ARAB REPUBLIC OF EGYPT

A FRAMEWORK FOR HOUSING POLICY REFORM IN EGYPT:

Developing a Well Functioning Housing System and Strengthening the National Housing Program

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The World Bank

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US$ 1 = LE 5.339

ABBREVIATIONS AND ACRONYMS

ADEMI	Asociación para el Desarrollo de Microempresas, Inc.
AHS	American Housing Survey
APR	Annual Percentage Rate
BOT	Build, Operate, and Transfer
CAPMAS	Central Agency for Public Mobilization and Statistics
CARD	Center for Agricultural and Rural Development
CBE	Central Bank of Egypt
CDA	Community Development Association
CGC	Credit Guarantee Company
CHBR	Center for Housing and Building Research
CPI	Consumer Price Index
EFS	Egypt Financial Services
EMFN	Egyptian Microfinance Network
EMRC	Egyptian Mortgage Refinance Company
ESA	Egyptian Survey Authority
FAR	Floor Area Ratio
FHFB	Federal Housing Finance Board
FOGARIM	Fonds de Garantie pour les Revenus Irréguliers et Modestes
FUNHAVI	Fundación Habitat y Vivienda, A.C.
GAHBC	General Authority for Housing and Building Cooperatives
GOE	Government of Egypt
GOPP	General Organization for Physical Planning
GPM	Gradual Payment Mortgage
GSF	Guarantee and Subsidy Fund
HDB	Housing Development Bank
HIECS	Household Income, Expenditures, and Consumption Survey
HUD	U.S. Department of Housing and Urban Development
ID	Identification
IFC	International Finance Corporation
KFW	German Bank for Reconstruction
LE	Livres Egyptiens
M&E	Monitoring and Evaluation
MBA	Mortgage Bankers Association
MENA	Middle East and North Africa
MFA	Mortgage Finance Authority
MFC	Mortgage Finance Company
MFH	Microfinance for Housing

MFI	Microfinance Institutions
MHUUD	Ministry of Housing, Utilities, and Urban Development
MIWR	Ministry of Water Resources
MOF	Ministry of Finance
MOI	Ministry of Investment
MOJ	Ministry of Justice
MOLD	Ministry of Local Development
MOSS	Ministry of Social Solidarity
MSAD	Ministry of State for Administrative Development
NAHB	National Association of Home Builders
NAR	National Association of Realtors
NBE	National Bank of Egypt
NHP	National Housing Program
NGO	Non-governmental Organization
NUCA	New Urban Communities Authority
PPP	Public-Private Partnership
REFC	Real Estate Finance Company
REPD	Real Estate Publicity Department
SEWA	Self Employed Women's Association
SFD	Social Fund for Development
SOMA	Survey of Market Absorption
TAPRII	Technical Assistance for Policy Reform
UNDP	United Nations Development Program
USAID	United States Agency for International Development
VSB	Villes sans Bidonvilles

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I. EXECUTIVE SUMMARY

1.0 Objectives

The two key objectives of this policy note are to provide recommendations for a policy-based approach to housing sector reform in Egypt and to improve the delivery of housing subsidies under the National Housing Program (NHP). The paper builds on the key findings of recent research and analysis related to affordable housing in Egypt, presents a framework for moving forward with housing policy and subsidy reform focusing on two priority areas:

- **Comprehensive housing sector reforms** designed to put in place over the medium and long-term the foundations of an efficient and well-functioning urban housing market, by making more effective use of Egypt's existing housing stock, maximizing the role of the private sector in housing production and financing, and targeting government assistance to the poor who are unable to afford shelter provided in the market place; and

- **Improvements to the NHP**, particularly regarding cost-efficiency, affordability and distributional impacts of housing subsidies, private sector participation, and effectiveness of the institutional framework, all of which can be initiated immediately and used to leverage longer-term reforms in the housing delivery system.

It is important to note that this is not a substitute for a complete housing policy, but rather a framework that focuses on specific policy issues that need to be addressed in Egypt.

2.0 Challenge: A Constrained Housing Market

Egypt has made significant progress in launching a mortgage finance system, reforming the land and property registration system, formulating an improved property tax law and a Unified Building Code, implementing a new Rental Law, and expanding the variety of affordable housing typologies offered under social housing programs. The most evident sign of the GOE's commitment to improving housing conditions in the country was the launch of the National Housing Program (NHP) in 2005 with the goal of providing 500,000 housing solutions by 2011.

Despite these advances, however, the majority of Egypt's housing stock is still constrained by very high vacancy rates, rent control, and informality. Indeed:

- ***Almost 3.7 million urban housing units are unused, either vacant or closed.*** The scale of vacant urban housing units, much more serious than in other emerging markets, is a specific and puzzling phenomenon of the Egyptian housing market. One explanation is that the sustained rapid appreciation in value over the past 25 years and the lack of alternative investment mechanisms until quite recently meant that housing and real estate have consistently served as an inflation-proof savings and investment mechanism, without need of the rental yield.[1] The idea of renting was even less attractive due to the imposition of rent control until 1996. Even now, the

[1] Despite some slowdown in the early 2000s, this trend has continued unabated and has very recently reached new heights, fuelled by major inflows of foreign investment in real estate in Egypt from regional investors.

continued perception of uncertainty about the enforceability of the new rental law makes many owners hesitant to rent out their unoccupied units. Poor targeting of government subsidized units, and unattractive locations of subsidized units in New Towns, have further exacerbated the problem.

- ***An estimated 42% of the housing stock in Greater Cairo is frozen under rent control.*** Since the passage of Law No. 4 of 1996 that freed the rental market for newly built units, but grandfathered existing rent-controlled units for the duration of the contract, the rental market is showing signs of increased dynamism. However, the TAPRII Greater Cairo Housing Demand Survey found that 42% of the total urban housing units in Greater Cairo are still locked under the rent control regime under current grandfathering arrangements, and that this is not necessarily benefiting the poor. Locking such a large proportion of units out of the market greatly constrains residential mobility, causes lack of stock maintenance, and distorts the overall housing market.

- ***Some 45% of new urban housing is produced by the informal sector.*** During the inter-census period (1996-2006), the urban housing stock is conservatively thought to have grown by an annual average of 2.8% or 263,838 units.[2] Of these, 55.6% were formal and 45.4% informal (built without government authorization and registration). Constrained by high building and zoning standards, as well as a bureaucratic and costly permitting process, many families and small developers operate within the informal sector to meet the growing housing demand of lower income households with units of relatively good quality. While informal housing provides a low cost housing solution, it undermines urban planning efforts and does not allow households to use mortgage finance.

While these three distortions are not entirely additive (e.g. an informally built unit may be held vacant and/or under rent control), it could be conservatively estimated that 50% - 75% of the urban housing stock in Egypt suffers from such market constraints. These combined market weaknesses directly affect the affordability of housing, the success of the newly initiated mortgage system, the mobility of labor (economic growth), and the government's ability to address the shelter needs of poor households.

3.0 Goal: A Well-Functioning Housing System

The 500,000 low-cost units to be provided under the NHP are a temporary palliation for Egypt's chronic housing problem. However, the GOE has the timely opportunity to leverage the NHP subsidies and the political momentum created by the program to initiate the reforms needed to build a well-functioning housing system. Indeed, the GOE has the proverbial chance to 'hit two birds with one stone.'

What is a well-functioning housing system? Broadly, it is a housing system in which the supply response is elastic, the market produces products people want in a price range that is affordable, housing production takes place in an efficient manner so that the value of the output is as high as possible for any set of given inputs, and that the key input markets – land, finance, construction and regulation – are themselves functioning well. As such, a well-functioning housing system can greatly improve a country's economic efficiency, especially in the rational use of investments, in labor mobility, and locational choice.

[2] The preliminary results of the 2006 census made available by CAPMAS do not allow for a precise calculation of the number of housing units. As such, the total number of housing units in urban areas was inferred as the sum of "apartment units" (shiakha) and "one/more independent rooms" (hogra mostaqila). This figure is counter-balanced by the exclusion of single family housing and the failure to account for housing units converted into offices.

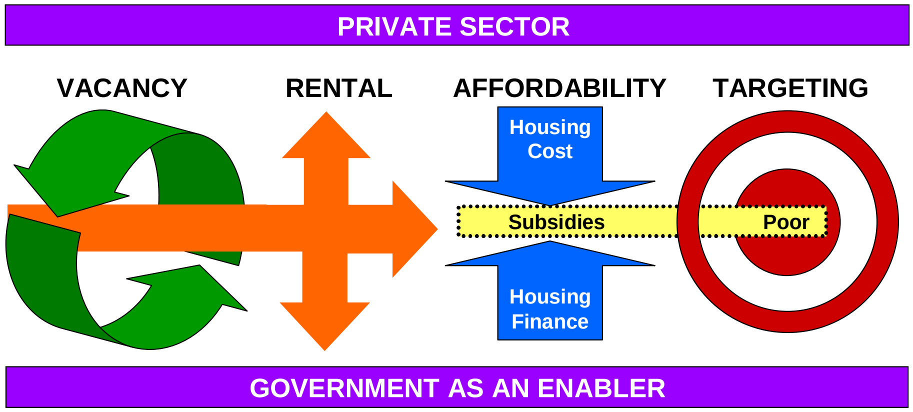
Why should the GOE improve the functioning of the housing system? There are significant fiscal and macroeconomic consequences of a poorly functioning housing system. For example, a well-functioning housing market produces a wide range of house types with a broad range of prices and tenure options, which reduces the demand for government subsidies. Over the past 25 years, the public sector built as much as 36% (1.26 million units) of all formal housing units supplied in urban areas. This came at a significant fiscal cost of LE 26.4 billion, not including additional off budget subsidies related to the cost of land and off-site infrastructure. Moreover, while the Ministry of Finance has allocated over LE 1 billion per year towards the NHP, it is estimated that the true off- and on-budget NHP subsidies will reach LE 4.4 billion per year, or around 0.7% of GDP for this program alone. Clearly, housing subsidies represent a sizeable fiscal burden for the Government of Egypt.

A poorly functioning housing system has negative macroeconomic consequences. Of foremost concern is that the current investment model of purchasing housing and holding it vacant is based on capital appreciation without cash-flow. This investment model is highly vulnerable to an economic downturn, it pushes housing prices upward, and it is an unproductive use of capital. High levels of vacancy and rent controlled housing stock, moreover, produces an inefficient urban system which has a negative effect on economic growth and limits labor mobility and participation.

The framework for a well-functioning housing system in Egypt presented in this Note consists of the five action channels listed below (see Figure 1). The framework provides recommendations for addressing existing distortions to the current *stock* of housing (vacant and rent controlled units), improving the *flow* or production of housing (decreasing the cost of housing supply) and enabling better household access to housing (improving affordability and targeting, and reforming Government role) as a way for moving forward. The five channels are as follows:

- **Vacant Units.** Unlock the stock of vacant housing through (1) tax reforms and innovative subsidy instruments that provide incentives to owners of vacant units to release them to the market and (2) developing a liquid rental market.
- **Rental Market**. Create a fluid rental market by (1) strengthening rental market regulations and streamlining tenant eviction procedures and (2) accelerating rent decontrol.
- **Affordability.** Enhance affordability of new housing options by (1) increasing access to housing finance through incentives for lenders to further expand down-market and (2) decreasing the supply cost of housing and transaction costs of accessing it. This dual approach to improving affordability will minimize the size of public subsidies needed.
- **Targeting.** Improve the targeting of public subsidies to ensure that they are provided to (1) the lowest income households who require them to obtain adequate shelter and (2) specific market segmentation to assist in clearing well-defined market blockages. Successful targeting along those lines will significantly reduce the need for future subsidies.
- **Government.** Transform the government into an enabler of the housing market that can (1) better understand housing markets and react to changes, (2) effectively engage the private sector in the delivery of housing, (3) provide an effective regulatory framework, and (4) formulate policies to have in place a well-functioning housing market/system and assist low-income households to afford housing solutions.

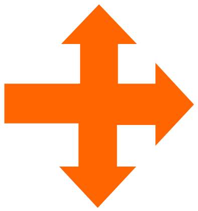
Figure 1: Framework for a Well Functioning Housing System in Egypt



4.0 Recommendations

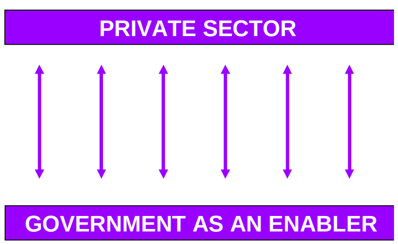
The recommendations detailed in this Note are divided into (a) reforms needed to develop a well-functioning housing system and that require a medium/long-term outlook, and (b) reforms that are immediately actionable under NHP and that will simultaneously work towards the goal of developing a well-functioning housing system and help MHUUD efficiently create 500,000 housing solutions by 2011 (see Table 1).

Table 1: Summary of Recommendations

Housing System Channel	A Well-Functioning Housing Market	Improvements to the NHP
 **VACANT UNITS**	**Goal:** Unlock the stock of vacant housing through (1) reforms that provide incentives to owners of vacant units to mobilize them, (2) disincentives to holding units off the market, and (3) developing a fluid rental market.	
	• Conduct a vacancy survey to determine vacant unit status and causes • Consider tax incentives linked to utilization of vacant units • Utilize streamlined lease and eviction procedures to promote rental utilization • Link disincentives to holding vacant units to the improvements currently underway in the real estate tax system	• Use NHP subsidy for qualified buyers for unfinished units (possibly link to mortgage or consumer loans) • Use NHP subsidy for qualified owners to complete units (possibly link to mortgage or consumer loans) • Use NHP subsidy as an eviction guarantee, thereby enabling recipients to use it for rental units • Use subsidy to assist down-payment (key money) for rental units • Investigate feasibility of transportation subsidy for New Town residents
 **RENTAL MARKET**	**Goal:** Create a liquid rental market by (1) strengthening rental market with clear and simple regulations and (2) accelerating rent decontrol.	
	Rental Market Regulation: • Define model rental contractual agreements governing the rights and responsibilities of tenants and landlords and related issues (termination, rent adjustment, etc) • Develop an ombudsman or other out-of-court mediation to lower the costs of dispute resolutions • Establish low or no-cost windows for registration of rental contracts • Streamline eviction procedures and offer education of judges, as for mortgage sector • Provide consumer education and publicity campaigns on rent reforms ***Rent Decontrol:*** • Review international models of rent decontrol to further strengthen Egypt's approach to grandfathering • Condition right to bequeath to acceptance of rent increases, or limit tenure right of heirs • Support low income tenants with rental allowances in this process	***Improvements to Existing Rental Program:*** • Relax unit size constraints (to address local demand, cost differentiation) while keeping overall cost limits ***New Rental Programs:*** • Subsidies to landlords to provide housing to a low-income tenant • Project-based vouchers or soft loans to support landlord investment improving low-quality or unfinished units to be rented to low-income tenants • Use NHP subsidy as an eviction guarantee, thereby enabling recipients to use it for rental units • Use subsidy to assist down-payment (key money) for rental units

Housing System Channel	A Well-Functioning Housing Market	Improvements to the NHP
	Goal: Enhance affordability by (1) increasing access to housing finance and (2) decreasing the supply cost of housing. This dual approach to improving affordability will minimize the size of public subsidies needed.	

Housing System Channel	A Well-Functioning Housing Market	Improvements to the NHP
	Mortgage System: • Continue efforts to improve legal framework/ revise tripartite contract • Develop credit and housing market information systems • Develop new credit risk sharing programs with GSF, including mortgage guarantee insurance, to encourage expanded and down-market lending • Stop current GSF "3-month payment" guarantee • Promote GFS's credit enhancement roles • Separate guarantee function from subsidy role • Develop pre-titling guarantee by GSF for mortgage loans until registration ***Microfinance for Housing:*** • Provide support (e.g., product information, credit information, liquidity support) for development of low income housing loan products • Explore credit enhancement systems for housing microfinance in GSF ***Land Use Planning and Building Standards:*** • Increase the land development ratio (land coverage and max permissible development) • Modify regulations on building height, floor-area-ratios, and land for services • Streamline land subdivision and permit process • Make use of well locate public land for affordable and mixed-income housing • Authorize relaxed standards in specified special "popular" neighborhoods with local government regulatory control • Provide incentives for mixed-income housing developments • Provide regulation for mixed commercial/ residential use • Develop regulations for development of private land for affordable housing, including "special zones" • Inventory public lands in cities and new towns and investigate use of *Awqaf* lands • Review ban on conversion of agricultural land for urban use in special zones, especially the agricultural land pockets (*mutakhalellat*) • Enhance ongoing efforts in improving land registration • Consolidate survey and registry in one institution	***Mortgage System:*** • End below-market interest rates (10.5%) for NHP linked loans; banks to provide mortgage loans under NHP at market interest rates • Explore using interest rate buy-downs to assist affordability • Consider provisional registration or post-construction permits to allow eligibility for mortgage loan • Register properties built on State land • Consider, in the medium term, to pay for future GSF mortgage insurance guarantee, for NHP-eligible households ***Microfinance for Housing:*** • Develop a more affordable core housing scheme that is based on the beneficiary acquiring a microfinance loan • Build on current lending in microfinance for housing by National Bank of Egypt, Bank Alexandria, and Banque du Caire) • Use savings as a rationing device and underwriting tool for housing microfinance ***Land Use Planning and Building Standards:*** • Make land for NHP projects available to match employment, transport, and education opportunities/needs of low income households • Allow use of NHP subsidies for housing on non-State land • Relax land and building standards for the *Beit Al-Ailaa* (family house) and *Ibni Beitak* (build your own house) programs • Introduce mixed-use residential/commercial development to allow cross subsidies to operate at the project level

Housing System Channel	A Well-Functioning Housing Market	Improvements to the NHP
 **TARGETING**	**Goal:** Improve the targeting of public subsidies to ensure that they are provided to (1) the lowest income households who require them to obtain adequate shelter and (2) specific market segments to assist in clearing well-defined market blockages. Successful targeting along those lines will significantly reduce the need for future subsidies.	
	• Better enforcement of existing criteria to help limit vacancies and speculation • Streamline targeting methods for all federal subsidized housing programs • Consider additional targeting criteria to improve accuracy	• Pilot new targeting methods using existing mechanisms ("piggy-back" approach) o Proxy income eligibility using MOSS or food ration programs o Consider test of Proxy Means Testing o Consider use of electricity usage or car ownership as income proxies • Consider additional targeting criteria to improve accuracy o Over-crowded and/or poor living conditions; single parent families o Residents of informal areas and slums o "Group" applications for extended family moves to New Towns or other areas
 **GOVERNMENT**	**Goal:** Transform the government into an enabler of the housing market that can (1) effectively engage the private sector in the delivery of housing, (2) provide an equitable regulatory framework, and (3) formulate policies to keep the housing system on track.	
	Private Sector Engagement: • Enhance the role of the private sector in servicing and collection of rents in government projects ***Institutional Framework:*** • Establish high-level inter-agency "policy" council with a strong technical secretariat • Provide proposed National Housing Authority and high level policy council with greater policy-making and investigation/evaluation/monitoring resources • Merge/streamline public housing supply institutions to reduce duplication • Develop rental sector regulatory agency • Help strengthen the capacity of Governorates and their economic housing funds	***Private Sector Engagement:*** • Engage more private lenders via market-based lending and credit enhancements • Develop PPP policies in NHP projects that include private sector risk sharing in completion costs, timing, and marketing goals • Utilize private collection services such as those of Housing & Development Bank ***Institutional Framework:*** • Initiate a high-level inter-agency working group • Increase outreach/public awareness of NHP options • Improve budgeting by accounting for land and infrastructure costs • Monitor post delivery of NHP units for vacancies, resale and rent to third parties

II. INTRODUCTION

1.0 Objectives

The two key objectives of this policy note are to provide recommendations for a policy-based approach to housing sector reform in Egypt and to improve the efficiency of delivery of housing subsidies under the National Housing Program (NHP). The paper builds on the key findings of recent research and analysis related to affordable housing in Egypt, presents a framework for moving forward with housing policy and subsidy reform, and provides detailed short and medium/long-term recommendations for the achievement of this objective. The current effort to assist the Government of Egypt (GOE) in the formulation of effective housing policies and improved subsidy mechanisms involves close collaboration between the GOE's Ministry of Housing, Utilities and Urban Development (MHUUD) and Ministry of Investment (MOI), the World Bank, and two USAID-financed projects: Technical Assistance for Policy Reform II (TAPRII) and Egypt Financial Services (EFS). This policy note is the outcome of the collaboration of the USAID TAPRII project, the World Bank, and the GOE through the MHUUD and MOI ministerial working sessions conducted in April, May and September 2007, as well as technical meetings with ministerial representatives. The two key themes are:

- **Comprehensive housing sector reforms** designed to put in place over the medium and long-term the foundations of an efficient and well functioning urban housing market for all, by making more effective use of Egypt's existing housing stock, maximizing the role of the private sector in housing production and financing, and targeting government assistance to the poor who are unable to afford their shelter; and

- **Improvements to the NHP**, particularly regarding cost-efficiency and distributional impacts of housing subsidies, affordability, private sector participation, and effectiveness of the institutional framework, all of which can be initiated immediately and used to leverage longer-term reforms in the housing delivery system.

