitly supported financially by the fiscus for the operating costs of maintaining infrastructure services for indigent households.

Financial products

- Grants for the rehabilitation of existing infrastructure (project basis);
- Grants for the eradication of backlogs in service connections to existing formal houses (project basis but against per household cost norms); and
- Grants for additional bulk infrastructure capacity (project basis).

House- hold led delivery



Overall Approach

- The state should over time phase out the current subsidy regime and should introduce a household-led housing programme for households earning below R10,000.
- The final components of this programme need to be determined but should include registered ownership to well located serviced sites or in upgraded well located existing informal settlements.
- Whichever programme/s are selected, HDA should be responsible for assisting the municipality to assemble and make available the well located land at predetermined input costs.

Financial products

- Supply side support comprising a site and service scheme subsidy, in-situ upgrade subsidy, HDA land subsidy, building material subsidy
- Demand side support comprising the facilitation of unsecured and pension-backed lending . Equity and debt support should be provided to selected intermediaries.

Human settlement strategy-Proposed Strategy cont.

Formal housing delivery (ownership)

Overall Approach

- The state should support financial institutions to extend loans on lower priced housing products (down to R150,000) that can be supplied at scale sustainably by private developers to households earning between R7,000 and R15,000 . State could support participating financial institutions through range of mechanisms.
- To qualify, the adherence to lower more affordable housing and service specifications should be tightly prescribed and lending institutions should be required to share risk.
- To access the mortgage loan, households still need to be credit worthy.
- Consideration could be given to entitling first time home buyers earning less than R3,500 to a capital grant on the mortgage linked to a requirement (possibly on a sliding scale but up to a ceiling amount).

Financial products

- Securitization
- Equity Investment
- Lending Cost Subsidies
- Mortgage Insurance

While work is required to investigate all these options further, the DFI's should have the mandate and capacity to pursue this range of options.

Rental housing delivery

Overall Approach

- The state should actively support corporate and household rental housing provision in appropriate locations.
- The focus should be on promoting substantial increases in targeted supply of rental accommodation (e.g. rooms and small units) in targeted areas and thereby promoting more competitive rentals.
- An investment incentive could be introduced to encourage supply at prescribed minimum standards.
- The current Social Housing and CRU subsidy schemes should be phased out over time. The viability of SHI should be supported.
- The SHRA could regulate the new scheme and could also administer the incentive.

Financial products

- In designated areas a variable investment incentive amount should be provided against targeted products - provided on a wholesale basis to accredited municipalities to implement.
- In targeted existing residential areas the introduction of a rates rebate for property owners who construct additional dwellings (densify existing suburbs)

Human settlement strategy-Proposed Strategy cont.

Rural Housing

Overall Approach

- Generally the demand for new accommodation in rural areas is low except where there are specific economic projects (e.g. mining) or evictions of farm employees from existing farms.
- Consequently the focus in rural areas should be in respect of the provision of infrastructure, particularly the eradication of service backlogs to existing established houses and the upgrading and rehabilitation of the existing infrastructure platform.
- Where new demand exists household-led housing approaches are indicated.

Financial products

As per the relevant components above.

Redevelopment/ Replace ment of Hostels

Overall Approach

- Generally the benefits of upgrading hostels are negatively offset by the very high cost as well as the ongoing social disruption of failing to integrate the often highly alienated hostels dwellers into the broader community.
- Consequently, except in specific circumstances, the option of demolishing the hostels and accommodating hostel dwellers in incremental or formal housing projects in the general area is strongly indicated.
- An incentive (access to an incremental or mortgage backed housing subsidy) to vacate the hostels should be investigated

Financial products

As per the relevant components above.

Human settlement strategy-Proposed Strategy cont.

Secondary Housing Market Activity

Overall Approach

- The secondary market is an important component of the housing sector.
- Recent evidence suggests that transactional activity in this market is starting to increase.
- The mortgage backed ownership product should be available to existing as well as to new houses.
- Need to introduce a specific programme aimed at addressing the issue of households who received a subsidy house, but have not yet received title.
- Other initiatives to increase transactional volumes should be considered.

Financial products

As per the relevant components above.

