Engagements in housing microfinance – on whose terms?

Abstract

Efforts to improve living and housing conditions in urban Africa were subject to major changes since the 1950s, according to political upheaval and different economic perspectives on development. In the face of the neoliberal agenda, development policies increasingly focused on structural adjustment and the reduction of public expenditures and subsidies since the 1980s. At the same time, microfinance initiatives gained considerable attention, especially in Asia and Latin America.

Matching the ideas of neoliberal economic development, microfinance is seen as a key to improve the livelihoods of the poor, and international organisations like the UN or World Bank increasingly support the scaling-up of the microfinance sector.

In Africa, conventional microfinance started to penetrate markets with some delay compared to Asia or Latin America, but the rise of microfinance institutions and the constantly increasing numbers of clients suggest that microfinance in Africa is just in its initial stages. Although the sector still faces shortcomings and several challenges, a lot of governments have taken considerable steps towards the liberalisation of financial markets. Besides conventional microcredits for small and medium enterprises, home improvement loans were developed, after it became obvious that large amounts of the credit sums were invested in housing.

In Dar es Salaam, Tanzania, housing microfinance is politically supported in order to improve housing conditions. So far, three NGOs are providing housing microfinance to dwellers of unplanned areas, while pursuing quite different strategies. Drawing from findings gained during field research in 2009 and 2010, these strategies will be compared, and the terms underlying those credits will be discussed. Who is in the position to apply, and who is in the position to decide about the investments financed by housing microcredits, are the main questions this paper seeks to address. A critical discussion on the benefits attributed to this approach, but also on the various potentials for conflicts, should bring us closer to answer the viable question related to the conference's topic: „Engagements in housing microfinance – on whose terms?“

The development of policies on informal housing

The process of rapid and uncontrolled urbanisation in Africa has attracted the interest of development cooperation for decades. Unfortunately, „faced with other development priorities, governments and international agencies have been reluctant to encourage investment in housing“ (JONES & DATTA 1999: 3), so that these ambitions often ended up as small-scale punctual projects, instead of integrated and holistic concepts. In accordance with shifting ideas of development theories, different – partly overlapping – phases of strategies to increase the supply of affordable housing were pursued (cf. HARRIS & ARKU 2006 / 2007; HARRIS & GILES 2003): Public housing initiatives, coupled with massive slum clearance, often proofed to be an expensive failure in the face of the massive growth of informal settlements during the first decades after independence. It was in this context, that Turner's “aided self-help” approach to housing became popular, and in the following years so called *site and service* or *slum upgrading* schemes became the dominant strategy for upgrading informal settlements (TURNER 1976). After severe shortcomings of the self-help approach became obvious, like cost increases or the imperative only to include households with permanent incomes (cf. LOHNERT 2002: 60f.), the “popular” or also called “enabling approach” gained importance in the 1980s. It concentrated on

government policy reforms towards decentralisation and democratisation (HARDOY & SATTERTHWAITE 1995: 136ff.; STREN 1990: 47) and was clearly embedded in the shift towards market liberalisation. Active public engagements in housing provision were reduced or even stopped totally. Within the last years, in accordance to the neoliberal agenda, interventions within the housing sector concentrated on the provision of housing finance. This trend was heavily influenced by the booming microfinance sector, and microfinance for housing developed to the new dominant strategy propagated by international agencies, like UN Habitat and the World Bank.
Jones and Datta summarise this trend as “from self-help to self-finance” and argue that the recent advocacy of microfinance for housing is based on the publicly perceived success of microfinance itself and a “high degree of optimism and the tendency to cite ´positive` experiences” (1999: 4).