This document builds upon several recent studies and reports carried out in the 2005-2007 period. The first note, entitled ***Analysis of Housing Supply Mechanisms*** (World Bank), analyzes the situation of housing supply in urban areas in Egypt, including the study of existing formal and informal mechanisms for the delivery of urban housing, the institutions responsible for supply and regulation, the characteristics of the formal and informal stock, and the institutional and regulatory framework governing land use planning and development. The second is a ***Housing Demand Study in Greater Cairo*** (USAID TAPRII), which uses household data surveyed in December 2006 and yields results on the housing demand and household characteristics in the Greater Cairo Region. The third is an ***Analysis of Subsidized Housing Programs*** (USAID TAPRII), which assesses past, existing and pipeline subsidy programs in Egypt. ***International Best Practices*** were presented at a high-level workshop held in April 2007 with the intent of assessing different schemes of housing subsidies and reforms used in other emerging markets, in order draw lessons pertinent for Egypt. Finally, a note (World Bank) summarized the framework for moving from a program-based to a policy-based approach to housing sector reform, which was jointly developed by the World Bank and USAID TAPRII teams and discussed with GOE policymakers in the high-level workshops of April and May 2007, and endorsed in September 2007. These studies and reports are briefly summarized in the Annex (section VII) to this report.

2.0 Background

Until recently, GOE housing initiatives have largely focused on housing supply programs rather than the formulation of housing policies. Government-produced, subsidized housing in Egypt has been significant in scale, cost, and impact on the urban landscape. During the past 25 years, the government built as much as 36% of all formal housing units supplied in urban areas at a cost of some LE26.4 billion. Almost without exception, the land upon which the housing was built was State land in remote locations. During this era, private sector production of formal housing was small and catered mostly to the upper end of the housing market. Rampant informal housing development at the fringe of existing cities, catering to middle- and low-income households, was unsuccessfully proscribed by the authorities. Rent control was in full effect and quelled the rental market. Finally, housing mortgage systems were legally unfeasible.

Egypt has made significant progress in introducing reforms to create a more efficient housing market. Formation of the Mortgage Finance Authority (MFA) to regulate real estate activities, enactment of the Real Estate Finance Law, establishment of Mortgage Finance Companies (MFC), amendments to the Capital Markets Law to strengthen the legal and institutional framework governing mortgages, and establishment of the Egyptian Mortgage Refinance Company (EMRC) to provide liquidity to the market have all been completed. The Guarantee and Subsidy Fund (GSF) was also established with the objectives of delivering upfront housing subsidies to low-income households to enable them to access mortgage finance, providing a temporary social safety net to borrowers who experience adverse life events that lead to payment defaults as well as developing incentive products for the private housing finance market to grow and expand down-market to the low/middle-income segments. The well-attended Euromoney Egypt Housing Finance Conference, held in May 2007, successfully engaged private and public housing finance and delivery institutions with policymakers and regulators. More ambitious reforms to the housing and land markets have also been initiated. The launch of the NHP with adequate funds budgeted over a multi-year period, the reform of the land and property registration system through the introduction of a title system and major reduction in fees, and the ongoing formulation of an improved property tax law and a Unified Building Code are important steps towards a comprehensive reform of the housing delivery system.

Since the inception of the National Housing Program in 2005, the GOE has introduced numerous improvements and continues to seek innovations to help meet demand. In the course of the three years since its launch, the NHP has gradually shifted away from its initial target of the government building 500,000 new units for homeownership equally split between new and existing towns. Instead, the NHP redefined its target to a more attainable and demand-responsive goal of creating 500,000 housing "solutions", introduced rental and self-build housing options at a substantial scale in response to demand, and reached agreement with the Ministry of Religious Endowments to utilize subsidies for rental housing to be developed on the much-better located *Awqaf* land. The GOE has also explicitly budgeted for housing subsidies under the NHP, relied on transparent upfront subsidies (although subsidized land and some interest-rate subsidies still persist), and actively promoted private sector production of housing. As of May 2008, the spectrum of housing types and tenures offered under the NHP has greatly expanded, and the pipeline exceeds the initial goal of 500,000 units. Plans for affordable rental housing now exceed 211,500 units and about 91,000 self-build units are also planned. Thus, together these options far exceed the more traditional public ownership programs, at 170,000 units. Ownership units to be provided by the private sector now reach above 288,000. Mortgage lending under NHP has also been initiated. Within the GSF program (which is implemented within the scope of the NHP, even if its units count over and above the 500,000 unit target), there are currently 4,100 qualifying households that have benefited from upfront subsidies administered by the GSF, which also facilitated beneficiary access to mortgage loans through Banks and MFCs (for a total volume of approximately LE 100 million)[3]. All but 10 cases were

[3] Banks accounted for 83% of the number of loans and 81% of the total volume of mortgage finance processed by June 2007 (average loan amount of LE 22,425), while MFCs accounted for 17% of the number of loans and 19% of the total volume of mortgage finance (average loan amount of LE 26,735).

new units, mostly controlled by the GSF in new urban communities including 1,200 units in New Damietta and the remainder near Cairo and Giza (6th October, Al-Shorouk). By June 2007, as many as 18,000 applications had been received. As for the subsidies administered by the NHP agency, it is unclear how many mortgage loans have currently been extended.

Despite these promising advances, however, much of Egypt's housing stock still remains constrained by very high vacancies, rent control, and informality. A summary of main issues is as follows:

(i) **Almost 3.7 million housing units are unused, either vacant or closed.** According to the 2006 census, the total number of unused units in urban areas in Egypt reached 4.58 million units, of which 1.18 million were closed and 3.40 million were vacant. Due to the lack of detailed breakdown by unit use in the preliminary census results made available by CAPMAS, it was estimated that 3.72 million or 81.3% of these 4.58 million unused units are for housing use, while the remaining 18.7% are for work use (commercial and office space in mixed-use buildings, housing units informally converted into office space, etc).[4] The scale of vacant urban housing units, much more serious than in other emerging markets, is a specific and puzzling phenomenon of the Egyptian housing market. One explanation is that units are traditionally acquired and kept vacant for offspring years, even decades, in advance of their need. Another explanation is that the sustained rapid appreciation in value over the past 25 years or so and the lack of alternative investment mechanisms until quite recently meant that housing and real estate have consistently served as an inflation-proof savings and investment mechanism, without need of the rental yield.[5] The idea of renting was even less attractive due to the imposition of rent control until 1996. Even now, the continued perception of uncertainty about the enforceability of the new rental law makes many owners hesitant to put their unoccupied units to rent. Poor targeting of government subsidized units, as well as the mostly unattractive locations in New Towns, have also further exacerbated the problem.

(ii) **An estimated 42% of the housing stock in Greater Cairo is frozen under rent control.** Since the passage of Law No. 4 of 1996 that freed the rental market for newly built and the then-vacant units, the rental market is showing signs of much dynamism. The TAPRII Greater Cairo Housing Demand Survey found that 81% of all the new units accessed in the 2001-2006 period were through rental contracts signed under the new law (only 19% were for ownership). Yet, the TAPRII survey also indicates that 42% of the total urban housing units in Greater Cairo are still locked under the old rent control regime, and that this is not necessarily benefiting the poor. This greatly constrains residential mobility, locks a large proportion of units out of the market, causes lack of stock maintenance, and distorts the overall housing market.

(iii) **Some 45% of new urban housing is produced by the informal sector.** During the inter-census period (1996-2006), the urban housing stock is conservatively thought to have grown by an annual average of 2.8% or 263,838 units (9% higher than the annual average for

[4] This estimate is based on the fact that of the 9.74 million occupied units in buildings in urban areas (excluding work and official establishments), 81.3% or 7.91 million units were used for housing and 18.7% or 1.82 million units were used for work. The assumption therefore is the breakdown of unused (both vacant and closed) units would follow the same distribution between housing and work uses.
[5] Despite some slowdown in the early 2000s, this trend has continued unabated and has very recently reached new heights, fuelled by major inflows of foreign investment in real estate in Egypt from regional investors.

the previous inter-census period 1986-1996 where the average was 241,916 units).[6] Of these, 55.6% were formal and 45.4% informal. Constrained by high building and zoning standards, as well as a bureaucratic and costly permitting process, many families and small developers operate within the informal sector to meet the growing needs of lower income households.

(iv) **Much housing is poorly located, especially for moderate and low income families.** Government low-cost housing program are sited in the distant New Towns or on remote desert area, making the livelihood struggle for inhabitants much more difficult, if not impossible. The formal private sector, aiming mostly at the upper-income, car-owning market, also tends to prefer desert locations. Thus, housing in informal areas, which are located within or on the immediate fringe of existing cities, is in high demand.

The main challenge today is to devise affordable housing policies and strategies that address the distortions that to date constrain the housing market from functioning efficiently. The first critical steps in this regard were the abolition of the rent control legislation in 1996, after five decades during which it severely distorted the housing market, and the creation of the regulatory and institutional frameworks governing housing mortgage finance. The key remaining challenges that the new affordable housing policy will need to address are to: (i) put in place the institutional frameworks and incentive structures needed to enable an expanded private sector role in the financing and delivery of affordable housing; (ii) rationalize the subsidies provided to limited-income groups by eliminating off-budget subsidies and developing efficient targeting instruments; and (iii) ensure the development of a viable rental market to serve the needs of the lowest income groups in conjunction with some homeownership opportunities.

Improvements to the NHP can be used to catalyze improvements to the overall housing market. First, it is of paramount importance that the millions of vacant units in urban areas be activated. By allowing NHP-eligible households to use their subsidy entitlement for the purpose of renting privately-owned units, either by using the grant for down payment on a long-term lease to reduce the rent level or as a guarantee to reduce landlords' perceived risk of eviction costs that deter them from availing their vacant units, it may be possible to unlock a portion of the vacant units, facilitate residential mobility and restore the fluidity to the housing market. A pilot program such as this may also serve as a catalyst for building confidence in the rental/eviction law, and thereby indirectly unlock many more vacant units and strengthen the overall rental market. Second, pilot projects within the auspices of the NHP that aim to lower planning, land development and buildings standards as means of reducing total housing development costs could serve to demonstrate the financial feasibility of constructing housing for low income households within the formal system that can effectively compete with the informal sector in terms of affordability. Third, allowing NHP beneficiaries to use their subsidies as a down-payment to purchase existing privately-held units and enabling them to access private mortgage finance would greatly expand the demand for used housing, in addition to enhancing households' affordability and increasing their choice of where to live. Finally, the current political momentum behind the NHP to deliver the 500,000 affordable housing units as promised by the President provides an opportune moment to improve and streamline the institutional context with the aim of creating a more efficient housing production system.

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[6] The preliminary results of the 2006 census made available by CAPMAS do not allow for a precise calculation of the number of housing units. As such, the total number of housing units in urban areas was inferred as the sum of "apartment units" (in Arabic *shakka*) and "one/more independent rooms" (in Arabic *hogra mostakela*). This figure is counter-balanced by the exclusion of single family housing and the failure to account for housing units converted into offices.

III. THE LONG-TERM VIEW: COMPREHENSIVE HOUSING MARKET REFORMS

The majority of Egypt's housing stock is constrained by rent control, informality, and vacancy. The urban housing crisis in Egypt results from a distorted housing market caused by policies that have failed to reconcile supply and demand, and have curtailed the private sector. Although Law No. 4 of 1996 liberated new rental units from rent level caps, rent controlled housing that was grandfathered under the new law is still the dominant form of tenure in Greater Cairo, with 41.7% of the housing stock under its regulation. Rental under the new law is 8.7% of the stock, and ownership represents 36.8% of housing. Households in search of low cost accommodations have turned to the informal sector, which is estimated to have built about 45% of housing stock in recent years. Moreover, fears of unenforceable tenant eviction laws and escalating housing prices have motivated many owners to keep vacant units locked up and off the market. Indeed, estimates of housing unit vacancy range between 20% and 30% in urban areas. While these three distortions are not wholly additive (e.g. an informally built unit may be held vacant), it could be conservatively estimated that 50% - 75% of the urban housing market in Egypt suffers from such market distortions. These distortions continue to push up housing prices, severely limit household mobility, and place a huge housing subsidy burden on the GOE.

*The annual housing need of limited income groups in urban areas is conservatively estimated between 165,000 and 197,000 units***.** The National Housing Program, with its pledge of 85,000 units per year, would thus cover almost 50% of the estimated need. Short of the informal sector catering to the remaining 50%, this means that policy reforms need to be put in place to remove the distortions in the housing market that have kept a large number of units vacant and have stifled investment in the rental sector.

The Ministerial working sessions conducted in April and May 2007 resulted in the development of a framework for moving from a program-based to a policy-based approach to housing subsidies that was endorsed in a September 2007 workshop. Stakeholders agree that the following are the main sector issues in Egypt and that addressing these issues through a coherent and comprehensive approach is key to the transition, and specifically to the role of government and subsidies in enabling more access to affordable housing. Emphasis is placed on using the NHP's platform and subsidies to support needed reforms and decrease the need for continued deep subsidies for much of the housing production in future, while at the same time utilizing resulting housing market improvements to strengthen the NHP.

(i) **Expand affordable housing options and access to finance by addressing multiple income segments.** A large gap exists between incomes and the NHP housing supply costs. The expansion of affordable housing options should be addressed using a two-pronged approach of (1) removing regulatory impediments that increase the cost of housing supply, and (2) expanding access to housing finance, with a focus on mortgage finance for middle-income households and micro-finance and other innovative approaches to address the needs of the lowest income deciles.

Past housing assistance programs in Egypt focused on delivering a few housing products of relative high standard in remote locations, requiring high subsidies, and offering little choice or adaptability of products to beneficiaries' needs. Instead, Government should identify multiple income segments, and target subsidy programs and necessary regulatory reforms at each. As an illustration of this concept, strengthening the mortgage market addresses the needs of households with high incomes. Providing incentives for mortgage lenders to expand lending down-market would address the needs of middle-income households. Implementing regulatory reforms (i.e. adapted planning, land use and building standards) to allow lower cost housing alternatives to be produced would benefit lower-middle income families. Finally, the Government could reserve subsidy resources for the lowest income families who would not be able to obtain housing without such assistance.

(ii) **Stimulate the rental market.** A second key challenge is the need to stimulate the rental sector. The passage of Law No. 4 of 1996 freed the rental market for newly built and vacant units but allowed rent control on existing units to continue (and with provision for first-generation contracts to be passed on once to family members). Since then, and especially since 2001, the rental market is showing signs of dynamism. The TAPRII Greater Cairo Housing Demand Survey found that over 80% of all units (homeownership and rental combined) accessed in the 2001-2006 period were governed by rental contracts signed under the new law. Yet, the TAPRII Survey also found that 42% of the surveyed housing units are still locked under the rent control regime, and that these units were found to disproportionately benefit high income groups as well as the elderly. This constrains residential mobility, locks a large proportion of units out of the market, causes lack of stock maintenance, and distorts the overall housing market.

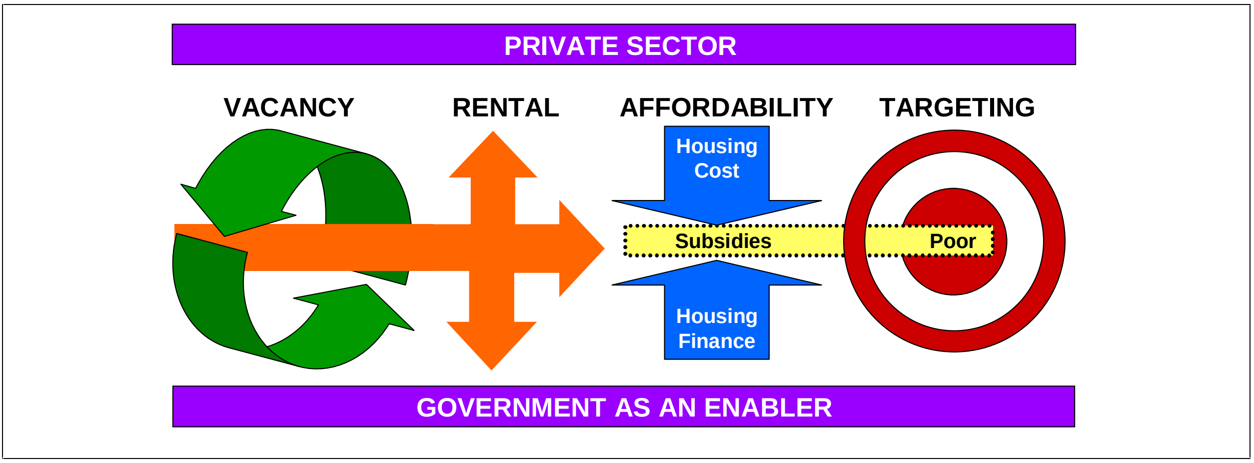
(iii) **Unlock vacant units.** Vacant urban housing units in Egypt reached 3.7 million units in 2006 (excluding instances of incomplete subdivision or buildings). The TAPRII Survey provides insights on reasons for holding vacant units, including that 60% of vacant units in Greater Cairo are held for children until marriage. Due to uncertainty about the enforceability of the new rental law, owners are hesitant to rent the units. The prevalence of vacant units is a specific and puzzling phenomenon of the Egyptian housing market, which is due to several reasons: (a) lack of incentives to rent and residual fear of rental contract complications as a result of the former rent control system; (b) housing as savings and investment mechanism, with rapid appreciation in value coupled with perceived problems associated with renting renders the annual rental yield unattractive; and (c) no penalty for holding units vacant (property tax payments are negligible). Reasons possibly explaining the high share of new vacant units are lack of financing for owners of semi/un-finished buildings and unattractive locations in the new towns, where the decision of moving in or selling the unit (and cashing on windfall profits if acquired at below-market levels) is contingent on the new towns gaining a critical population mass.

(iv) **Improve the government support system for housing production.** A large number of government agencies at the central and local levels have been active in the production and/or financing of affordable housing, often working with overlapping mandates, unclear jurisdiction and conflicting objectives and uneven terms and level of subsidies. The NHP provides a critical framework to rationalize subsidy objectives, harmonize the level of subsidies and the different institutions. The following key principles could guide the NHP: (a) separating housing production from housing finance mandates; (b) using the private sector as much as feasible, both for finance and development, (c) restructuring existing entities to minimize overlap and maximize operational efficiency (collection efficiency, production cost, etc); (d) harmonizing subsidies across agencies and establishing clear subsidy principles, effective targeting and eligibility criteria, costs, etc; (e) creating sustainable long-term financing for subsidies; and (f) improving the information base for housing markets.