Contract or/Developer support

Overall Approach

- A key developmental outcome within the Housing Sector is that it promotes sector transformation and provides economic opportunities for emerging contractors/developers.
- Accordingly there is a need for a support programme that provides bridging finance and support to targeted developers.
- In addition, current payment delays within the public sector (provinces and municipalities) are resulting in significant failure
- , particularly of these emerging firms.
- Accordingly there is a need for payment guarantees or factoring to alleviate this problem. This is most effectively implemented with the active support of the National Treasury

Financial products

- Bridging Finance Loans
- Payment Guarantees

Contents

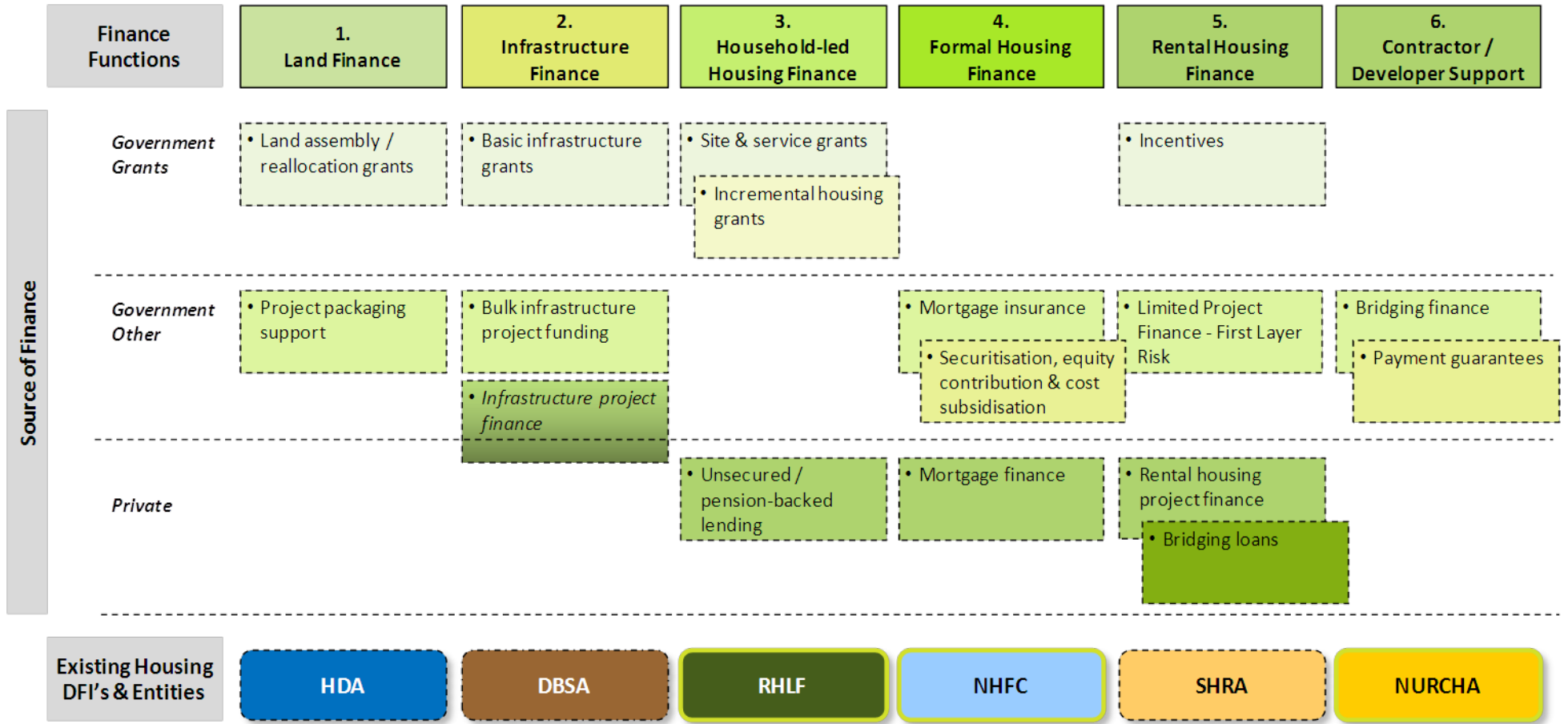
1. Strategic Analysis
2. Proposed Development Finance Strategy
- 3. Institutional, Statutory and Financial Implications**

Institutional implications

- The proposed development finance strategy **will require a coordinated mix of interventions and instruments within a framework that allows high levels of flexibility.**
- More specifically **the analysis suggests that a range of finance products are required within the following categories:**
 - **Land Finance:** Including land assembly/reallocation grants and land/ project packaging support
 - **Infrastructure finance:** Including basic infrastructure grants and bulk infrastructure project funding
 - **Household-led housing finance:** Including subsidies and unsecured lending.
 - **Formal housing finance:** Including mortgage finance and related support such as insurance, securitisation etc.
 - **Rental housing finance:** Including rental project finance and incentives
 - **Contractor/Developer finance:** Including bridging finance for emerging contractors, bridging finance for emerging housing developers and payment guarantees for contractors and service providers.

Institutional implications cont.