The microfinance boom in Africa and approaches on housing microfinance

The entire microfinance sector in Africa is still largely underdeveloped, less profitable and still hindered by high transaction costs, while often not including the very poor. Repayment defaults are more likely to occur in Africa than anywhere else, especially in urban areas, where social pressure is lower than in rural regions (GIESBERT 2008: 4).There have been some successful experiences in other continents while in Africa “microfinance as a specific housing product is in its infancy and therefore only starting to be documented” (TOMLINSON 2007: iv).Nonetheless, microfinance providers and institutions are mushrooming all over the continent.
Building on the advantages of microfinance that have been observed in Asia and Latin America, dominant organisations like World Bank and the United Nations currently propagate microfinance for housing as the key strategy for large scale improvement of housing in Africa, after it was observed that large parts of microcredits were directly invested in home improvement.
Daphnis and Ferguson had published the first publication written on housing microfinance in 2004, while the UN Habitat report on financing urban shelter (2005) refers to a significant potential of housing microfinance for urban upgrading purposes in the future. The small-scale lending to low-income residents for housing related purposes (i.e. alterations, extensions, improvements, new construction, infrastructure upgrading etc.) is what characterises housing microfinance schemes, while a range of different institutional varieties from individual small loan agreements to Rotating Savings and Credit Associations (ROSCAs), Community Shelter Funds or Savings and Credit Cooperative Societies (SACCOS) can be identified as housing microfinance providers (cf. JONES & DATTA 1999; TOMLINSON 2007; UN Habitat 2005).
Usually housing microfinance services are offered by local NGOs or microfinance institutions (MFI), sometimes with the support of governments or international donors. One of the most dominant approaches, especially in Africa (cf. GIESBERT 2008), is to motivate residents to form saving groups, since the reliance on social networks seems to be one of the reasons for the microfinance success. Within social networks and hence saving groups, social pressure is used to enforce repayment and regular savings and is often utilised as a form of collateral.
Housing microfinance provides households with the advantages to access credits for housing on the one hand, while it also enables homeowners to improve their homes according to their own needs and perceptions.During the last years many initiatives in different African countries have been elaborated and the potential for the housing

microfinance sector is huge given the high urbanisation rates of African cities. Even commercial lenders are trying to develop housing credit products for low and medium income groups and enter markets step by step.

Housing Microfinance in Dar es Salaam, Tanzania

Until October 2010, three NGOs had set up specific housing microfinance schemes for dwellers of unplanned settlements in Dar es Salaam. Their differing strategies were studied during intense field research between October 2009 and March 2011 and some of the findings will be presented in the following. Since the underlying terms vary strongly from one organisation to the other, the providers and the credit conditions will be presented, followed by a characterisation of their respective customers. Their own needs determine the investment priorities and they found their own ways in dealing with the credit regulations. Benefits for the customers are manifold and will be summarised, while also problems and conflicts have evolved between providers and customers, but also within the providing institutions.

The largest provider, as measured by its number of clients, is Habitat for Humanity Tanzania, the local branch of the international NGO Habitat for Humanity. By the end of February 2011 its housing microfinance product *Makazi Bora* had 507 active and a total of 980 registered clients.The loans of *Makazi Bora* can be used for finishing, completion, repairs, extensions, shop construction or connections to basic infrastructure as electricity or water. The potential credit volume increases with every successive loan, from 200,000 to 800,000[1]TSh for the first and 3 million for the third loan.Repayments can take up to 24 months, depending on the customer’s abilities and the monthly instalments start one month after receiving the disbursement. Since the credit provider is a non-profit organisation, interests are very low with 2%. In case that loans are used for expenses other than specified in the forms, clients have to pay higher interests of 5% as penalty, and in case of a delay of instalments, an additional 1% of the monthly amount has to be paid. Moreover, costs arise for the initial registration and for an insurance covering the loan in case of death.
One of the major conditions for interested customers is that they live or built their house in Mbagala ward, on the southern urban fringe of Dar es Salaam, where unplanned urban expansion is proceeding rapidly and where the *Makazi Bora* office is located.