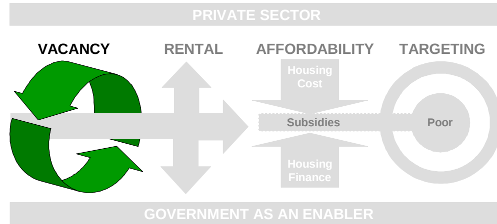
In sum, the framework for a well-functioning housing system in Egypt consists of five action channels (See Figure 2). It is not a substitute for a complete housing policy, but rather a framework that focuses on specific policy issues that need to be addressed. The framework provides recommendations for addressing existing distortions to the current *stock* of housing (vacant and rent controlled units), improving the *flow* or production of housing (decreasing the cost of housing supply) and enabling better household access to housing (improving affordability and targeting, and reforming Government role) as a way for moving forward. The five channels are as follows:

- **Vacant Units.** Unlock the stock of vacant housing through (1) tax reforms and innovative subsidy instruments that provide incentives to owners of vacant units to release them to the market and (2) developing a liquid rental market.
- **Rental Market**. Create a fluid rental market by (1) strengthening rental market regulations and streamlining tenant eviction procedures and (2) accelerating rent decontrol.
- **Affordability.** Enhance affordability of new housing options by (1) increasing access to housing finance through incentives for lenders to further expand down-market and (2) decreasing the supply cost of housing and transaction costs of accessing it. This dual approach to improving affordability will minimize the size of public subsidies needed.
- **Targeting.** Improve the targeting of public subsidies to ensure that they are provided to (1) the lowest income households who require them to obtain adequate shelter and (2) specific market segmentation to assist in clearing well-defined market blockages. Successful targeting along those lines will significantly reduce the need for future subsidies.
- **Government.** Transform the government into an enabler of the housing market that can (1) better understand housing markets and react to changes, (2) effectively engage the private sector in the delivery of housing, (3) provide an effective regulatory framework, and (4) formulate policies to have in place a well-functioning housing market/system and assist low-income households to afford housing solutions.

Figure 2: Framework for a Well Functioning Housing System in Egypt



The improvements described in the following sections are divided into (a) reforms needed to develop a well-functioning housing system that require a medium/long-term outlook and (b) reforms that are immediately actionable under NHP that will simultaneously work towards the goal of developing a well-functioning housing system and help MHUUD efficiently create 500,000 housing solutions by 2011.



1.0 Unlocking the Vacant Housing Stock

Why are there so many vacant units and why does it present a problem? There are two, interrelated reasons for the high level of vacant units in Egypt. First, real estate has proven to be a low risk investment vehicle. Because there have been few investment alternatives for Egyptians, families put their savings into housing units either for anticipated capital gains or to secure the unit for future use. Second, decades of rent control and stringent tenant protection laws deter owners from renting housing units they may not be using (either because it was an investment or an inheritance). When these two factors are combined, the result is an extremely volatile investment model. An investment in housing that does not produce a cash flow return means that capital appreciation is the sole source of profitability. This situation puts significant pressure on housing prices and thereby broadens the housing affordability gap in the overall market. Relieving this pressure, by inducing owners to rent the unused units via both incentives and penalties, will stop the trend of rising housing prices.

Since the mid-1980s, the urban housing stock's annual production rate was almost double that of the urban population growth, with the result that the total urban housing stock far exceeds the number of urban households and a significant number of units is vacant. The average annual growth rate of the urban housing stock in Egypt (3.6%) far surpassed that of the urban population (1.9%) during the inter-census period (1986-1996). By mid-2005, the total number of housing units in urban areas in Egypt reached close to 9.49 million units. By contrast, in January 2005, the total number of urban households was estimated at 6.84 million. During the inter-census period (1996-2006), the urban housing stock is conservatively thought to have grown by an annual average of 2.8% or 263,838 units (9% higher than the annual average for the previous inter-census period 1986-1996 where the average was 241,916 units). The result is that in 1996 there were 1.4 housing units per urban household and 2.64 million housing units that were vacant or unused. Taking into account multiple unit ownership (10% of urban households owned/controlled 20% of the total housing stock according to a survey based study by the Ministry of Planning in 2003), there still was in 2005 about 20% of the total urban housing stock that could be considered to be potentially available on the market, whether units ready for occupancy or those that are still under construction or which have remained unfinished for a long time.

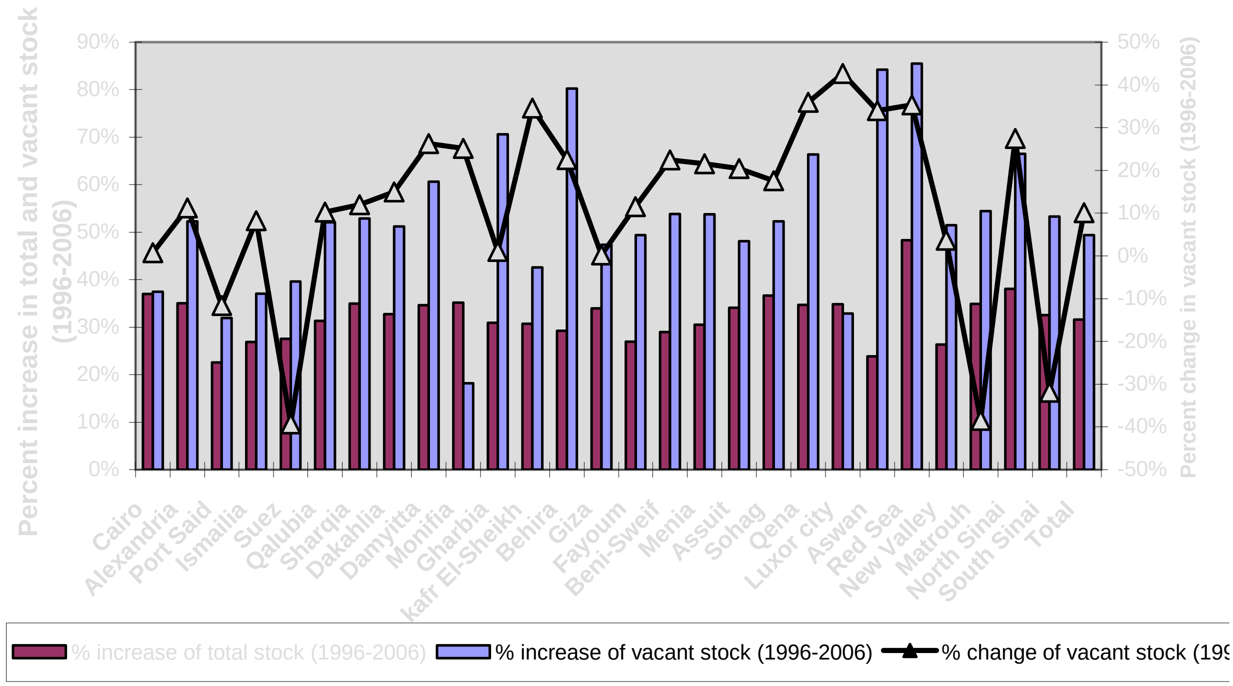
Vacancies at this level are tying up a considerable portion of Egypt's housing capital. Indeed, the vacancy rate has risen from 12.8% in 1986, to 19.1% in 1996, and currently represents nearly one-third of the stock. The problem is largely an urban phenomenon, with vacancy rates of 28% in Cairo, 34% in Giza, and 35% in Alexandria. Both formal and informal areas are impacted. Another major issue is the severe concentration of vacancies in some of the New Towns where vacancy rates of 50% or more are not uncommon. As a comparison, vacancy rates in developed markets are roughly 4% to 6%, which is sufficient to allow for turnover and mobility without affecting rent levels. Rates are higher in some emerging markets. In addition, the impact of Egyptians working abroad must be considered. However, vacancy rates, especially for countries in the region (which may also have considerable numbers of persons working abroad) generally appear lower than in Egypt.[7]

Vacancy rates increased in the last decade in nearly all Governorates. Census data provides the key source of data for an overview of the housing stock and vacant units. Figure 3 illustrates the percent

[7] The World Development Indicators shows vacancy rates of 15% in Tunisia (1994), 11% in Kuwait (1995), but only 6% in India (2001) and 4% in the Philippines (1990). During Brazil's rent decontrol efforts, a housing survey in Sao Paulo indicated a vacancy rate of 9%, with 0.2% of units closed.

change in the total housing stock from 1996 to 2006 and the percent change in the vacant and unused stock. Cairo was alone among the major urban areas for which the total stock and the vacant stock increased by about the same rate (37%). Thus, Cairo's vacancy rate stayed constant at about 28% over the decade. In Alexandria, Giza, Qalubia, and Dakahlia, however, the vacancy rates all increased, and now total one-third or more of their housing stock.

Figure 3: Change in Vacant Housing Stock (1996-2006) by Governorate



Source: World Bank, based on 2006 Census.

There are considerable vacancies in both the private and subsidized housing stock in the New Towns – vacancy rates for Government-provided housing in some districts are exceptionally high, ranging from 50% to over 90%. Studies conducted by MHUUD indicate that in many New Towns the vacancy rates exceed 40%, clearly higher than the nation-wide vacancy rate of 31.6% and the 28% rate in Cairo. Because many New Towns face serious underutilization of the housing stock, a qualitative survey focusing on the 6th of October as a case study, was carried out under TAPRII.[8] Research was conducted on private formal housing in Hay El Ashgar, an area within 6th of October New Town, and government subsidized housing constructed through the Mubarak National Youth Housing Project and the 6th of October City Authority (a semi-autonomous authority affiliated with NUCA).[9] NUCA has constructed 27,704 units (as of December 2006), 42.5% of which is low cost housing. The Mubarak Youth Housing project constructed 14,769 units in sizes ranging from 53m2 to 135 m2. In these areas, the vacant housing represents purchased but locked units, as well as unsold units. The overall vacancy rate for government housing is 35.4%. This "average," however, conceals exceptional variation in rates ranging from none in the large 6th district, to over 53% in the 10th district, 51.4% in the larger Mubarak Youth Housing units, and nearly 94% in El Amal housing. The percent of total vacancies concentrated in four districts (El Motamayez, and the 10th, 11th, and 12th districts) account for 54.5% of the total of vacant units. The

[8] See Housing Demand Study, Annex B.
[9] As has been noted, the Demand Survey utilized a sampling framework suitable for a household survey, and as such, is not an appropriate vehicle for determining vacancy rates. The qualitative survey was carried out to supplement Census data and other findings on vacancies.

vacancy rate in the Hay El Ashgar project is 84%. Of the 2,982 units sold, 80% have been delivered. Of these, 80% are closed. Clearly, both subsidized and private units in these areas are suffering from severe lack of real demand. If such vacancies exist in relatively well-located 6th of October, one can only imagine the scale of the vacancy problem in poorly located New Towns. It is also interesting to note that the other well-located New Town, New Cairo, has no new affordable housing.

Housing in the New Towns faces unique challenges requiring strategic intervention and investment. The high level of unfinished and unused housing stock surely has a negative impact on the growth and functioning of the 6th of October, and similar new cities.[10] Neither a vacant unit tax nor an improved rental market will be adequate if there is very limited demand for both subsidized and private housing in the New Towns. The special problems facing the new towns include: (i) lack of regular and affordable transportation; (ii) very low densities and immense distances with the New Towns themselves; (iii) shortage of educational services; (iv) lack of critical population mass makes for security concerns (robberies are frequent); and (v) prices for goods and services are exceptionally high. In addition, there are few opportunities for small entrepreneurs and informal activities that are so important for lower-income Egyptian families. The GOE is working on economic development plans for these areas. At a minimum, these plans should include affordable transportation to places of employment. Also, the rigid zoning regime and segregation of uses is not familiar to Egyptians. Permitting mixed-use commercial and residential development in the New Towns, and also shops on the ground floors of apartment complexes, should allow for employment opportunities and reduced household trips for daily necessities.

Egypt's high vacancy rate has numerous causes – one of these is the residual effect of rent control. The most important explanation of unused housing stock is the rent control legislation that froze rents at significantly below-market levels and which remained en force for five decades from 1944 to 1996. Coupled with stringent tenant protection laws and with courts' unwillingness to evict tenants irrespective of unit vacancy or non-compliance with contractual terms, such legislation acted as a disincentive to: (i) real estate developers, who stopped investing in the rental sector and focused development activities on high-end housing for homeownership; (ii) owners of vacant units, who became reluctant to release these to renters for fear of not being able to repossess them; (iii) building owners, who stopped maintaining units whose rental yield represented a negligible fraction of needed maintenance and capital investments, and who found themselves with a liability instead of an asset (since no investor would purchase a rent-controlled unit with existing lifetime and multi-generational tenants); and (iii) households occupying rent-controlled units (with an average rent of LE 34.5 per month), who would not release such units even if they stopped occupying them, except upon receiving a significant key money payment. It is therefore not surprising to find that owners of vacant units, whether purchased as an investment or for children's future use, would rather keep these vacant instead of renting them. This attitude is thought to have persisted to a large extent even after the reversal of the rent control law, as many owners of vacant units appear to opt for a wait-and-see approach, especially until a pattern of swift court-enforced tenant eviction starts taking place. This may be partly due to the psychological effect of rent control, but also to the long standing practice of acquiring units for children early (which reflects the lack of alternative investment vehicles).

A second important explanation is that until very recently investing in land or real estate was the only available or viable channel for investment and perceived as a safe, inflation proof way of storing wealth. Several households would thus place all their savings to acquire housing units (and where they occupied rent-controlled units, such unit would constitute their first owned unit), whether for investment or for future use, including their children's. Additionally, since real estate taxes are not likely to be a burden, there is little additional penalty for holding vacant units that could be rented out under the new law.

[10] Housing Demand Study, Annex B, page 31.

Generally, there are five categories of vacant units. First, rent-controlled units whose tenants or their heirs no longer need or use them, but which they keep until they receive what they perceive as an adequate amount of key money to be shared with the landlord. Second, there are units which households purchase for the future use of their children. Third, units or even entire buildings which remain for a long time under construction, unfinished yet or lacking access to infrastructure, as households gradually invest their savings in real estate as a way to store wealth. Next, there are units which have still not been sold by developers, a problem which was exacerbated in recent years as a result of an oversupply of real estate in the middle and upper segments of the market (including huge over supply in the New Towns) that was coupled with a decline in purchase power due to a major devaluation of the Egyptian Pound. Finally, there are the units purchased as an investment, but whose expected return is not in their potential rental yield but rather in the expected asset appreciation.

Interestingly, in the latter case, even when a household places a unit for sale, a general trend is not to settle for less than the asking price. The asking prices are often unrealistic, as they tend to project past upward trends instead of current market dynamics. It appears that many households would rather wait instead of selling short of their asking price (with little consideration given to the opportunity cost). This trend has become especially apparent in the past few years. Indeed, despite the oversupply and shrinking demand, asking prices in many cases continue to be unrealistic, which means that such assets remain locked. Finally, a generally weak property rights system due to lack of registration of land and property in urban areas further constrains the housing market and adds to the transaction costs due to the high risk associated with purchasing unregistered units, despite the reliance on proxies to registration such as *saha wa nafaz*, *saha tawqi'e*, and powers of attorney.

Egypt's housing subsidy programs have also contributed to the vacancy problem. Poorly targeted subsidies as well as an inability to ensure that recipients have not benefited from earlier government assistance may result in multiple ownerships. There is anecdotal evidence that households enter the subsidized unit lottery in order to secure a unit for their child or relative, rather than immediate use. These units, purchased at a discounted price, then remain vacant until the child marries. Moreover, the location of public housing schemes in the New Towns does not reflect the preferences or needs of many of the poor. It comes at a large cost in terms of social networks and transportation costs and lack of economic opportunities in remote locations. Demand is limited for subsidized units located in many of the New Towns because of the lack of employment opportunities, lack of amenities, high transport costs, or simply lack of transportation. Also, the initial Greater Cairo master plan was premised on the idea that the New Towns would accommodate low income workers. Low income recipients of the subsidized units in New Towns may choose to continue living in their current housing, even in overcrowded conditions, because of access to employment and social networks.

While the TAPRII Demand Survey was based on a sample of households rather than housing units, and therefore does not fully capture the magnitude of the vacancy problem, it does provide some insight as to the reasons that households claim for keeping units vacant. Of the surveyed households, 5.8% reported owning one or more units in addition to their residence. As shown in Table 2, about one-half of this group had control over one additional unit, while 18% had two additional units, and 31.5% reported owning 3 or more units in addition to their residence. The majority owned the units (68.5%) and most of the units are finished, but as much as 46.5% are not rented and remain closed.

Table 2: Status of Units for Households Having Multiple Units

# of extra units		**Tenure Type**		**Finished or Closed?**		**Rented?**	
1 extra unit	50.5%	Old rent law	14.5%	Finished	84.8%	Old rent law	34.0%
2 extra unit	18.0%	New rent law	8.5%	Not finished	15.5%	New rent law	19.5%
3+ extra units	31.5%	Owned	68.3 %	Closed	22.3%	Not rented	46.5%

Source: TAPRII Greater Cairo Household Demand Survey

Interviews with the landlords of surveyed buildings (see Table 3) highlighted their desire to keep units vacant for children so as to secure a home for them to move to when they marry as the main reason for holding extra units. Nearly 78% of households and 60% of landlords cited this as the reason for the vacancy. Respondents also cited avoiding problems related to renting – the fear that they will not be able to evict the tenant when they wish to use the unit for an alternative use. Clearly, this reason must underlie the owners' worry of not being able to repossess their units at the time that their children marry. Other reasons included that the unit was purchased as a long-term investment or it is located in an undesirable location. The majority of vacant units were closed by either their owners or tenants who had previously occupied them. Those retained by tenants could not be, by law, rented without the landlord's agreement, hence the deadlock.

Table 3: Reasons Cited for Holding Units Vacant and Closed Units in Surveyed Buildings

Reason for Vacancy	Closed Units for owners of multiple units*	Vacant Units owned by landlord not offered for sale or rent**	% Buildings in the Survey**	% of closed units in these Buildings
Holding for children	77.9%	59.7%	2.9% had….	1% - 5% closed
Long-term Investment	8.6%	9.2%	13.1% had…	6% - 10% closed
Problems with Renting	4.9%	10.0%	48.8% had…	11% - 24% closed
Poor marketability	3.4%	18.9%	27.9% had…	26% - 50% closed
No financial need	15.0%	(not asked)	7.4% had…	51%+ closed

Source: * TAPRII Greater Cairo Housing Demand Survey; **TAPRII Building Survey

Additionally, according to the building survey, 84% of the buildings had at least 10% of their units vacant. Nearly one-half of the buildings had up to one-quarter of their units vacant, and 7.4% of buildings that were surveyed had over one-half of their units vacant. Again, the TAPRII Demand Study was based on a CAPMAS sample of households, and therefore cannot be used to estimate overall vacancy rates. Entirely vacant buildings, for example, were not included in the survey.

In the TAPRII Survey, only 10.5% of vacant units were offered for either sale or rent, and they were mainly in low-income districts like El Basateen, El Marg and El Salam. Indeed, it appears that in low income and informal areas, there is greater willingness among landlords to rent their excess units. Intrinsically, it is interesting that even in the informal sector there is an oversupply of housing (estimated in Greater Cairo at 500,000 units and at 15-20% of the total stock).[11] The intersection of informality, vacancy, income and willingness to rent unoccupied units is a topic that requires additional exploration.

A survey of vacant and unfinished units, to distinguish the various causes so that appropriate programs can be put in place, is strongly recommended as a high priority action. While there are indications of multiple reasons for the high vacancy rate, there does not appear to be enough information upon which to base concrete policies, especially since the TAPRII Survey was based on a sample of households rather than housing units, and therefore did not fully capture the magnitude of the vacancy problem. Therefore, it is recommended that Egypt conduct a survey of vacant units in order to devise solutions pertinent to the various causes. *In fact, it may be desirable to conduct two types of surveys: a random sample of vacant units and an in-depth examination of a smaller selection of vacant units representing the different typologies.* The Census provides a good overview of vacancy rates by governorate, but not enough

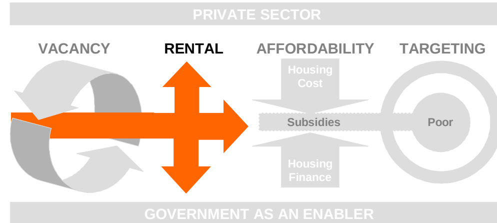
[11] The aggregate is based on the results of a sample of three informal settlements studied in detail in the Housing Supply Analysis Note.

systematic information is known about the vacant units – their location, size, quality, ownership status, completion status, costs to complete, formal or informal sector, whether they are subsidized, and so forth. An in-depth assessment of a few selected units should be carried out by an expert team who would undertake an appraisal and an engineering examination, as well as an interview of the owner. For example, unfinished units, even in the informal sector, could be assessed for costs to complete and land registration issues. In the informal sector, the units would also be examined to determine structural or infrastructure deficiencies. These in-depth assessments, combined with the vacant unit market survey, would provide information on which to project total costs for addressing various deficiencies.