Mapping finance functions and current institutions

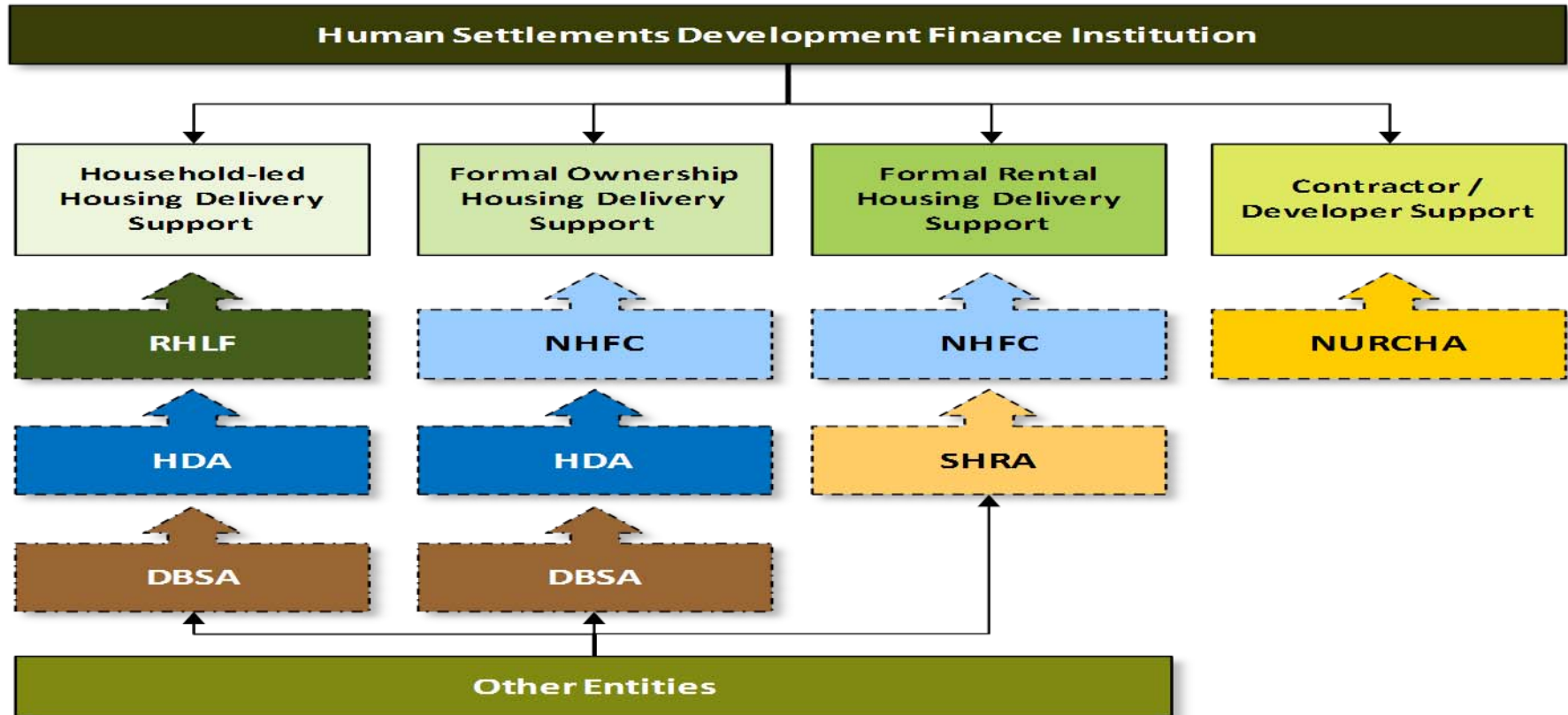


Institutional implications cont.

- The broad development finance strategy presented **requires a government response that ensures that development finance functions are appropriately institutionalised but also have the capacity to evolve over time**
- It is **proposed that a consolidated Human Settlements DFI be established over time**
- It is **proposed that consideration be given to the phased consolidation of the NHFC, RHLF and NURCHA as the nucleus of a new Human Settlements Development Finance Institution. The core rationale is as follows:**
 - 1) **Provide an institutional basis for enhanced coordination**
 - 2) **Provide a platform that can begin to address the scale of the housing requirements indicated most critically by:**
 - **Providing a significant balance sheet.** It is noted that estimated combined assets of the three entities is some R3 billion (NHFC: R 1,3 billion; RHLF: R 326 million and NURCHA: R 494 million in 2010). Importantly it is believed that the combined balance sheet could be more effectively utilized to leverage private sector finance into the human settlements sector.
 - **Leveraging skills and human resource assets.** The three entities have a combined staff of some 138 people (NHFC: 86; RHLF: 10 and NURCHA: 38) which a broad spectrum of skills and expertise.
 - 3) **Effect significant cost savings over time** as the duplication of governance structures, compliance requirements, systems etc. are addressed
 - 4) **Clear, strengthened and transparent mandate and processes** which would strengthen the role of the three entities and the Minister and would **ensure that the entities are more directly governed by NDoHS policy.**

Institutional implications

Allocation of key housing finance functions.....



Thank You