The home improvement loan of Women’s Advancement Trust (WAT) is the oldest housing microfinance product offered in Dar es Salaam. By March 2011, they had however, only served 80 clients with specific housing credits[2]. The loans can be used for construction, repairs, plot purchase and the connection to basic services like water and electricity supply. The credit volume is depending on the client’s ability to save 31% of the enquired amount and can range between 300,000 and 2.5 million TSh. The period of repayments can be chosen by the client ranging from 3 to 24 months. Interest fees are very low with 0.83% per month and there are still no penalty fees for loan divergence or for delays. Additionally, costs arise for the insurance, for registration and for supervision and expertise provided by WAT.
So far, WAT offers the housing microcredit in unplanned settlements, where they had arranged information events and seminars on their product. Until March 2011 this

[1] In May 2011, 1000 Tanzania Shilling (TSh) = 0.45 Euro.
[2]Currently, WAT istryingtoaccesslandforplanneddevelopmentoflow-costhouses. 400 clientshavelinedup in ordert o accessthesesurveyedplots on the urban fringe, most oft hem tenantswishingtobecomehouseowners.

included four distinct wards for the home improvement loans. Currently, the organisation tries to alter their focus towards the planning of large-scale housing projects for the low-income groups similar to the strategy of the Federation of the Urban Poor, which is presented in the following.

The Federation of the Urban Poor, supported by the local NGO Center for Community Initiatives (CCI) and its main sponsor Slum/Shack Dwellers International (SDI), offers a totally different housing microfinance product. It doesn't target the improvement of existing units in unplanned settlement, but aims at the construction of a new planned low-cost housing area at the urban fringe, similar to former *site and service* approaches.

By March 2011, ten households lived in the low-cost houses, which were constructed according to planned layout by an architect and with support from a public agency developing low-cost construction methods that are locally adequate. Individual connections to water supply and wastewater collection are planned but not yet installed and the area is still not connected to electricity supply.The construction of a basic unit of 2 rooms and a bathroom (which is not equipped) costs less than 3 million TSh, but the construction and financing process is divided into three steps: first, a clients have to take up a loan of 1 million TSh for the construction of the foundation before another 1.2 million can be enquired for walling. The last step comprises roofing and the purchase of window frames and doors. After the finalisation of the small unit, clients have the option to extend their dwelling by another room and a kitchen. In total a large unit with all basic facilities like toilets and sinks, may cost between 5 and 7 million TSh.Interest fees are 10% per loan and an insurance has to be paid as well, additional to the deposit of 100,000 TSh per loan. Monthly instalments start after the completion of the work and are fixed to 62,000 TSh per month. So far there are no penalties for the delay of instalments, and in March 2011 it seemed that only very few clients had started paying off their debts on a regular basis. In order to control that money is spent for construction only, the money is not handed out in cash but directly used for the on-plot production of the construction materials.

Although the low construction costs coupled with formal development might attract a large number of customers, progress had been quite slow. Clients have to be members of the Federation of the Urban Poor and so far the Federation chooses clients by discussing about theirindividualhousing need and their abilities to repay the loan in a meeting.

Table 1 summarises some of the most important terms and conditions of the respective housing microcredit providers. While Habitat for Humanity is providing credits to individuals, access to the respective credit product of the other institutions is restricted to group members. In case of default, the other group members have to cover the costs of repaying the credit, which is one of the basic characteristics of the microfinance principle. Customers, however, fear this as long as they don't know each other very well and usually prefer to be independent.