The current GOE effort to revamp the property tax system should include a close review of taxation tools that could provide incentives for owners to make productive use of their vacant units and disincentives to leave them vacant. The implicit subsidies which housing enjoys in many other countries through tax breaks, credits and exemptions are few in Egypt because housing is little exposed to tax regimes. The property tax imposed by the Ministry of Finance is universal on all residential properties (even that of squatters), except in the New Towns and on vacant land. Yet, the annual effective property tax yield is extremely low due to very low assessments that are only updated once per decade, a long list of exemptions (including all new town developments), and lax collection. The Ministry of Finance is currently engaged in a major overhaul of Egypt's real estate taxation system. It is recommended that the review of the taxation system include elements such as tax deductions for owner-occupied units and rental income tax exemptions for units rented to low income households. Given the significantly high vacancy rates in some of the New Towns, it is highly recommended that the current across the board property tax exemption be removed as a means of economically dissuading owners from not renting out vacant units. Also, to be effective as a disincentive for holding vacant land for speculation, consideration should be given to expanding the property tax to include serviced land or simply impose a vacant land tax, which existed in Egypt but was abolished for technical design flaws rather than noncompliance with the constitution. In fact, the reform of property tax rates should include assessments linked to the market values of properties (land plus building), rather than the present system of assigning nominal values to the physical built space.

Encouraging the use of mortgage finance could induce more households to purchase used/vacant units or to finish incomplete units. Consumer education campaigns, speeding up property registration to facilitate sale of existing units, and promoting development of microfinance for housing to assist lower income households to complete unfinished units, especially relevant to vacancies in the informal areas, could all play a role in decreasing the vacancy rate. Similarly, credit enhancement policies to promote down-market mortgage lending would reinforce those efforts. However, it is important to note that increased utilization of mortgage finance makes sound real estate investment fundamental even more critical. The volatile investment model of purchasing units for capital appreciation alone would be exacerbated by the use of mortgage finance.

Of utmost importance, improvements to rental market regulations and operations will be crucial to alleviating the vacancy problems. Reform of the rental sector is one of the key topics of the Framework, and is addressed in the next section.



2.0 Developing a Fluid Rental Market

2.1 Enhancing Rental Market Regulation

Since the passage of Law No. 4 of 1996 that liberalized new rental contracts, the rental market is showing signs of considerable dynamism. According to the TAPRII Housing Demand Survey, the decontrolled rental sector has absorbed more than 80% of new housing acquired during the 2001-2006 period. Thus, the new law has central importance for catering to the housing demand of the young and mobile in Egypt. Additionally, the new law rent-burden levels recorded by the TAPRII Survey for Cairo average 23.3% of income. This is similar to rent burdens recorded internationally for large cities. It is likely, moreover, that the new law has improved efficiency in the housing sector by increasing housing stock turnover through lower contract durations. Nevertheless, many consider rent levels as high and volatile. Also, key money has not disappeared. Some rental contracts are still informal and provide the tenant little protection, such as against arbitrary terminations after a sale or during modernization.

2.1.1 Model Rental Contractual Agreements

The use of model rental contractual agreements that include the rights and responsibilities of tenants and landlords and other key issues such as termination, rent adjustment, etc. Such template/model agreements would ensure that key provisions of the law are part of the contractual agreement between landlord and tenant, and thus address any problems of information asymmetry, minimize ambiguities in the landlord-tenant relationship and reduce potential disputes that may arise. Such provisions include the rights and responsibilities of both parties including such issues as rent setting, payment and annual escalation, if any, security deposit, if any, responsibilities for maintenance and inclusions, utility-related issues (connection contracts, payment, etc), termination notice and proceedings, etc.

In addition, it may be warranted to introduce in the regulatory framework for rental markets a default term contract such as a 2, 3 or 5-year period that applies in instances when no contractual provisions say otherwise. Such a default term contract would ensure tenant tenure protection without compromising the landlord's rent setting capacity or flexibility to dispose of the housing asset.[12] After decades of rent control and very long-term leases, Egyptian tenants are adjusting to shorter rental contracts practiced under the new law. However, according to the TAPRII Survey, tenants still desire tenure security in the form of longer-term rental contracts. Such "default" tenure could thus balance the needs of both parties. In the case of term contracts, roll-over is the standard going forward; when the initial term ends, the landlord either gives notice or the contract will be automatically renewed for another period within the rent-setting/escalation parameters set in the contract. Clearly, options for agreeing on short-term leases should be kept, for example, if the landlord foresees alternative uses for the property in shorter time. Special termination options for the landlord and tenant would need to be legally defined both in the case of term and permanent contracts; however the necessary minimum is much less comprehensive for a term contract, which reduces the likelihood of litigation.

2.1.2 Eviction

Eviction of a rental tenant under the New Law can be a lengthy process in Egypt, and one that is poorly understood. Recent amendments to Law No. 4 of 1996 introduced provisions which benefit the landlord under new contracts. An important one is that agreements notarized in the presence of the contracting parties may operate as enforcement orders such that landlords are no longer required to have recourse to the courts to enforce tenancy agreements. These provisions do not pertain to agreements governed by the

[12] The analogy is 5 year fixed-rate mortgage which is a compromise between security and costs.

old rent law however. In addition, in the mortgage sector, Egypt already has embarked on an eviction enabling program, including both a new law and a training program for judges. This approach could be expanded to rental properties. Streamlined court procedures or extra-judicial procedures have proven to be important elsewhere. In Colombia and Brazil, for example, rental eviction case durations have been reduced within a decade from several years to 3 to 6 months. Additionally, a local ombudsman system for mediating tenant-landlord conflicts below the court level is today mandatory in a number of jurisdictions, including Colombia and Spain.

An interesting program option for Egypt could be a public eviction guarantee for social tenants accepted by private landlords. Eviction in housing is an option de-facto determined by government activity, which sets legal eviction rules, defines court procedures and determines the availability of substitute housing for evicted tenants that usually interacts with a court's willingness to spell out an evict order in cases where the rental contracts have not been registered (e.g. for a family). In several developed economies, the public housing stock provides such substitute housing. A lower-cost alternative for emerging markets, next to some public emergency shelter, could be a locally managed pool of private rental landlords offering lower quality (and cost) units, which are affordable for an evicted tenant or, if necessary in some situations, coverable by public rent allowances. Clearly, such a proposal carries a fiscal risk and should be enabled only once lease registration and streamlined eviction processes are in place. Also, groups in need for protection (e.g. female-headed households, elderly) may be targeted by such a guarantee. It requires local government initiative to define and manage the substitute housing stock, or equivalently roaster of private landlords.

2.1.3 Registration of Rental Contracts

A simple and costless registration system for leases, as practiced in Brazil and as legislated in Egypt, could have considerable advantages for Egypt. The benefits for landlords consist in access to clear and streamlined conflict settlement and contract enforcement procedures. The benefits for tenants include the protection against eviction in the case of house sale or comprehensive modernization, and other legal protections in conflict. The GOE would need to play the main role in setting up the system. Registration fees should be low to maximize enrollment incentives, and the process needs to be a simple one (arguably a registration by deposition at Real Estate Publicity Department, for units whose ownership rights have been registered). As a pay off, however, the public sector could expect greater levels of tax formality in the rental sector as well as significant revenues from the currently informal sector. The challenge, however, is what to do about unregistered units, which represent a very large proportion of the urban housing stock. It is therefore critical to sustain the property registration reform momentum, as otherwise the net effect on the rental market of strengthening regulations and streamlining eviction procedures would be negligible.

2.1.4 Taxation

An unfavorable rental tax regime may be thwarting the effort to open vacant units for rental use, as well as causing widespread informality of rental contracts. It is believed that the large majority of Egyptian rental investors pay currently no income or property taxes for their rented units. Formal property tax liability for example mainly applies to the 20% of new law contracts and a few old law contracts where rents exceed a minimum tax threshold of LE 10 per month. De-facto all the rent-controlled housing stock is tax-exempt. Moreover, local property tax evaluation committees tend to severely under-assess gross rental revenue.

Going forward, the incidence of rent control will be reduced and more contracts become formally tax-liable. An unfavorable tax regime, at least for non-corporate investors, in which income taxes on rental property are paid largely independent of the net income on the unit, is likely to keep discouraging greater formality levels. The tax base is currently defined as 50% of gross rental income, with no additional deduction possible for the higher costs of comprehensive modernization of the unit. The tax rate is up to 20%, which means that rents are de-facto subject to a flat 10% tax, reducing landlord profitability regardless of the actual profit level.

The property tax reform that is currently underway includes a proposal intended to arrive at a 10% tax rate with a tax base of 15% of gross rental revenue. This new scheme would translate into an additional 1.5% mark-up to the 10% gross revenue income tax, deepening the financial disincentive to formally register and rent an unoccupied unit.

It is recommended that the rental taxation exposure for small, individual landlords be very limited. The majority of landlords in Egypt are individuals and families who rent out one or two units. Rental income for these landlords should be reported as part of the unified income tax law. To avoid discouraging potential landlords from putting units on the rental market, there should be a waiver for the first unit (up to a specified size or value), or a waiver if total rental income does not exceed a specified level. However, for those few corporate landlords, an investment model of taxation should be used, where both income and costs associated with the rental unit are reported, with deductible expenses allowed for maintenance and repair costs, interest paid on mortgage loans taken to finance the investment, and economic depreciation.

In summary, it is recommended that Egypt continue strengthening the framework for tenant-landlord relations. The improvement of the system should include: (i) model rental contractual agreements with the roles and responsibilities of tenants and landlords, as well as strengthening the regulations governing lease termination and introducing as may be needed default contract terms; (ii) a registration system to formalize leases (for both consumer protection and taxation purposes); (iii) mandatory mediation prior to court action, e.g. through local ombudsman or property valuation committees; (iv) consumer, landlord, and judicial education regarding the revised rules; and (v) a streamlined rental eviction process (in parallel to the ongoing initiative in mortgage finance) and consideration of a public eviction guarantee as a safety net for certain qualifying households and as an additional incentive for landlords to bring their units into the rental markets. Additionally, it is recommended that the issue of landlord/investor taxation with regards to the rental market be further examined to ensure that there are no disincentives to invest in or reasons to keep units out of the rental sector.

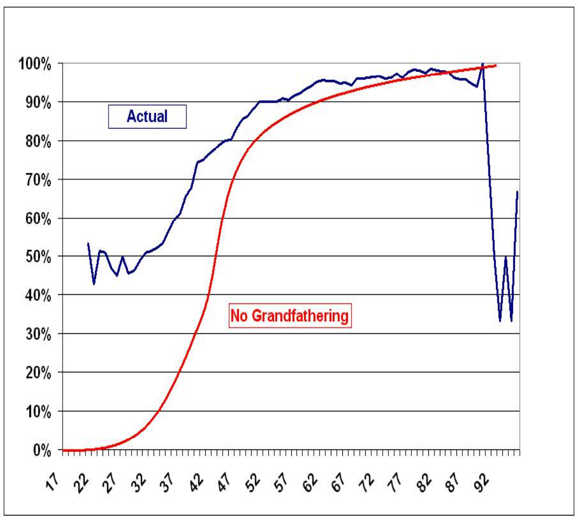
2.2 Accelerating Rent Decontrol

The series of rent control laws imposed by the GOE as early as 1944, but especially during the 1950s and 1970s, has had serious effects on the housing market in Egypt. Rent control was originally conceived as a temporary measure in the aftermath of World War II; it was later extended to preserve housing affordability for limited income groups. Rent control forced housing investors to concentrate solely on building housing for sale, which implied a focus on the upper income segment of the market. Professional long-term investors in rental housing, such as insurance companies, exited the market facing severe losses on their existing holdings. At first, rent control law applied only to units built during the 1940s, but controls were gradually extended and applied to all new construction (i.e. no targeting).

Renting is tantamount to owning, for the insiders. Rent control prompted the application of key money for new rental contracts or to release an old rent-controlled agreement. A comprehensive World Bank study on the rental sector in Cairo found that, in practice, key money is roughly equivalent to the net present value of the difference between market rent and the frozen rent level over the duration of a long-term tenancy contract.[13] In effect, renting has been tantamount to owning in Egypt, and households expect to have – and have had – exceptionally long leases relative to most other rental markets worldwide.

Bequeathing rules create new generations of insiders and perpetuate distortions. The 1996 law grandfathered existing rental contracts, thereby allowing units to be passed on one time to a family member (parent, spouse, offspring, or any relative of the first degree) living in the household 2 years prior to the death of the tenant. Indeed, this provision, although not uncommon for rent decontrol in its first phase, is frequently abused. A typical form of abuse seems to be children, or even grand-children, moving into the apartment shortly before the anticipated deaths of parents or grand-parents, just to comply with the letter of the law. Anecdotal evidence about more serious infringements includes the changing of residence on the government issued identification card and the name on household utility bills to prove occupancy. As a result, about 50% of tenants in the age group 25-35 years (household heads) are living in controlled stock, paying rents usually not exceeding 5% of stated household income (Figure 4).

Figure 4: Share of Old Law Tenants by Age Group



Source: Based on TAPR II Survey data.

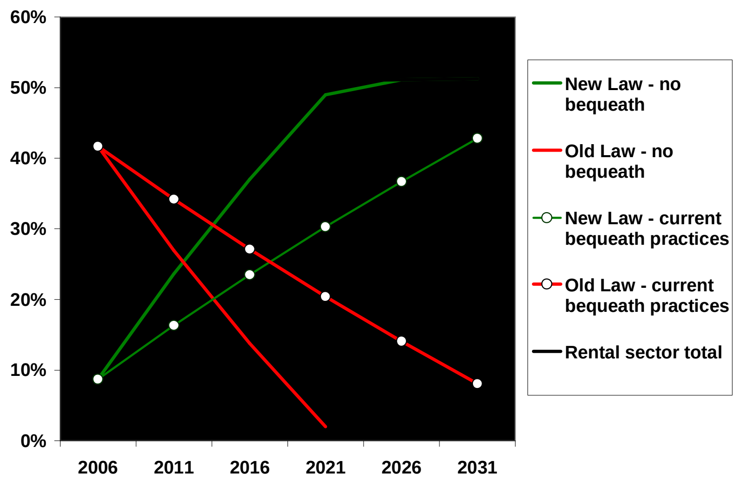
Going forward, without further action, the rent-controlled sector will remain for another three decades. As Box 1 details, the current situation of massive bequeath of old rental contracts to the younger generation will likely leave Egypt with a large part of its housing stock under rent control for a long period. A simulation presented in Figure 5 suggests that it could be three decades. Even a radical reform scenario in which bequeath would be prohibited altogether would still mean that Cairo had a rent-controlled sector of 14% of the housing stock by 2016 (Figure 5).

[13] Hardman, A, Malpezzi, S. and S.Mayo. 1995. “Egypt Rent Regulation Reform Study for the Arab Republic of Egypt”. Study commissioned by the World Bank. Cairo.

Box 1: The Cost of Doing Nothing to the Rent Controlled Sector

In 2006, already 10 years into the new law, 41.7% of the TAPRII surveyed housing units in Greater Cairo were still under rent control and only 8.7% were non-controlled (i.e. 83% of the rental stock). It can also be inferred from the survey data that about 50% of the old rental contracts are bequeathed to the next generation, for whom both mortality rates and conversion or termination incentives will remain low over the coming decades. Given this constellation, terminations of old law contracts with subsequent closing of new law contracts are unlikely to reduce the old rental stock by more than about 5-6% (referring to total housing stock), within a 5 year period. In other words, at the current conversion pace it would take more than 30 years to eliminate the rent controlled sector in Greater Cairo. By 2021 almost 21% of the housing stock would be under rent control, half of the current controlled stock. Even a radical reform scenario in which bequeathing was prohibited altogether (as was de-facto implemented in Spain in 1994) would mean that Cairo would still have a rent-controlled sector of 14% of the housing stock by 2016, and about 5% by 2021.

Figure 5: Permanence of Rent-controlled Old-law Stock in Cairo under Current Bequeath Practices and Bequeath Prohibited, % of Total Cairo Housing Stock



Source: Forecast based on TAPR II Survey data.
Note: Forecast uses demanders survey data, assuming that 80% of new rental contracts closed during 2001-2006 were old rental contract conversions/terminations and 20% from other sources (vacancies/new construction, other). Forecast does not use explicit mortality table for bequeathing tenant generation.

The cost differences between controlled and non-controlled rent contracts are considerable. Since tenancy changes in old law contracts usually come with the payment of key money, it has been claimed that average rental payments in greater Cairo – considering foregone interest on key money – do not differ substantially from market conditions.[14] However, the majority of old law tenancy changes seem to

[14] Hardman, Malpezzi and Mayo (1995)

be intra-family, where key money payments are unlikely or at most in-kind.[15] Moreover, marginal rental payments (i.e. for a current tenant facing the choice to move or stay) certainly differ, since key money is usually payable to the landlord and non-recoverable in the case of a move. This means that mobility decisions are highly affected. Figure 6 indicates rent-to-income ratios by income quintile for old and new law tenants for the TAPRII Survey households.

[15] Unfortunately the TAPRII survey did not record the level of key money paid separately.

Figure 6: Rent-to-Income Ratio by Income Group, New vs. Old Law Tenants

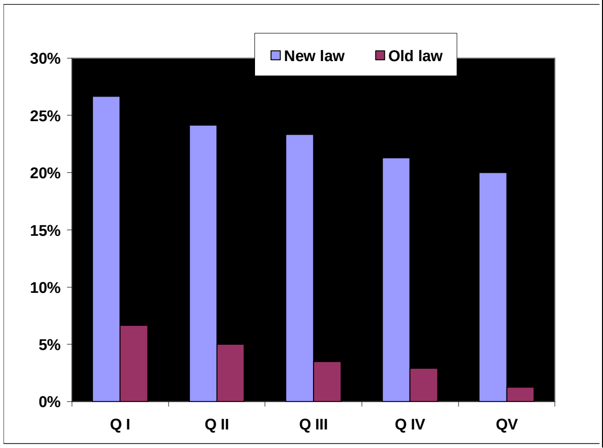
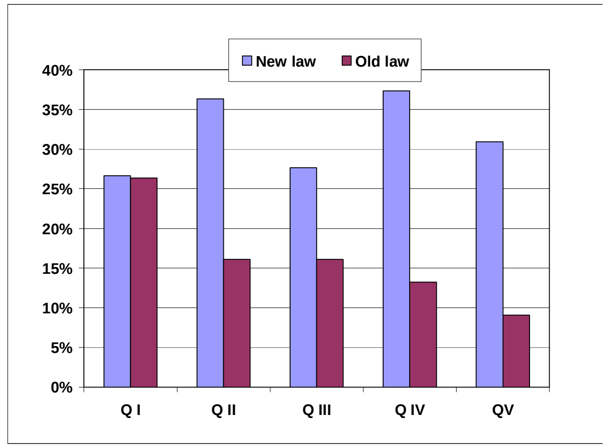


Figure 7: Total Housing Cost to Income Ratio by Income Quintile



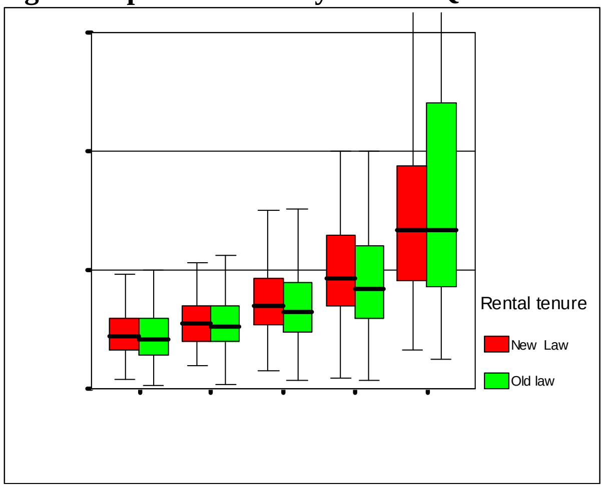
Source: TAPRII Survey data. Income is standardized for household size.

Total housing costs differ from rents for poorer households. Tenants under rent control in Cairo generally pay third parties for services that the landlord would usually provide, or whose costs would be passed through in the rent. These charges are for capital repairs, sewerage and water services, and even real estate taxes. The total of these payments, together with rent, provide an estimate of total housing costs. The results indicate that differences between old and new law tenants narrow systematically for poorer households, but not for higher income tenants. In the first income quintile, for example, the rent-to-income ratio under the old law is only 7% while the housing cost-to-income ratio is 26%, comparable to new law rent burdens. For tenants in the fifth income quintile the housing cost-to-income ratio under the old law still barely exceeds 9% while the rent burden under the new law is 20%.

Ongoing rent controls will create efficiency losses for the labor and housing markets. The wide differential between controlled and de-controlled rents provides a powerful incentive to extend old rent law contracts and reduce mobility. Indeed, the mobility indicators derived from the TAPRII Survey are very low by international standards (roughly 1.8% of families in Greater Cairo relocate per year). Since under the old rent law, many households pay far less for housing and controlled housing is concentrated in valuable inner city locations, unavailable now for higher value uses, this means also a distortion of the overall housing and land market. Moreover, rent control impedes the market process of "filtering" in which individuals with high incomes purchase expensive (often new) units, and free up older, more economical units for lower income households.

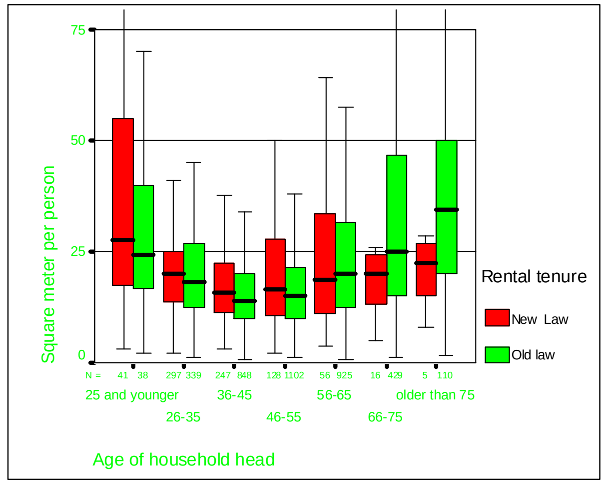
Excess housing consumption is usually a companion feature of rent control and for Greater Cairo this can be detected among the elderly and richer households. In the case of the richest households in the fifth quintile, 50% have over 33 and 25% have over 61 square meters per person. Similarly, many older households occupy large spaces, certainly partly with an eye on bequeathing them to the next generation. The bequeathing motive apparently also makes subleasing by the elderly unpopular, a common feature in rent control environments elsewhere. Finally, while the impact on vacancies cannot be observed in the TAPRII Survey data, but the low rent levels are likely to contribute to high vacancy rates. With a nominal monthly rent level of on average LE 34.5 (instead of LE 230, the market rental value), a person with an old law lease could have more easily chosen to hold on to his unit for future use by living elsewhere and keeping the unit closed or vacant for his children or for future investment. Analysis for Sao Paulo has shown that the rent decontrol act of 1991 enhanced the supply especially of small, low-cost rental units. Supply came almost entirely from units held vacant before the passing of the law.[16]

Figure 8: Housing Consumption of Old Law Age Group of Tenants by Income Quintile



Source: Based on TAPRII Survey data.

Figure 9: Housing Consumption by Head of Household



Source: Based on TAPRII Survey data.

Note: Box contains central 50% of observations (25%-75% of distribution), fat black bar represents median (50%-value of distribution).

The TAPRII survey data analysis yields several conclusions on the distribution function of rent control. First, virtually no affordability redistribution ('vertical equity') of the rent control system can be detected. The rent-to-income ratio under the old law is lower for all household income strata, including the richest. Second, the poorest households have higher rent-to-income ratios and total-housing cost-to-income ratios in both cases, old and new rental law. Third, the main beneficiaries of rent control in terms of rent differences are richer and older households, with considerable overlap of the two groups, especially in central Cairo. The highest income old law tenants consume more space than under the new law, and older tenants under the old law also consume much more space.

The rent control regime has also no systematic social safety net function e.g. for families with children. A household type analysis of the TAPRII Survey data reveals that single parents are strongly overrepresented in rent-controlled apartments. This seems to indicate social consensus, if not the law, that the partner who is not raising the children – usually the male – leaves the unit after a divorce.[17] Extended families are also strongly represented, with grandparents typically being the tenant. In contrast, nuclear families, usually young and with small children, are strongly underrepresented. Singles are overrepresented in rent-controlled stock: these are often elderly (and potentially socially vulnerable), but in many cases also young singles occupying an inherited rent-controlled unit.

International experience suggests several lessons for approaching rent decontrol. First, residential and non-residential rent controlled stock should be treated differently, with rent setting in non-residential

[16] Source: unpublished research undertaken for the World Bank in 2006 by Eduardo Rottmann.
[17] Also, the reverse causality – with the availability of a low-cost unit simplifying a divorce – should be considered, especially in the light of a high share of single parents found in the total sample.

stock being left to the market.[18] Second, rent adjustments within the residential stock should be introduced gradually to converge toward market rents in a two-step approach of rapidly covering operating cost at first followed by quid-pro-quo rent adjustments against landlord investments.

A faster pace of decontrol is not only necessary, but also feasible, as international experience shows. The closest analogy to Egypt appears to be Spain, which, like Egypt, started reforming its severely controlled stock in 1984 by completely decontrolling new contracts while keeping all earlier contracts under rent control. Transfer of contracts between the living, however, was banned and bequeaths were limited to two generations.[19] The initial reform phase was characterized by a coexistence of high and volatile rent levels in the liberalized market segment and token rents in the controlled units.[20] In 1994, a second reform law was thus promulgated with two main thrusts. First, it reformed the legal framework for liberalized contracts to provide greater tenure security, which would eventually result in a unified approach for all contracts. Secondly, they began de-grandfathering the previously controlled contracts. The de-grandfathering strategy used in Spain was multifaceted. For very old contracts (closed prior to 1964) the right to bequeath was conditioned on the tenant accepting an increase in rents to a level capturing foregone inflation. Alternatively, a tenant could forgive the right of bequeath and keep the old rent level. For all other contracts closed prior to 1984 the right to bequeath became limited to one generation, to first degree heirs only, and for them only up to the age of 25 or two years after the death of the tenant, whichever comes later. This effectively meant discontinuation of bequeaths. For all contracts, also, a mechanism to raise rents to a level capturing foregone inflation since the introduction of controls was established. If the tenant was a socially vulnerable household (under 3.5 minimum wages) unable to afford these rent levels, the landlord became eligible for a tax support scheme. A reform program inspired by the Spanish experience is about to be implemented by the Kingdom of Morocco, under a World Bank program. Liberalizations with parallels to the Spanish approach have also taken place in Latin America (e.g. in Brazil in 1991 and in Colombia in 2001).

Other interesting rent decontrol mechanisms can be found in the former socialist countries of Eastern Europe. East Germany initially moved all rents to levels covering operating costs and in exchange supported poor households via special rent allowances. Poland, Latvia and Russia similarly liberalized rents using rent allowances; in Poland, local government resistance later intercepted the rent adjustment process, however, Latvia and Russia allowed for market rent levels to be reached quickly. In the more strictly managed process in East Germany, in a second phase landlords were allowed to differentiate their rent charges within a predetermined range by the amount of investment in the unit. The investments were supported by a large public modernization loan program, requiring much administrative burden. In a final phase, many countries have adopted a reference rate (Germany) or indexation (Spain) system to govern rent adjustments and deter usurious rent levels.

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[18] Currently in Egypt even commercial property rents are "controlled" with only a 1% per annum increase in rent allowed. Attempts to raise the allowable increase have been met with strong resistance from interest groups. Most transfers of rental commercial property take place through large key money payments.
[19] Including cases in which such bequeaths had already taken place once or twice.
[20] For an empirical review, see Eastaway and Varo (2002).

Box 2: International Experience Provides Lessons for Rent Decontrol Reform

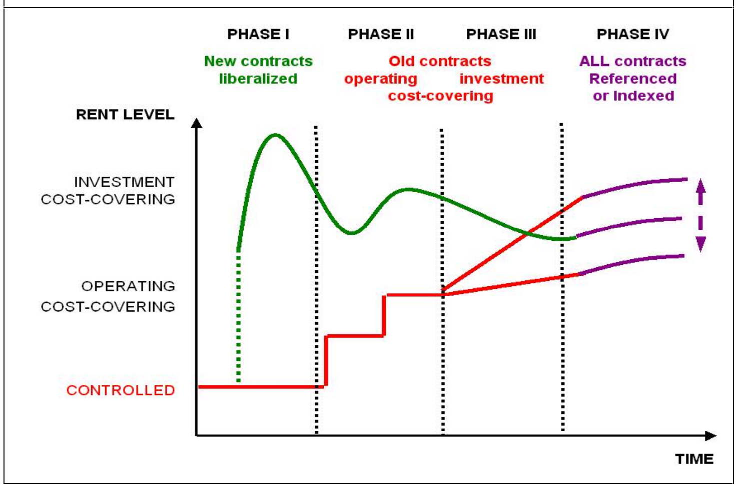
First, a gradual approach is recommended. Rent adjustments need to be phased in order to create gradual convergence toward market rents and limit the financial burden of tenants. However, initial shock adjustments are justified when controlled rent levels are extremely low compared to operating costs, in order to limit the losses from depreciation, which is the case in Egypt. Moreover, some sort of support for needy tenants should be designed. In Spain, the administrative complexities lead here to some reform delay.

Second, the agreement of tenants to a decontrol process cannot be obtained without a proportional service being provided by the landlord. This is clear in the case of rents that are not sufficient to cover current operating costs (Phase II in figure 10). However, beyond that level rent adjustments should be permitted in exchange for capital repairs and modernizations (Phase III in figure 10).

Third, final rent control regimes need to be defined for *all* rental contracts, eliminating inequitable situations between tenants.

Finally, while there is no systematic empirical analysis on the impact of liberalization on rent levels, there is ample anecdotal evidence of initial overshooting phases being followed by calmer periods, resulting in a decrease of initial tenant resistance (green line in Figure 10). The rule of thumb is that the larger the rent controlled stock relative to the total stock is, the more pronounced the initial overshooting and the more likely a subsequent relative decline in rents will be.

Figure 10: Rent Decontrol Process – a Stylized Portrayal

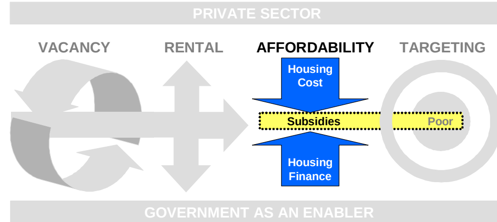


It is important that all rental contracts be treated alike. As the Spanish example shows, second generation rent legislation after an initial liberalization is often necessary in order to react to market failure, to significant increases in rent and contract term volatility, or to abuses. More importantly perhaps, in combination with de-grandfathering the regulatory system must unify the legal framework for all rental contracts and buy important political support for a de-grandfathering strategy by reducing popular anger against reforms.

Source: Finpolconsult

Political feasibility will likely be an obstacle to rent decontrol in Egypt. Many rent control beneficiaries in Egypt (mainly Cairo) are said to be wealthy and politically influential. Europe has a comparable case in the Czech Republic, where prime location rentals in Prague are occupied by members of parliament and government for nominal rents. A case has been launched to the European Supreme Court to rule on the issue. Managing the transition in Egypt will require also either allowances or tax support for landlords in exchange for accepting low rents. In the case of Spain, due to a mix of fiscal concerns and program implementation issues, the process took almost 10 years. Many Egyptian landlords are finally reportedly impoverished and have little ability to keep operations in order, let alone to invest in their properties. This is a relevant constraint, as rent increases in the first phase will be accompanied by an obligation by the landlord to fund services taken over by tenants currently (i.e. elevator maintenance, repairs, sewerage, waste disposal). In a second phase, investment in the unit should occur. One option might be a public loan program to support landlords' ability to invest. Much will depend on whether the general investment climate for rental housing improves and new, better capitalized investors will come into the market (see below).

In summary, it is recommended that Egypt initiate a second phase of rent reforms by de-grandfathering old law rents completely. When linked with the reforms proposed to develop a fluid rental market, this would create a unified and rationalized regulatory framework for the rental market. Among other measures, annual rent increases should be allowed proportional to landlord capital repairs and modernizations. Tenants may opt out of rent adjustments in return for eliminating their right to bequeath. If possible, contract term should be limited after inheritance to the juvenile phase of the heir, or to a maximum term after death. Unbundling the rent control issue, whereby income-generating (commercial, offices, retail, etc) and residential uses, are tackled through two different processes, each with its own time horizon for de-grandfathering, may also prove to be useful to decrease political resistance.



3.0 Expanding Housing Affordability

Perhaps the greatest obstacle to providing suitable housing for all Egyptians is simply that most families have very limited incomes and sources of equity. Moreover, they have difficulty devoting enough resources to housing, especially given the other pressing demands on family budgets. Only broad and equitable economic development will eventually overcome this affordability constraint. However, greater housing affordability can be reached through a two-pronged approach of (1) increasing access to housing finance and (2) reducing the cost of housing. Mortgage finance expands affordability by allowing families to pay for housing over time, while reduced land use planning and building standards allow for lower housing production costs. In the past, housing assistance programs in Egypt have focused on delivering a few housing products of relative high standard, requiring high subsidies, and offering little choice or adaptability of products to beneficiaries' needs. Instead, Government should identify multiple income segments, and target subsidy programs and necessary regulatory reforms at meeting the housing needs of each.

Figure 11 below illustrates existing gaps in the Egyptian housing market. Income quintiles that are fully served by a housing type category are shaded solid, quintiles that are partially served are shaded in hatch, and income groups not served by a housing type are not shaded. Clearly, the informal sector is serving the bulk of the housing demand from very low-income households. Moreover, subsidized housing program are not reaching the lowest income quintiles sufficiently. As mentioned previously, the social safety net that rent control provides is disproportionately benefiting upper income households.

Figure 11: Product Gaps in the Egyptian Housing Market

	Income Quintile				
	1st	**2nd**	**3rd**	**4th**	**5th**
Market Ownership	Not Served	Not Served	Not Served	Partially Served	Fully Served
Subsidized Ownership	Not Served	Partially Served	Fully Served	Fully Served	Partially Served
Rental Market	Partially Served	Partially Served	Partially Served	Partially Served	Partially Served
Rent Control	Partially Served	Partially Served	Fully Served	Fully Served	Fully Served
Informal	Fully Served	Fully Served	Fully Served	Fully Served	Partially Served

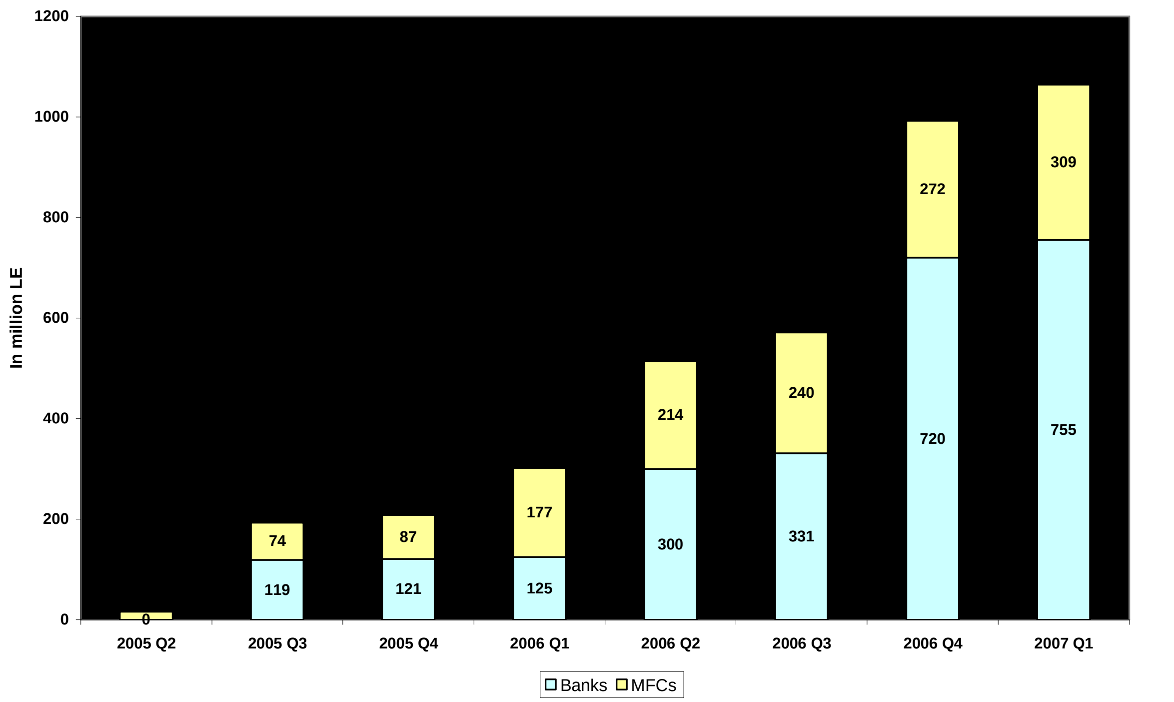
= Fully Served
= Partially Served
= Not Served

Expanding housing affordability includes strengthening the mortgage market for upper income households, permitting low cost housing solutions for the poorest households, and applying the correct mix and type of housing finance and subsidy to each income segment in between.

3.1 Strengthening the Mortgage Market for Upper and Middle Income Households

In recent years the government has placed much emphasis on activating the mortgage finance market. Although the GOE issued a new housing mortgage finance law in 2001 to enable access to housing finance, the mortgage market has developed slowly, mainly on account of the lack of land and real estate registration. The mortgage sector is still in its early stages, with just over LE 1 billion in mortgages currently registered under the new law. This rate of growth has been impressive over the last two years (see Figure 12), and the expected growth rate for next year is even higher (for example, the pipeline of mortgages under the NHP amounts to over LE 400 million). Nearly three-quarters of the registered mortgage loans have been made by non-Bank Mortgage Finance Companies (MFCs) and the remainder was issued by banks. A much larger volume of non-registered mortgages is held by banks for which figures are not known.[21] By comparison, the total amount in outstanding installment loans, the traditional way to finance housing in Egypt, is believed to be in the order of LE 5 or LE 6 billion.

Figure 12: Cumulative Mortgage Debt Outstanding in Egypt



Source: Presentation by MOI at the Euromoney Conference, May 2007.

The enactment of the Real Estate Finance Law 148 of 2001 created the legal framework for mortgage lending in Egypt (including the tripartite mortgage agreement), its principal regulatory agency the Mortgage Finance Authority (MFA), and the GSF. A liquidity facility, the Egyptian Mortgage Refinancing Company (EMRC), has recently been established with participation from the Central Bank of Egypt (CBE), banks, MFCs and the International Finance Corporation (IFC), to provide long-term funds for mortgage lending to non-bank Real Estate Finance Companies and commercial banks.

Additional regulatory changes have been made to facilitate the growth of mortgage lending:

- Law 143 of June 2006 amended the stamp-duty law of 1980 and eliminated stamp-duty on mortgage loans;
- Law 88 of 2003 was amended in June 2005 allowing the sharing of individual credit information upon the individual signing a consent clause, the establishment of a private credit bureau (Q3 of 2007), and the sharing of credit information with non-bank financial institutions;
- Clarification of Law 148 concerning the use of adjustable rate mortgages; and

[21] These are mostly older housing loans secured through non-mortgage means.

- A new foreclosure law holds considerable promise in shortening the property recovery and eviction time, and an awareness and education campaign among judges and court-personnel will strengthen the implementation of the law.

This is remarkable progress and an indication that the expansion of the mortgage sector has considerable political priority.