TABLE 1: Terms and conditions of home improvement loans in Dar es Salaam

Terms and conditions	Habitat for Humanity Tz. / Makazi Bora	Women's Advancement Trust	Federation of the Urban Poor
Designated use of loan	Finishing, extension, completion, repairs, shop construction, connection to basic services	New construction, repairs, finishing, plot purchase, connection to basic services	Construction of 2 or 4 room house at planned site
Specific location / target group	low and medium income dwellers in Mbagala ward	Low and medium income groups potentially in all unplanned settlements in DSM	Members of the Federation of the Urban Poor; construction in Chamazi
Eligibility criteria	- house is located in Mbagala - monthly payments do not exceed 25% of income - any kind of formal/informal land title - construction has reached roofing level	- formation of savings group of 15-20 clients - assessment of income - license of occupancy	- member of Federation - group evaluation of need and income - savings account - experience in savings, credit and repayments within savings group of Federation
Collateral	- one guarantor - Movable assets - savings	- two witnesses from the group - ownsavings - group savings - movable assets	- three witnesses - group savings - movable assets - family savings
Costs	- 2% interest per month (if diverted 5%) - 20,000 TSh membership - 1% insurance - in case of delay of repayment: 1% of monthly instalment - 10% of loan amount saved in bank account	- 0.83% interest per month - 1% of loan amount as credit fee - 1% insurance - 4% of loan amount for technical supervision (5% in case of new construction) - 25% of loan amount saved in SACCOS account	- 10% interest per loan - payment of deposit of 100,000 TSh at bank account - 1% insurance

Source: own data

As often argued by critics of microfinance, clients of the above mentioned organisations (except the Federation members[3]) do not belong to the lowest income groups. On average the monthly household income of a client was 720,000 Tsh, while non-client households had to rely on monthly incomes of 355,000 TSh. The median income of housing microfinance clients, however, was considerably smaller with 380,000 TSh per month, indicating that housing microfinance customers comprise a very heterogeneous group. Another factor contributing to this figure might be the fluctuating incomes from informal sector occupation.

As shown above, clients of Habitat for Humanity and Women's Advancement Trust can choose individually what they want to finance and therefore each household had its own investment priorities ranging from structural improvements, beautification, roofing and the replacement of old corrugated iron sheets, improvement of sanitary facilities, connection to the power grid to the new construction of rental units or shops.

Although it is often argued that housing microfinance does not contribute to income generation, it was observed that more credit clients (74%) engaged in renting out rooms and shops than non-clients (32%). Other clients improved existing rooms that were rented out, and were able to increase rents. Only in Chamazi renting out is not an option, since most households build the very small 2 room units and because the area is very far away from public transport facilities.

Credit clients are also more financially literate than non-clients, having more ideason how to invest money for long-term benefits and being integrated in other savings and credit schemes. They participate in weekly informal savings groups in order to repay their credits or use also other cooperatives and savings institutions to access cheap credits. Since the products of the housing microfinance providers rarely cover the full costs of the envisaged home improvement projects, many clients are also able to find other ways to access the missing amount, like saving in cash and material for a longer period prior to requesting the credit. Most of them have stated that especially the trainings and information seminars have helped them to understand financial mechanisms and how they can achieve better housing conditions and even benefit financially from their housing assets.Most of the credit clients wish to receive another credit after repaying the recent one. In general they have a clear vision about what they want to improve in the next step, how much this would cost and how they can access the financial means.

Basically, most customers appreciate the conditions especially of WAT and *Makazi Bora*, because they are much more favourable compared to conventional microcredits. On the one hand interests are smaller and on the other hand instalments have to be paid on a monthly basis instead of weekly repayments, making it easier for households to access money in due time.

However, there are also problems and conflicts arising between customers and providersconcerning indebtedness and required monthly repayments. Within the first year of its operation, some *Makazi Bora* clients diverted their loans for other income-generating activities or private expenses, so they had to pay a monthly interest rate of 5%. They were furious, arguing that the money was not sufficient for their proposed activities, but deeper investigations by the organisation proved that some of their credit officers had made clandestine arrangements with clients promising them thatthe misuse of their loan would not be uncovered. WAT has not yet installed any punishment in the case of diversion of loans, but is planning it, while the

[3]UntilOctober 2010 only 1 customerlived in Chamazi, so thatthebaselinesurveyonlyincludesclientsofMakazi Bora andWomen'sAdvancement Trust.