Similarly, progress is being made in the property and mortgage registration process:

- NUCA and MFA signed a protocol in September 2006 to stimulate property registration in the new urban communities, which is finally being implemented and is showing results. The protocol provides for the transformation of the *Takhssiss* form of land allocation (a conditional transfer of ownership) into a legal instrument acceptable to lenders. This transaction is made possible through NUCA's authorization of landholders to mortgage their contract (in effect converting it to ownership), provided that they paid NUCA the full land price owed.
- MFA, working closely with the Ministry of Justice (MOJ) issued three circulars that were widely distributed to all Real Estate Publicity Department (REPD) offices: (i) January 2007: lists the procedures governing the authentication of mortgage contracts, the registration of a mortgage as an encumbrance on the land, the requirement of lender approval as a precondition for registration of subsequent transactions on mortgaged properties, and procedures associated with foreclosure. (ii) March 2007: instructs REPD offices to facilitate block registration of NUCA landholdings (a prerequisite to the subsequent registration of *Takhssiss* contracts). (iii) Clarifies the tripartite contract. To date, over 1,000 condominium units, built by NUCA and handed over to the GSF at the time of its creation, benefited from registration. The units were made available to eligible low-income families who received an upfront subsidy and a mortgage loan. Further collaboration between the MFA and NUCA ensured that information circulars have been disseminated to the different New Town Authorities with key procedural issues related to the protocol.
- Fees for title registration were lowered in August 2007 to a maximum of LE 2,000[22] as a significant incentive for owners to register their property.

While it is still too early to assess the impact of the protocol, it is expected to have an important stimulating effect on registration and mortgage finance in New Towns, especially for first transfer instances (from developers to beneficiaries). For future transfers, the lack of capacity at the Egyptian Survey Authority (ESA) in providing cadastral information may create problems.

Regulatory areas that need to be addressed with some urgency are: [23]

- Development of guidelines for consumer information/disclosure and "truth-in-lending", standardization of loan closing procedures.
- Removal of statutory limits (Law 148) on mortgage debt-to-income ratios (now set at 25 percent). Setting statutory limits that are difficult to adjust pose unnecessary limitations on lending: (i) the 25 percent limit may reduce the borrowing power of many low-income families and hence decrease their option for home-ownership; (ii) it does not take account of differences in borrower circumstances (e.g, type of family arrangement, remittances); (iii) as Egypt's mortgage and consumer lending markets develop, a total debt-to-income ratio will become more relevant as an underwriting criteria.
- Removal of the statutory definition of what is to be considered a person or household of low-income (an individual with an income equal to or less than LE 1,000 per month or a household

[22] The fee has dropped successively from 12% in the early 1990s to 6%, 4.5%, 3%, and finally to a flat fee

[23] This section draws from Blood, Roger (2007). *Mortgage Finance Project: Prospective Use of Mortgage Default and Related Lines of Insurance in Support of Home Mortgage Financing Activity* (Unpublished report prepared for the World Bank)

with an income equal to or less than LE 1,500) and the related restrictions on the targeting of subsidy programs.

- Establishment of a regulatory framework concerning escrowing funds in support of financial transactions, including home-purchases with mortgages. Currently, deposits made by the home-buyer to the builder are not protected and segregated from other builder funds, which leaves the buyer mortgage borrower unprotected.
- Termination of the current GSF cash-flow guarantee program and redesign a mortgage insurance product that will more explicitly advance the goals of the MOI and MFA.

A major concern of GOE is the expansion of the mortgage market to lower-middle income groups who need affordable long-term mortgage finance to acquire their own home. To reach that objective, GOE established the GSF[24] under the authority of the MOI, with the mandate to develop innovative products to stimulate the private housing finance industry to grow in scale and expand down-market. While its focus has been on the mortgage market its mandate includes the expansion of non-mortgage-based finance for housing as well.

The GSF has three types of mechanisms to fulfill its mission: (i) it can issue guarantees/credit enhancement initiatives (with the full faith and credit of the Egyptian Government), (ii) provide subsidies, and (iii) engage in physical development of low-income housing for which it receives government land free of charge. This latter function is not perceived as a core task, but rather a means to raise revenue and create opportunities to initiate mortgage lending. The focus here is on its two main products: a mortgage cash flow guarantee product and a down-payment subsidy program.

The GSF offers an upfront subsidy for low-income household (defined as a LE 1,500 maximum monthly household income). The upfront subsidy of up to 15% of the value of the housing unit is capped at a maximum of LE 15,000 (initially LE 10,000), with the value of the qualifying unit not exceeding LE 85,000 (initially LE 75,000). Households are required to make a minimum down-payment of 10%. With the maximum monthly payment for low-income households set at 25 percent of income the maximum monthly payment for the program is EL375 per month. This buys a loan of LE 32,000 at current market conditions of 13 percent interest rates for a 20 year term. An additional subsidy is the exemption of payment for the GSF guarantee fee of 1 percent. Contrary to the NHP, the GSF is a demand-side subsidy issued to the borrower. It applies to existing units on the market (provided that they are either registered or deemed to be "registerable") and to new construction. However, additional supply-side subsidies apply to most new construction schemes (i.e., developers of GSF-approved schemes in new towns can apply to NUCA to obtain land at no cost and off-site infrastructure at 50% of its actual cost). The total subsidy is therefore much higher than the on-budget subsidy of LE 15,000 per household. About 4100 subsidies were allocated by May 2008.

Current explorations to make the subsidy program more accessible to lower income segments and in line with the NHP requirements include the application of a Graduated Payment Mortgage (GPM) graduating at 7.5 percent per year over the life of the loan. Such instrument would make the initial payment considerably lower. However, GPMs suffer from negative amortization through the initial years, which makes the program considerably less attractive to lenders. At the same time, the high required down-payment, the supply side subsidy and the upfront subsidy make the negative amortization risk to lenders small. The risk that household incomes do not increase at the set graduation rate is a more serious concern. Alternatives such as *the buy-down of monthly payments, say, over the first five-years of the loan* might be more market-friendly, and feasible in Egypt where savings constraints are less of a problem than monthly payment constraints. These and other subsidy issues are explored under the NHP section below.

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[24] GSF was capitalized with 1200 residential units and shops which are being sold. It holds roughly LE60 million in cash on which it earns 7 percent, and has LE274 million in receivables.

Mitigation of credit risk through some form of credit guarantee can play an important role to draw lenders into the mortgage market, and eventually, provide the comfort lenders need to move "down-market" or make loans for the renovation of rental housing that is being transferred to home-ownership. GSF has developed a loan guarantee that is mandated for every loan originated by MFCs regulated by MFA. The program provides lenders up to 3 monthly installments every five years on behalf of delinquent borrowers. It intends to avoid legal action and loss of the home when borrowers experience temporary financial distress. The fee for this credit guarantee is one percent of each monthly installment, shared by lender and borrower (but in fact passed through to the borrower). Low-income borrowers are exempt from payment but are receive the same GSF coverage.

However, rather than serving as an incentive for lending, the guarantee is perceived by MFCs as expensive relative to potential benefits, as *unfair* because commercial banks are not charged and as *an ineffective tax* because it doesn't appear to respond to a product in demand by either the lenders or the borrowers and in fact can lead to moral hazard problems if borrowers exploit their guarantee privileges. In addition, lenders have misgivings about the level of capital held by GSF to pay out claims particularly in case of a systemic reason for default. The system has not been tested, since no delinquencies have occurred. The following recommendations are made[25]:

- The GSF should consider phasing out the current guarantee product, which is focused on a narrowly defined and obligatory default guarantee that is inconsistent with best practices for mortgage default insurance; mortgage default insurance must be able to rely substantially on the recoverable value of collateral property.
- GSF should lead the way in exploring the establishment of regular mortgage insurance, most likely under its institutional structure. A special regulatory framework has to be created, the CBE and the EMRC (the liquidity facility) will have to agree to provide institutional and financial incentives for lenders to use the mortgage insurance product, and MFA will have to agree to give GSF similar favorable treatment. GSF will need to build up capacity which is a key challenge since there is a short supply of qualified people in this specialized field.
- It is advisable that the existing GSF guarantee and subsidy functions be separated. As of today, only the accounting of both arms is differentiated and the guarantee unit has not yet been staffed. But, if the credit insurance activities are to operationally activated and expanded, the different functions should correspond to distinct institutions, each with their own organization, governance, capital, funding, procedures, etc. The subsidy is intended to bring into the mortgage market households that would not otherwise be eligible for a loan by bridging the affordability gap, and it would need a constant influx of capital to pay for the subsidies towards this end. On the other hand, the guarantee function is intended to tease mortgage lenders further down-market and lower the cost of borrowing and is meant to be a self-financing.

3.2 Introducing Microfinance for Low Income Households

Microfinance for housing (MFH) is a subset of microfinance, designed to meet the housing needs of the poor and very poor, especially those without access to the banking sector and to formal mortgage loans. MFH is designed for low-income households who wish to expand or improve their dwellings, or to build a new home incrementally, relying on a series of small loans. MFH differs from formal mortgage lending in two key ways: the loans are smaller and shorter term, but more importantly they are usually not collateralized by the property. MFH clients generally cannot qualify for formal mortgage loans, for a

[25] Blood, Roger (2007).

variety of reasons, including low income, informal sources of income, lack of land title (although some microfinance institutions make this a precondition) and a dwelling that does not meet formal building standards. Relative to micro enterprise loans – namely working capital and fixed assets loans to micro entrepreneurs – MFH loans are, in some cases, somewhat larger and of longer duration. Finally, however, housing and micro enterprise loans may sometimes be indistinguishable. First, many micro businesses are conducted in whole or in part from the home, and secondly, many micro lenders have learned *a posteriori* that some portion of their SME loans are being used for housing improvements.

Egypt's microfinance industry, by far the most extensive in the region, has a broad, nationwide network of providers, including public and private banks, MFIs, and Non-Government Organizations (NGOs).[26] Intensive development work has been done over several decades, supported by the GOE, donors and foundations. Key issues of microfinance development - credit, savings, new products, regulation, and outreach - are now codified in *The National Strategy for Microfinance***,** completed in 2005.[27]

Table 4: TAPRII Housing Demand Survey Responses Regarding Households Contact with the Financial Sector

Dealings with the Financial Sector	Dealings with Banks
• Families: 16.8% • Single demanders: 10.5%	• Current account: families (7.9%); singles (4.0%) • Savings accounts: families (8.5%); singles (6.5%) • Loans, mutual funds: families (2.7%); singles (1.1%)

Plans to offer MFH are already being considered in Egypt by several banks involved in micro-lending, catering to both formally-employed and informal sector low income households; thus, the experience exists for expanding MFH to Egypt's wider network of lenders. All the issues surrounding the expansion of microfinance worldwide are being addressed in Egypt, including: commercial self-sustainability versus greater affordability through relying on "soft" money or guarantees from donors and foundations (such as USAID with the Alexandria Businessmen Association and the Social Fund for Development through local NGOs); the appropriate regulatory structures for MFIs and NGOs; and, most importantly for purposes of this Note, the pros and cons of association with government subsidy programs**.**

According to the National Bank of Egypt (NBE), their current clientele for micro housing loans cannot afford the self-build programs now offered under NHP, for example the Beit Al Ailaa, as this requires LE 25,000 upfront, as well as a loan to finish the house. The NBE loans for MFH are generally small – LE 250 to LE 5000, repayable over a one year term with APR of 30%. The clients are often from informal areas, earning livelihoods as grocers, traders, and street vendors. This raises an important issue for MHUUD – could, or should, MFH be linked to an alternative "very" affordable housing program under NHP like a self build program for a modest unit spread over a number of years or a program for completion of unfinished units? An alternative would be that the sector develops independently of NHP, although perhaps supported by MHUUD via affordable building materials, low cost housing design, or land.

NBE and Bank of Alexandria are already planning to roll out microfinance for housing loan products. NBE plans to launch microfinance for housing in the fourth quarter of 2007. Plans include loans up to a maximum of LE 5,000 with an APR of 30%. The term has not yet been decided. NBE has also been studying using MFH loans for electricity and sewerage hookups. In addition, a savings plan may be mandatory prior to granting some types of loans, and also holding 10% of the loan balance as an interest

[26] The National Strategy for Microfinance (2005) was undertaken by the Central Bank of Egypt with the Egyptian Banking Institute and the Social Development Fund with support from USAID, KfW, and UNDP.
[27] The National Strategy or Microfinance (2005).

bearing account. Since MFH loans are generally not collateralized by the dwelling (or land title), and since many borrowers are informally employed, mandatory savings are very frequently used by micro lenders worldwide to determine ability to pay and in some cases also as collateral. Bank of Alexandria also plans to introduce MFH as a product among its microfinance offerings, and is considering requesting technical assistance from USAID to develop MFH.

It is recommended that current efforts to develop MFH be supported with technical assistance on loan product development and marketing. The loan portfolio is expected to be *fully commercial*, similar to current bank loans for micro enterprise. MFH is not a panacea for the difficult problem of low income housing, however, MFH could be an important addition to low income finance and housing policy over the long-term. As part of the down-market expansion effort represented by MFH, GOE should also investigate credit enhancement possibilities for expanding MFH lending. Egypt's guarantee program for micro-enterprise finance, CGC, could be expanded or replicated for MFH, in the same way that FOGARIM in Morocco was specifically created to assist with MFH (see Annex 2.4). Support for product development and technical assistance could be provided through the donor community.

3.3 Increasing the Supply of Affordable Housing Units

Increasing the number of rental and homeownership units in the market will help to push prices down. This is especially true for well-located modest units, as these are in high demand. Such an approach underpins recommendations to stimulate the private sector supply of affordable housing (as discussed in Section 5), to bring vacant units onto the market (as discussed in Section 1), and to make rental markets more fluid and efficient (as discussed in Section 2).

3.4 Streamlining and Relaxing Land Management and Building Regulations

Several urban planning reforms are also currently taking place in Egypt. The MHUUD's General Organization for Physical Planning (GOPP) has completed a draft unified planning and building code called the Law Concerning Physical Planning, Urban Harmony, Building and Conservation of Real Estate Wealth. The draft was finalized, and it is undergoing deliberations at the Housing Affairs Committee in the People's Assembly. The Law replaces a host of previous laws and decrees and groups them under one legislative framework.[28] Importantly, it mainstreams the strategic planning process in lieu of the traditional master planning approach, and calls for decentralizing the preparation of strategic and detailed land use plans with technical assistance provided for local governments in need. The draft revised law also decentralizes to Governorates the responsibility of establishing adapted planning and development standards in urban upgrading projects, instead of the traditional reliance on national blueprint standards set in the planning law, which are unrealistically high and ill-suited to upgrading projects. However, the related Executive Regulations, which spell out actual planning and building standards have yet to be drawn up, which is critical since many aspects were referred to the Executive Regulations.

Many observers have put much hope in the new law as a means to allow more local control of planning and to allow more flexible and realistic standards for subdivision and building. However, it is difficult to judge whether this is true given that the Executive Regulations have not yet been formulated. A reading of the text of the draft law itself gives very little hint of this, and in fact seems to impose the same or even stricter hierarchical control of all aspects of planning, local development, and building. Local planning

[28] In particular, it replaces all or parts of Law 106/1976 (the building code, with its many amendments), Law 3/1982 (physical planning law), and Laws 49/1977 and 136/1981 (old rent laws).

units are mentioned as responsible for strategic and detailed local strategic plans within their jurisdiction, but both the standards to be applied and the ultimate approval rests with the national GOPP (or through its regional offices). Exemptions and variations to the law for a particular area can only be made by the national Higher Council for Planning and Urban Development (itself to be set up under the law) upon request of the concerned Governor. Building and street standards, to the extent to which they are mentioned in the draft law, seem to be exactly the same as under old legislation. It is implied that local units are allowed to set building requirements in existing urban areas which have none, and also that these units should make regulations which meet residential density limits to be set by the Executive Regulations. The Executive Regulations will also govern special zones such as downtown and historic zones, redevelopment areas, and unplanned areas. The Executive Regulations will also spell out standards and procedures relating to all building works and all fees, licensing, and supervision relating to buildings. All these big issues thus put onus on the Executive Regulations. A reading of the articles does not give the impression that the proposed law changes the already onerous, bureaucratic, and costly building permit regime, although there is emphasis on the occupancy permit. Moreover, there is no mention in the draft law of the possibility of creating special "popular" or "affordable housing" zones with special standards.

It is hoped that new Unified Building Code will overhaul the system that has traditionally been characterized by (i) complex and unwieldy building regulations, (ii) a bureaucratic and costly process for building permit issuance; and (iii) unrealistically high planning regulations and standards. Indeed, the urban planning law prescribes inadequate and mostly undifferentiated standards including low densities, limited land coverage ratios, large setbacks, and a rigid zoning regime that prescribes detailed land uses without flexibility for the market to determine land uses.

A direct result of the excessively high building standards and complex regulatory system is the vast amount of housing produced by the informal sector. Limited income groups, unable to afford formal housing or adequately located and serviced land upon which to build especially in large cities, found that they had no option but to seek shelter in informal and squatter settlements. Construction costs in the informal sector, even with a 20-30% cost add-on in extra-legal payments to circumvent problems with local authorities and utilities and navigate the bureaucracy associated with informality, are still more affordable than formal housing supply, especially by the public sector. The end housing product is also more suited to people's needs and the progressive construction method is more adapted to their priorities and affordability level. Indeed, almost 45% of new urban housing is produced by the informal sector. . During the inter-census period (1996-2006), the urban housing stock is conservatively thought to have grown by an annual average of 2.8% or 263,838 units (9% higher than the annual average for the previous inter-census period 1986-1996 where the average was 241,916 units). Of these, 55.6% were formal and 45.4% informal.

Subsidized housing schemes are constructed with building standards that are unrealistic for the Egyptian context. In terms of land needed for typical public housing estates, the public housing neighborhood diagnostic carried out in the *Analysis of Subsidized Housing Programs* shows that the average land required per unit ranged from 39m2 to 115m2, with a clustering around 70-75m2 in the New Towns and in general lower averages for governorate housing.[29] These net averages are higher than those used by the MHUUD in calculating global land needs. Using the above land ratios would yield net residential densities of between 200 and 300 persons per feddan assuming full unit occupancy by a family of four[30]. For a large housing area, the addition of land for schools, other services, open space, and major roads would reduce this residential density considerably. For comparison, mature informal urban areas in Egypt

[29] Land was the total area bounded by the perimeter streets which defined the estate. It does not include recreational open spaces or services such as schools.
[30] Feddan is a unit of measurement prevalent in Egypt and which equals approximately 4,200 square meters.

have net residential densities in excess of 1,500 persons per feddan. This is not to say the 1,500 persons per feddan is a standard that is advocated.

Subsidized housing projects in Egypt are provided, in most cases, with a good standard of basic off-site and on-site infrastructure, but this comes at a huge cost to the public coffers. A huge fiscal challenge for the development of large subsidized housing projects is that infrastructure is expensive. As part of the *Housing Supply Analysis Note*, low-cost housing and associated infrastructure cost estimates were carried out, concluding that currently the cost of servicing land, including all associated off-site infrastructure, ranges from LE 266 to LE 333 per square meter of buildable land.[31] On-site infrastructure is costly because of the high planning standards and spacious grouping of buildings and the ample open areas between them. This is particularly true of newer projects (Mubarak Youth Housing for example) in the New Towns. The land required per unit within a superblock (not counting land for schools and other services) in most cases exceeds the housing unit surface area, frequently resulting in Floor Area Ratios (FAR) that can be less than 0.7. If the associated land needed for population-serving services (schools, playgrounds, etc.) are included, then land-per-unit ratios will normally exceed 130m2/unit.

The geographic mismatch of supply and demand for housing that has exacerbated the vacant unit problem in Egypt also adds to the high development cost of housing as most housing is located in distant New Town locations. Off-site infrastructure (trunk water, wastewater, power, and phone lines) serving a public housing estate must run over considerable distances, due to the remote location of most estates, especially in the New Towns. The same is true for main roads. Thus the cost of construction of these lines can be extremely expensive, as are the associated recurrent operating and maintenance costs. The expenses associated with off-site infrastructure for subsidized housing units will only increase in the future, as more distant and remote public lands must be found to allocate for housing programs. *Identifying land within already urbanized areas where subsidized housing could be built would serve the dual purpose of matching the locational demand needs of lower income households while also significantly reducing the overall cost of development by limiting the need for new trunk infrastructure construction.* Such areas could include *Awqaf* land, agricultural pockets, and the release of unused land held by State Owned Enterprises or decommissioned uses (e.g. Nozha Airport in Alexandria and Imbaba Airport in Giza).