Federation of the Urban Poor is eliminating any kind of potential misuse by not paying out clients in cash. In turn, they faced trouble with their clients because of some quality problems of construction, when a storm caused the collapse of a roof and the damage of some houses in Chamazi. Since all organisations understand very well, that with bad quality of construction, credit clients might be reluctant to repay their credits, they have tried to guard themselves against this threat. The Federation of the Urban Poor had to ask for donor support to repair the damages and has improved their construction technique to avoid the same problem to occur again. In contrast WAT is sending out their technical supervisors in order to check the existing unit and to discuss with owners and their respective craftsmen on how to construct in order to achieve the envisaged outcome. The approach of *Makazi Bora* is completely different, since they have the opinion, that customers should be responsible themselves and that they are the best ones to know what they need. Technical supervision is therefore not needed, and the technical officer is only responsible for crosschecking the costs of submitted credit requests.
Mostly relations between clients and providers are free from conflict, but deeper investigations and stricter control of repayments and investments by WAT and the Federation of the Urban Poor might stimulate conflicts. So far they have been reluctant to exert pressure on their customers, different from *Makazi Bora*, which has been trying to become financially sustainable as soon as possible.

All institutions presented here, have or have had internal problems, mostly concerning their staff, their funding or their credit procedures. In the beginning *Makazi Bora* employed only college and university graduates as credit officers, but experienced high default rates and trouble with customers who were identified as having diverted their loans. They were successfully solving the problem by replacing staff with people who had just finished secondary school and who basically lived in Mbagala as well. Relations between customers and credit officers were substantially improved and decreasing default rates confirm this. Construction in Chamazi by the Federation of the Urban Poor was hindered by the lack of financial resources for a long time. Group members are responsible to decide on loan repayment procedures and on who is getting the chance to build and additionally some of them engage in the on-plot production of the construction materials. Since most of them are not professional craftsmen, problems of quality of bricks and the whole structure appeared. In contrast, WAT is experiencing internal problems due to time extensive consultation procedures for the clients but also for their own employees. Many field visits of the staff are needed before any credit can be given to group members. Additionally the technical supervisor has to visit all clients before and after construction. This is extremely time-consuming given the fact that WAT only went to their direct neighbourhood for the pilot project. Most customers, however, are located far away from the office, adding to the time burden of clients and staff.

Engagements in housing microfinance – on whose terms?

The three housing microfinance providers presented have shown that the terms and conditions vary considerably from product to product. They specify more or less strictly who can apply, e.g. making loans available to Mbagala citizens (location-specific) or group members (membership-specific) only, but also by establishing norms on what the credit can be used. *Makazi Bora*clients , for example, cannot use their credit to start the construction of their house, since the organisation wants to support households to move into their house as soon as possible to avoid costs from

renting. In the case of the Federation of the Urban Poor, clients don’t have any choice at all, besides deciding to get indebted for a 2 or a 4 room house.
The organisations try to learn from their respective problems and have arranged for regular meetings with their customers in order to discuss shortcomings and potentials for improvement. Hence, their clients have the chance to induce changes of the product, like the reduction of interest rates in case of faster repayments for *Makazi Bora* loans.
Since all three organisations have formulated their own terms and conditions, they differ strongly and give different investment opportunities to their customers. While conventional microfinance is still based on group formation and social pressure as collateral, the success of the approach of *Makazi Bora* has shown that if clients can choose, they prefer to rely on themselves instead of being responsible for others. The terms and conditions defined by providers are therefore of enormous importance for a product’s success, since customers are usually very well aware of them. Most clients have benefitted in numerous ways, not only by having access to cheap financial means for housing but also by improving their own living conditions or even by increasing their income from rent. As long as terms and conditions consider the clients’ needs and abilities, housing microfinance can be a successful option to improve the housing situation in unplanned settlements.

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