Improvements to the public land management system would enhance the supply of public land available for affordable housing. The problem of poor site location that is often encountered in most affordable housing schemes and especially in the new towns, and which leads to limited occupancy, owes to the fact that there is a quasi-total reliance on public land. Several improvements to the public land management system could have a significant effect on ensuring adequate supply of well-located well-serviced land and thus improve the likelihood of success of affordable housing schemes include:

- Inventory and avail well located public land in cities (unused land held by state-owned-enterprises, decommissioned land uses such as Imbaba/Nozha airports, Governorate-approved developments beyond master plans e.g. around Cairo ring road).
- Inventory and selectively avail well located public land in new towns (Sheikh Zayed, 6th of October, New Cairo) coupled with urban transport investments.
- Review public land stocks controlled by the different sectoral ministries, and which have not been used or allocated, to assess the adequacy of such stock to their sectoral strategies. Excess land stock that is no longer needed or which does not fit the proposed use (often the case with land allocated for agricultural uses, but which falls within urban expansion zones of cities) should be channel to different uses.

[31] World Bank, Arab Republic of Egypt Analysis of Housing Supply Mechanisms, October 2006, pp 23–24.

- Repossess (subsidized) public land allocated to end users which remains undeveloped beyond contractual terms.
- Improve public land asset management (inventory public land, harmonize land disposition procedures among agencies, allocate land using market mechanisms, and restrict land price subsidies to clear policy goals such as for affordable housing, measures to reduce speculation including a vacant land tax);
- Introduce regulatory instruments and avail funds to enable acquisition of private land via negotiated purchase or preemption right (agricultural land pockets, called *Mutakhalelat* in Arabic, that can be developed after updating of the municipal boundaries, called Cordons); and
- Avail the land to developers through competitions rather than negotiated or a first-come, first-served basis. Elements of the competition could be the number of low income units, the percentage of low income units in the development, affordability of the units, the lease term for rental, or the required household contribution to the unit.

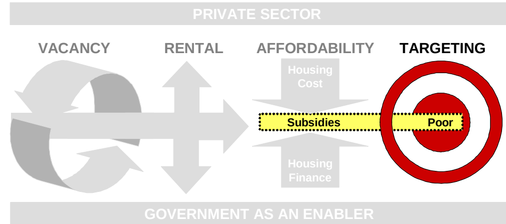
To reduce housing prices, the GOE must consider relaxed and adapted land development and building standards. Although new schemes aiming to stimulate the owner-builder or self-help housing process are being introduced in new towns, applicable planning and design standards remain higher than needed to achieve the housing affordability outcome that underlies the dynamic informal housing sector. A reduction in land allocation for services and street right-of-ways in developments would reduce the amount of land needed per unit, and accordingly the overall cost. Additionally, by permitting mixed uses, a housing development may be able to achieve a cross subsidy from the sale of rent of commercial space while also reducing residents' need to travel for distances for goods and services. Finally, improved property registration and streamlined building permit procedures would quicken the development timeframe and reduce risk and transaction cost.

Strong momentum is in place since 2004 to reform the dysfunctional urban land and property registration system. Egypt has two co-existing property registration systems. The *sejel ainee* (title registration, although in reality akin to parcel-based deed registration due to weak adjudication) applies in rural areas and is governed under Law 142 of 1964. The *sejel shakhsee* (person-based deed registration) applies in urban areas and is governed under Law 114 of 1946. It is estimated that only 5-10% of Egypt's urban land and real estate is registered under the *sejel shakhsee*. The GOE's efforts, with technical assistance from the USAID-financed EFS project and the World Bank, comprise two key initiatives:

(a) Removing critical legal and procedural obstacles hindering land and property registration in new towns in the aim of activating the mortgage market (a high demand is reported). This is carried out through the joint effort of NUCA and the MFA; and

(b) Converting the registration system in urban areas from *sejel shakhsee* to *sejel ainee*. This is coordinated and overseen by the Ministry of State for Administrative Development (MSAD) with the mandate of a commission created by a Prime Ministerial decree (No. 4 of 2004) to oversee the reform of the land and property registration system, involving cooperation between the Ministry of Justice's Real Estate Publicity Department (REPD) and the Ministry of Irrigation and Water Resources' Egyptian Survey Authority (ESA).

A well-functioning land and property registration system is fundamental for developing an active mortgage finance system, attracting investments, and creating an enabling investment climateThe launch of a systematic titling adjudication and registration program in urban areas including in New Urban Communities is a critical, albeit a massive, undertaking. The design of such program would need to avoid the pitfalls of the *sejel ainee* process that was applied in rural areas in Egypt, and which converted historically registered deeds into titles without adjudicating the titles or acknowledging the prevailing land possession (in Arabic *Hiyaza*) at the time of registration (it can mainly be credited for creating for each property a Cadastral Information Form). The proposed program will need to undertake the legal adjudicate of titles and reflect today's *Hiyaza* reality, in addition to vigorous community awareness and dissemination campaigns on the benefits of registration. In parallel, the simplification of the registration process is critical to remove a major disincentive to demand (e.g. removing duplicate steps such as the REPD checking on the survey work of ESA and iterative REPD-ESA steps that require applicants to visit each office 3-4 times at least; examining the feasibility of reorganizing the process to start with the legal component in REPD followed by the technical/survey component at ESA; discontinue the current practice of issuing of building permits and utility hook-ups without registered title/deeds).



4.0 Developing Effective Targeting

Although government subsidized housing programs are aimed at households with low incomes, there have been only limited attempts to target beneficiaries based on income, wealth thresholds or means tests. In fact, in most government housing programs the required qualifications are of the most rudimentary, with available units being distributed through administrative channels on the basis of waiting lists or by lottery if demand exceeds supply. Over decades the Egyptian government has relied on a standard application process to begin the housing unit distribution process. Authorities announce a new housing program and accept filled in applications (*istimarat*) from citizens. In the governorates, citizens in need of housing can apply at any time at the housing directorates. Although targeting and distribution of units varies from one governorate to another and even within a governorate from one year to the next, there are some common requirements. First, citizens wishing to acquire government housing units purchase applications from the Housing Directorate (usually LE 5 to LE 20). Second, it is usually required that an applicant be living in the governorate (as recorded on the ID card) and that he/she be married. Other criteria might apply, such as a statement that the applicant has no residential property. In any event the submitted application is screened and if considered accepted it is put on the waiting list. When a number of units (usually a phase of 250 to 1000 units in a particular site) are completed, either the oldest applications are picked by their date of submittal or all qualifying applications are submitted to a lottery and applicants are picked randomly until the required number is reached.

In 2001, MHUUD developed a basic point system under which beneficiaries qualify and units were to be allocated, but the scoring does not appear to be focused on low-income households. For example, higher points are given for applicants that are older and have higher education levels. It also puts an emphasis on those who are married and have more than one job, and gives considerable weight to those working in new towns. Whatever the merits of this point system, it is understood that it has hardly ever been used. Since most MHUUD housing is in very remote desert locations where there is little urban life, practically anyone can qualify for the purchase of units if they meet very simple requirements and can come up with the reservation down payment.

In all programs the allocation of units in a particular housing project is random, with valid applicants assigned units through lists. There is no means for a group of families to acquire units in the same building or area, and thus they cannot hope to bring with them even a fraction of the social networks and capital embodied in extended family or co-worker relationships. (Such is extremely important for those of limited income.) This stands in stark contrast to how general housing markets, including those of the informal sector, work. In these cases one knows exactly the unit being purchased or rented, including the pros and cons of the neighborhood and who will be neighbors. In new, and especially informal, residential areas there is the ability to re-produce at least some of the "social glue" upon which livelihoods of the poor depend. In new public housing, by contrast, one will be living with complete strangers. (It is no accident that theft is a common complaint in some new public housing estates.)

The TAPRII Survey indicates two very specific types of groups are currently looking for housing: young single men, mostly wishing for a unit in order to marry, and families within larger family units, many of whom are overcrowded or face various deficient conditions. Their characteristics are summarized in Table 5 (additional information on the "demanders" from the TAPRII Survey is found in Annex 1.1). Notably, both groups strongly prefer Greater Cairo and prefer a long-term rental contract rather than owning (although the family demanders are somewhat more likely to want to own). Some of the single demanders, even though their current income is low, are highly educated, and their future "permanent" income, combined with help from their families, may enable them to rent or purchase without a subsidy. On the other hand, current family "demanders" tend to be more overcrowded relative to the rest of the sample and to have more housing deficiencies. Probably as a consequence, they are significantly less satisfied their current housing conditions: 34% of the family demanders are dissatisfied with their housing, as compared with only 12.8% of the single demanders and 6.8% of the entire "non-demander" sample. The young, single demanders are more willing to start "small" according to survey results. Nearly half of them expect to get help from their parents as compared with less than 10% of the family demanders. Thus, the income circumstances of the parents should perhaps come into play. Similarly, 57% of the family demanders expect to get no outside help at all, as compared with 38% of single demanders.

Table 5: Profiles of Housing Demanders

Profile of individuals looking for housing (primarily young, single men)	**Profile of families looking for housing** (Average family size = 4.1)
• Income: lower overall, many with no income • Many are highly educated • For some, "permanent" income likely to exceed current income • 63% prefer long-term lease; 32% to own • Savings: lower than the demander families • Their families will help them purchase a unit • 71% prefer staying in Greater Cairo; New Cairo is the top choice among New Communities	• Frequently living with extended family • Over-crowded relative to rest of sample (35% have <40m2; average 1.6 persons per room) • Housing units tend to have more deficiencies • Significantly less satisfied with current housing • More frequently under new rent law at present • 60% want 80m2 or more • 54% prefer long-term lease; 37% own • 67% prefer staying in Greater Cairo; 6th October is the top choice among New Communities

Source: TAPRII Greater Cairo Household Demand Survey

Clearly, the "family demanders" and "single demanders" differ from one another. This merely serves to emphasize the point that some decisions should be taken as to which groups are "most deserving" of subsidy, rather than relying on self-targeting and the limited information that is currently collected in the application process. For example, a case can be made for a priority status in the NHP subsidy programs for low income families living in inadequate or crowded housing conditions. Other criteria, such as single parent households or nuclear families within large extended families, may serve to further refine the category of households "most deserving" of subsidy assistance. In contrast, young men – especially those that are single demanders – often have good future income prospects. Thus, they may be second priority candidates, best suited for rental housing, subsidized or non-subsidized, depending on their income and other circumstances. Rental units freed up under a vacant units/unfinished units program may offer opportunities. This is could be true for the sale of used units as well. In many societies, young people begin with small (often shared) rental housing, and proceed over time to larger rental units or home ownership.

Income verification is difficult. Although some 60% of demanders stated they have provable salaries (government and formal private sector employees), these salaries may well be only part of total household income, with additional incomes coming from secondary jobs, small business activities, rents from properties, transfers, family support, etc. In fact, some government employees have very lucrative alternative sources of income which are several times greater than the nominal salary. Also, the 40% of households stating that they could not document or prove any source of income is presumably is the self employed and those who work in the informal enterprise sector.

The Ministry of Finance has recently introduced a unified personal income tax system with national application. The minimum taxable income that must be declared exempts most limited income families, and these are precisely those families that any housing subsidy system would aim to target. The personal income tax system could be used, however, to help screen out those who are not eligible.

What might be effective identification and targeting mechanisms that could be implemented?[32] It is relatively straightforward from identity cards and other documentation to verify the age, gender and educational status of the applicant (head of household or individual demander), his/her marital status, and the number of dependents. The official town of residence of the potential beneficiary is also noted on identification cards, but frequently this has no relation to the actual, current address. This information, while verifiable, does not provide enough information to target subsidies. And the use of these cards would exclude those without official personal documentation, who tend to be the poorest.

- **Self-targeting is the least administratively burdensome method for targeting subsidies.** By providing small units or a less sought after forms of tenure (i.e. rental), higher income households will likely choose not to pursue subsidized units. This type of self-targeting has successfully been used in Egypt. But self-targeting may still exclude those in most need. For example, large families may be "self-screened" out of small units. Similarly, those without the required income documentation will be screened out even though they are likely to be lower income (self-employed, or informally employed). Projects in the new cities will screen out those without employment in these cities, without their own means of transportation, or who cannot afford costly transportation back and forth to their current places of employment. Finally, self-targeting still may not focus precisely enough on those most deserving of better housing, such as families with extreme overcrowding or poor housing conditions.

- **'Piggy back' housing subsidies on to other GOE safety net targeting programs.** The Ministry of Social Solidarity (MOSS – formerly the Ministry of Insurance and Social Affairs) runs both small pension and small social assistance (income support) programs aimed at the very poor and destitute.[33] This is run through an extensive system which includes 2,500 local welfare offices and 20,000 social workers. Eligibility includes widowed or divorced housewives, and a kind of means testing is applied (through home visits) to confirm eligibility. One weakness of the program is that eligibility requires full personal identification documentation, which some of the poorest segments of society do not have. Another piggy-backing possibility would be to link housing subsidies to the food ration card system. This system currently is very poorly targeted (relying mainly on self-targeting due to the poor quality of the rationed goods), but the GOE is currently improving the system, with the introduction of electronic ID cards to replace the ration cards. However, as with MOSS social assistance programs, eligibility requires full personal identification documentation, which some of the poorest households may not possess. There are also suggestions that the cash-transfer social assistance programs be modified to target mainly families with large numbers of school-age children. This kind of "conditional cash-transfer" approach, if instituted, could open a path for certain types of housing assistance.

- **Use proxies to estimate family income.** Proxy Means Testing relies on several correlates of poverty to identify the poor and, theoretically at least, can produce significant improvements in poverty targeting and outcomes. In a recent World Bank study, Proxy Means Testing was

[32] See David Sims, "Contributions to an Affordable Egyptian Housing Strategy", Consolidated Report, The World Bank, June 2007

[33] For more information on GOE's social assistance programs, see World Bank, "Egypt – Towards a More Effective Social Policy: Subsidies and Social Safety Net, No. 33550-EG, December 2005.

identified as having good potential in Egypt, and it suggests correlates or variables which be used, such as household head age, number of adults in a household, number of children in a household, women household head, educational status, and a number of others.[34] However, this approach has never been tried in Egypt, even on a pilot basis. Electricity consumption of a household has been suggested as one single income proxy to identify poor families.[35]

- **Family wealth assessments.** Assessing family wealth by asset inventories might have some screening value, but it might err both in exclusion and in leakage. Also, the administrative burden would be considerable. In addition, such items as a vehicle or air conditioning ownership may reflect historical asset acquisition rather than current income.[36] Even so, statistically there is a strong correlation between household assets, particularly owning a car, and predicted per capita consumption (see Table 6).

Table 6: Selected Asset Ownership by Household Income Quintile, Greater Cairo

Income	Automobile (%)	Automatic Washing Machine (%)	Mobile Phone (%)
Quintile 1	0.7	15.4	23.5
Quintile 2	1.7	26.4	40.1
Quintile 3	6.1	39.8	54.8
Quintile 4	12.7	58.2	73.8
Quintile 5	50.8	85.0	89.8

Source: TAPRII Housing Demand Survey

Leakage can frustrate attempts at targeted subsidy distribution; random checks may assist in keeping this to a minimum. Assuming that it were possible to effectively allocate subsidies for housing acquisition based income and other characteristics, there is no easy way to ensure that the targeted beneficiary actually lives in the unit, except through burdensome repeat inspections (which may be open to abuse). It is not uncommon, for example, in subsidized government housing programs for relatives of the qualifying beneficiary to live in the unit, or for the unit to be sold or rented to third parties, sometimes directly after delivery of the unit to the beneficiary. Random inspections should be carried out to determine the extent of leakage and to whom use of the unit is being transferred. If the new occupants would otherwise have been eligible, the course of action would be likely to differ than if a clearly ineligible household is the new occupant.

While the approaches discussed above could be applied to reduce abuse and leakage, the consequent administrative burden could be very high. Piloting a new application process under NHP would provide an opportunity to test these new approaches and build relationships with supporting agencies such as MOSS. A pilot program under NHP is outlined in Section 4 of Part VI.

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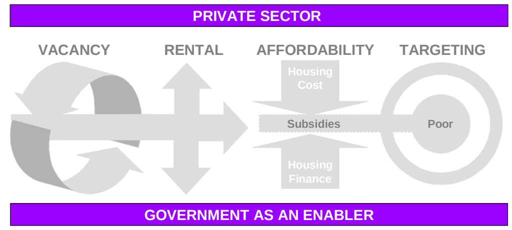
[34] World Bank, op. cit., Annex B.

[35] Studies have shown that there is a relatively strong relation between average electricity usage (Kwh per month) and per capita income (by quintiles). And practically all households consume electricity officially and can easily provide monthly bill statements. Yet the whole energy sector is riddled with subsidies and reforms in rates are being considered. These reforms will inevitably change electricity consumption patterns and thus it may be difficult to set up threshold levels for subsidy eligibility until such reforms are enacted. Also, if significant housing subsidies are linked to electricity consumption, and this link becomes well known, scenarios for abuse can easily be imagined.

[36] It is common for much of an Egyptian family's assets to have been acquired after the breadwinner returned with substantial savings from working abroad.



5.0 Enabling the Housing Delivery System

Enabling the housing delivery system includes effectively engaging the private sector in the delivery of housing, providing an equitable regulatory framework, and formulating policies to keep the housing system on track.

5.1 Engaging Private Sector Participation

The GOE must proactively assume its role as an enabler of the housing market rather than a producer of housing units. Experience in most countries[37] in similar stages of urban development and economic growth as Egypt's clearly shows that government's proper role in housing is to guide and regulate the private sector and to avoid directly producing housing, except in very special cases. Successful housing agencies in these countries concentrate on indirectly influencing both the supply and demand side of the housing equation, using subsidies sparingly and rather sharing risks which the private sector is unable to take. Significantly, the GOE's ability to form effective partnerships with private housing developers is key to meeting the goal of providing 500,000 housing solutions under the NHP in the short-term and to the long-term sustainability of enabling the provision of affordable housing in general.

Over the past 25 years, the public sector built as much as 36% of all formal housing units supplied in urban areas, which came at a significant fiscal cost of LE 26.4 billion. A plethora of public agencies and programs for direct affordable housing supply exist in Egypt including Governorates, NUCA, the Joint Projects Agency, the General Organization for Housing Construction Cooperatives, the Housing Finance Fund, the HDB, housing and development companies, and several development agencies. Together, these entities have delivered 1.26 million public units during the period 1982-2005 (36% of all formal housing units built during this period in urban areas) at a total cost of LE26 billion, excluding additional off budget subsidies related to the cost of land and off-site infrastructure. The largest supplier has been the Governorates with 44% of the public housing built in urban areas, mostly for low-and moderate-income households, which demonstrates the involvement of local governments, although the impact was reduced by limited local revenues and their activities focused on direct supply instead of enabling access of other investors to affordable land and housing. Although cooperatives delivered 22% of the public stock produced in the 1982-2005 period, they have been losing ground along with a falling budget[38], as well as the NUCA responsible for 20% of the public stock.[39]

At the central government level, housing programs have been dominated by public developers, public lenders, and assumption by MHUUD of all risk. Project development and construction is currently the main area of public-private cooperation. Developers are usually direct contract partners of MHUUD without any risk sharing such as commercial risk, marketing risk or credit risk. There is also an issue with the lack of a level playing field, as payment of the NHP down payment subsidy to private developers occurs only after the construction the phase (up to a maximum of LE 10,000), while public developers receive it at construction start (for the full amount of LE 15,000).

The positive trend of increased private sector participation and investment needs to be capitalized upon, and further obstacles removed for the private sector to play its lead role in housing supply. Between

[37] World Bank, *Housing Enabling Markets to Work*, April 1993.
[38] Now less than 20% of a LE1 billion peak per year (recorded in the 1995-1998 period).
[39] Their investment has also fallen to 5% of its former peak of about LE1.1 billion per year in the 1997-99 period.

FY2001-2002 and FY2004-2005, the private sector contribution has reached 88-90% of all new formal units with an average of 145,000 units per year while the public sector's annual average has fallen to 18,000 units. The public sector is withdrawing from direct supply while an invigorated private sector is playing an increasingly important role. Adequate (supply-side and/or demand-side) incentives need to be provided for the private sector to cater to the needs of low and moderate income groups, including making available well located and serviced land, streamlining bureaucratic procedures for land subdivision and building permit issuance and property registration, and enhancing the end-users' affordability levels through, among other things, enhanced access to mortgage finance.

Other areas of possible public-private cooperation in Egypt could include:

- **Developer finance.** The lack of developer finance is particularly problematic, as consumers are currently providing the bulk of development finance. Mexico's public agency SHF has addressed this issue by developing a monitoring system for low-income housing developers enabling it to provide guarantees for market-based bank developer finance and even securitizations.

- **Rent and mortgage payment collection.** Mortgage finance collection in the public lending channel has been outsourced in several instances to the Housing and Development Bank such as by the Alexandria Governorate. Privatization of this function is not essential as long as this is efficient, but could be a possible route to secure long-term sustainability. Private rent collection is today a standard in many Western European social housing developments.

- **Maintenance/ property management.** An important area to be explored for public-private cooperation could be property management, especially with an eye towards addressing the vacancy rate within public housing programs (both ownership and rental). Simple management or servicing contracts keep the investment on the public balance sheet, but shifts management and collection risks to the private sector.

A particularly problematic area, not limited to Egypt, is the failure to protect the public sector from downside risk. Current cost- and risk-sharing arrangements are purely contractual, due to the absence of a public-private partnership regulatory framework that could possibly govern the relationship. A common feature of such contracts is lack of clarity about risk sharing arrangements, often resulting in subsequent 'negotiations' between private and public parties about sharing losses. This minimizes both parties' incentives to mitigate risk (i.e. better planning, design and operating joint projects). Currently, private developers participating in the NHP barely face any commercial risk. Land is provided at a subsidized price and paid over time, thus requiring only a limited outlay of capital upfront. Consumers purchase the unit before construction, reducing the amount of developer capital needed to construct the unit. If construction costs increase, it is added to the sales price. Under these conditions, it is clear why so many of the developers who applied to participate in the NHP opted for the 100% subsidized option.

If private developers are required to share in the development risk, there must be sufficient compensation or upside to make the transaction financially feasible and commercially attractive. In short, they must see additional reward for assuming the additional risk. One way of accomplishing this is to allow for a greater mix of incomes (subsidized and non-subsidized units, which is also useful in reducing the risk of ghettoization of poverty and limiting the neighborhood risk to lenders) and a greater mix of land uses in large scale projects as a means of providing the developer more upside and reducing the amount of public subsidy needed to make the development project economically feasible. Another means of compensation is to give the private developer more flexibility to respond to changing market conditions, other than simply raising the sale price. If land is purchased at the "market" price from the government, perhaps there could be flexibility in the number of subsidized units to be sold or the type of subsidized unit. To provide further flexibility and spur innovation, the developers of large-scale projects should be granted some flexibility in land use standards (plot sizes and configurations, mixes of uses, etc.) to allow them to use design innovation as a means of reducing cost while retaining the quantitative target of the program in terms of number of subsidized units. Like the Planned Unit Development approach that is prevalent in the US, overall project design could be considered for permitting and approval rather than strict adherence to the zoning code.

Box 3: Application of Public and Private Partnerships to the Housing Sector

A Public-Private Partnership (PPP) refers to a contractual agreement formed between a public agency and private sector entity that allows for greater private sector participation in the delivery of an asset or service. Expanding the private sector role allows public agencies to tap private sector technical, management and financial resources to achieve public objectives such as greater cost and schedule certainty, supplementing in-house staff, innovative technology applications, specialized expertise or access to private capital. At the same time, the private partner has the chance to expand its business opportunities in return for assuming the new or expanded responsibilities and risks.

Risk sharing and transfer in a Public-Private Partnership (PPP) is based on two principles:

1. Share or cover risks only where the private sector cannot deal with it (e.g. catastrophic risks) or where the public sector has an information or management advantage (e.g. eviction).
2. Trade private sector risk protection against public subsidies in order to avoid public sector downside risk.

The first principle, as applied to housing, means that classical construction project risks, such as cost overrun risk, warranty risk, project marketing risk, as well as services such as rental and mortgage origination and collection risk should be borne by the private sector. The reason is that these are operational risks for which private sector firms should be sufficiently capitalized. Government should share risks, where private capital is insufficient or private sector has no risk mitigation at hand to manage the risk.

There are certain catastrophic risks, however, such as private counterparty bankruptcy or large swings in funding costs and inflation, where government is either automatically sharing risk, or should share risk in order to keep the private sector cost limited and help mitigate this risk. The case of counterparty bankruptcy has been notorious in miscalculated infrastructure PPP schemes, for example, in Britain. Applied to the case of housing in Egypt, the instances of bankruptcy appear to stem from project marketing and funding cost risks. Marketing risk sharing (the 50/50-model) is already practiced in Egypt; public risk shares could be further reduced over time.

The second principle – trading private sector risk protection against public subsidies – is common in Egypt. A private developer assumes the risk of building housing in exchange for a subsidy from the government (either in the form of grant funds or subsidized land costs).

A key element of any PPP is accurately calculating the cost of the risk sharing arrangement. To avoid falling into the trap of overly subsidizing the private sector, which would create serious market distortions, it is important to measure the private sector need or gap in making a financially feasibly transaction.

5.2 Rationalizing and Improving the Institutional Framework

Institutional reforms are needed to streamline the housing delivery system and better match housing subsidies with low-income households. Specifically, reforms should include: (i) unambiguous policy adoption of government's role as an enable of housing markets/systems, leaving housing supply and housing finance ultimately to the private sector with the provision of subsidies to cater to the needs of those unable to afford their shelter; (ii) merging, streamlining, and reducing existing public housing supplier institutions; (iii) developing a regulatory agency/function for rental housing markets and for housing construction; (iv) developing a function for managing incentives and subsidy instruments targeted at private sector lenders and developers; (v) putting in place a monitoring and evaluation framework/entity, which would feedback into the policymaking process; (vi) developing effective agencies at the Governorate level, with a separation of financing, development and regulatory functions; (vii) developing effective targeting and screening functions (through engagement of the MOSS, MFIs and lenders' underwriting capacity, NGOs, etc); (viii) developing capacities for public awareness, campaigns, and outreach; and (ix) creating a high level Housing Policy Council as the policymaking arm of the GOE.

A review of GOE entities which currently deal with housing shows that they are almost exclusively aimed at aspects of the supply of housing units. This is true both for the bodies which are under the umbrella of the MHUUD and also those found at the governorate level. Table 7 presents a matrix of current housing institutions set against their main functions.

Table 7: Current Housing Implementation Matrix

	Programming	Land Development	Housing Production	Financing	Risk & Guarantees	Subsidies	Targeting & Allocation
MHUUD				Strong		Strong	
NHP	Strong						Weak
NUCA	Weak	Strong	Strong	Weak	Weak		Weak
Coops	Weak	Weak	Strong	Weak	Weak		Weak
Joint Project	Weak	Weak	Strong	Weak	Weak		Weak
Hsg Finance Fund	Weak	Weak	Strong	Weak	Weak		Weak
HDB			Weak	Strong	Strong		Weak
MOI	Strong						
GSF	Weak	Weak	Weak	Strong	Strong	Strong	Weak
MFA	Weak			Strong			
National Banks				Strong			
CBE & NIB				Strong		Strong	
Mortgage Finance				Strong			
Governorates	Strong	Strong	Strong	Strong	Strong	Strong	Weak
Formal Private			Weak	Weak			
Informal Private							

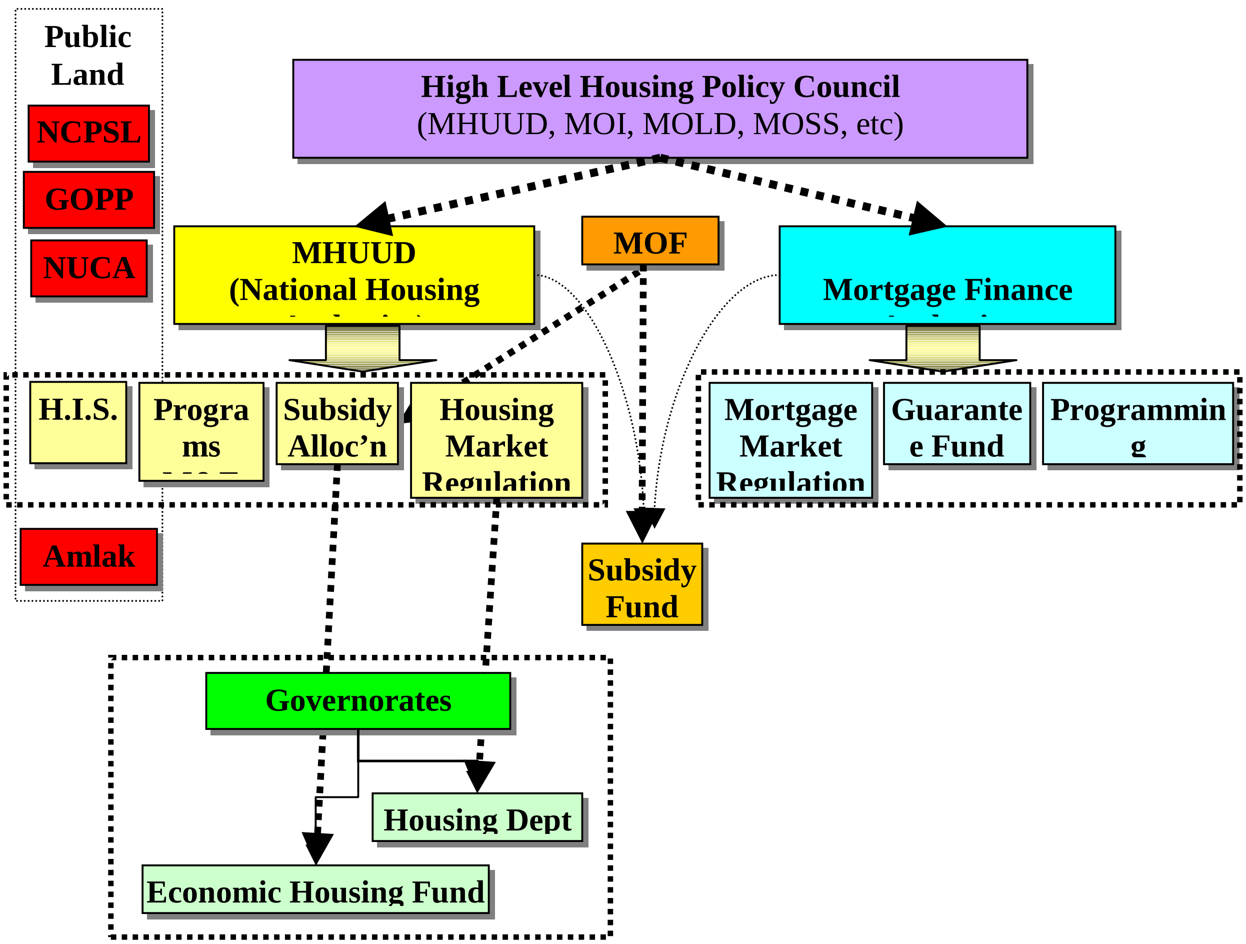
Strong **Weak**

There are a number of government agencies which carry out overlapping functions relating to housing supply. Programming, land acquisition and development, housing production, financing, beneficiary targeting and unit allocation are duplicated by at least five separate agencies. In addition, the 26 Governorates carry out parallel functions, largely through their economic housing funds. With the exception of the HDB, other banks, and the mortgage finance companies, there is little specialization. And all of these agencies, with the exception of the new GSF, are limited to supporting the supply of new housing and do not operate on the demand side of the housing equation. At the same time, the array of institutions related to housing have minimal mandate or focus on forming effective partnerships, regulating, or intervening in the private and informal housing markets. There is also a dearth of information and statistics needed to analyze and understand how these housing markets work. Government roles *vis a vis* private sector housing has been limited to some land allocations, enforcement of planning and building standards, and tax collection.

It is recommended that the GOE begin rationalizing the institutional framework under the NHP and introducing missing functions. In the long run, the management of Egypt's overall housing policy needs a high level apex body/authority which can function as the housing sector coordinator, but in the short-term an inter-ministerial working group, backed by a monitoring and research unit located in the MHUUD, could be formed.

In the long-term, there is a need for a high level policy council to serve as the decision maker for housing policy and programming, supported by a technical secretariat. The High Level Housing Policy Council would be responsible for policymaking related to the housing sector, including endorsement of strategies, plans, programs as well as the launch of new initiatives, and mainstreaming successful pilots at the national level. The GOE may also consider introducing in the medium/long-term a "National Housing Authority", which would combine the functions of the current housing sector of MHUUD, the Housing Information System (which the GOE has put as a key priority to the sector development). Such National Housing Authority would serve as the "brain" for the proposed Council and would be charged with preparing policy proposals, strategies and plans, establishing monitoring and evaluation systems, maintaining land and housing market data/information, studying markets, etc. With such information and analytical work in place, the Council would advise on the formulation of legislation and decrees.

Figure 13: Proposed Institutional Framework for Housing Sector



Whereas the Mortgage Finance Authority is already functioning and its structure and operations are relatively clear, the proposed National Housing Authority would entail a number of innovative functions, such as:

1. **A housing information collection function,** responsible for surveying and/or compiling data on the housing market including (1) new law rental production and rent levels, (2) progressive retirement of the old law rentals, (3) housing production and sales (both affordable and market rate units), (4) size and price levels in the second-hand housing market, and (5) quantity and terms of mortgages.

2. **A housing subsidies management function**, aiming at developing subsidy packages which are limited, are cost-effective, and which go to those most in need. An important part of this function would be developing and promoting effective targeting and screening mechanisms for potential subsidized housing beneficiaries (with links to NGOs, MOSS, and others partners.)

3. **A housing layout and standards function**, aiming at introducing less costly (and more affordable) residential land and building standards, including legislation for special "affordable housing zones" aimed at the small housing developer and owner-builder. Coupled with this would be a land market investigation function, aiming at identifying suitable urban expansion

land for affordable housing. This function would be undertaken in coordination with governorates, GOPP and public land management authorities.

4. **A housing monitoring, evaluation, feedback, and research function**, aiming at constantly improving the knowledge of housing markets and learning from experiences. This would include investigations of construction systems to explore cost-reduction innovations. It may prove cost-effective that some aspects of this function be out-sourced to specialized firms and consultants.

5. **An institution strengthening function**, assisting governorates to play important roles in affordable housing development within their jurisdiction. This would aim at governorate housing departments and the governorate economic housing funds.

6. **A publicity and outreach function**, aimed at informing the public of housing schemes which might benefit them and raising awareness of innovations in both rental and ownership housing markets.

Which agencies or institutions might be best suited to carry out these functions? The housing markets monitoring and research function (no. 4) and the land market and housing standards function (no. 5) both call for a small but dynamic research body with the means to outsource targeted investigations. Such a body would be the applied research arm supporting the proposed High Level Housing Policy Council. It might logically be located within MHUUD. A considerable amount of focused technical assistance and capacity building would be required to establish a pioneering unit that would monitor and investigate the dynamics of urban housing and land markets in Egypt.

Box 4: The U.S. Housing Information System

National housing information systems are typically composed of data collected through a national housing survey and data collected from multiple private sources. In the United States, for example, the Department of Housing and Urban Development (HUD) serves as the main compiler of housing statistics, issuing a quarterly compendium of housing data and an annual report.

HUD's Office of Policy Development and Research (PD&R) is responsible for maintaining current information on housing needs, market conditions, and existing programs, as well as conducting research on priority housing and community development issues. PD&R also maintains extensive data on the characteristics of subsidized housing units and tenants, which is collected from local HUD offices. The role of PD&R is to provide reliable and objective data and analysis to help inform policy decisions.

The main information sources for HUD's quarterly and annual publications come from six public and private sources.

Housing Stock:

- American Housing Survey (AHS). The National Census Bureau conducts the survey for HUD. The AHS collects data on the Nation's housing, including apartments, single-family homes, mobile homes, vacant housing units, household characteristics, income, housing and neighborhood quality, housing costs, equipment and fuels, size of housing unit, and recent movers. National data are collected biannually, and data for each of 47 selected Metropolitan Areas are collected about every six years. The national sample covers an average 55,000 housing units. Each metropolitan area sample covers 4,100 or more housing units. The AHS returns to the same housing units year after year to gather data; therefore, this survey is ideal for analyzing the flow of households through housing.

Housing Production:

- National Association of Home Builders (NAHB). NAHB is a trade association for companies involved in the construction or renovation of housing. The association surveys its members and collects city and county level building permit data to prepare reports on new housing starts, new housing characteristics, and new housing prices. Additionally, NAHB conducts a month survey of home builders to produce an index of their confidence in the business outlook.

Used Housing Market:

- National Association of Realtors (NAR). The NAR is an association of real estate brokers and agents. NAR conducts monthly national surveys of its members to collect current data on existing home sales, as well as profiles of home buyers and sellers. The NAR is the main source for housing price data.

Rental Market:

- Survey of Market Absorption (SOMA). Each month, the National Census Bureau (on behalf of HUD) selects a sample of residential buildings containing five or more units for the SOMA. The initial 3-month interview collects information on amenities, rent or sales price levels, number of units, type of building, and the number of units taken off the market (absorbed). Field representatives conduct subsequent interviews, if necessary, at 6, 9, and 12 months after completion.

Housing Finance:

- Mortgage Bankers Association (MBA). MBA is the national association representing the real estate finance industry. The association surveys members and provides weekly data regarding average mortgage commitment rates by mortgage product and volume measures of mortgage applications.

- Federal Housing Finance Board (FHFB). The FHFB regulates the 12 Federal Home Loan Banks that were created in 1932 to improve the supply of funds to local lenders that, in turn, finance loans for home mortgages. The Board is an independent regulatory agency of the executive branch of the U.S. Government. Each month, the FHFB conducts a survey of rates and terms on conventional mortgage loans.

IV. IMPROVEMENTS TO THE NHP

Now is the opportunity to leverage the NHP subsidies and the political momentum created by the program to initiate the reforms needed to build a well functioning housing system.

1.0 NHP's Evolving Profile

During the Presidential elections in 2005, President Mubarak pledged that the GOE will deliver/facilitate the delivery of 500,000 new affordable housing units in the six year period from 2005 to 2011, or about 85,000 units per year, 50% of which would be located in new towns and 50% in governorates. Under the current program guideline, each eligible household will receive an upfront subsidy of LE 15,000. The Ministry of Finance is thus allocating over LE 1 billion per year for this purpose. However, all off- and on-budget subsidies related to the typical unit are together estimated to cost LE 52,000 (70-75% of total development cost inclusive of infrastructure and the opportunity cost of land). This raises the price tag of this program to about LE 26 billion, which means, at existing subsidy levels, yearly subsidies of LE 4.4 billion (around 0.7% of GDP) to deliver 85,000 units per annum.[40]

The NHP Agency, placed under the MHUUD, is an interim program agency assigned the primary responsibility for implementation of the NHP through 2011. The Agency offers public or private developers upfront lump-sum subsidies of up to LE 15,000 per eligible limited income household to reduce the cost of newly built housing units, in addition to making land and off-site infrastructure available in new towns at no cost through the NUCA. When the program was launched, the basic housing unit envisaged under the program was a 63 square meter unit in multistory walk-ups, a construction cost of LE 50,000, and an up-front subsidy of LE 15,000 which is directly paid to the developers upon unit completion. The beneficiary pays a down payment of LE 5,000, and needs to finance the outstanding LE 30,000 through a 20-year mortgage credit corresponding to monthly installment payments starting as low as LE 160, and set to rise by 7.5% per year.

The NHP represents a significant departure from previous supply-side housing construction programs. It is similar in that it is a government managed and financed program which builds and delivers new housing units to beneficiaries under an "application regime." However, its design features stimulate the incorporation of the private sector into its implementation. It is also more transparent and offers more choice to beneficiaries. For example, it improves upon past programs through the following measures: (i) an upfront cash subsidy from the State budget rather than distortionary interest rate subsidies on soft loans for housing; (ii) a requirement for complementary mortgage or consumer loans which are now offered under new laws and institutions set up since 2001; (iii) beneficiaries seeking housing units will be able to choose among different down payment amounts and repayment schedules, including the option of an annual monthly installment escalator clause; (iv) there is an explicit intent to include the private sector in the finance and construction of units; (v) rental housing is included in the mix of units produced; and (vi) core housing and sites and services schemes are included as well.

Particularly, the NHP is attracting private sector developers to finance and build subsidized units, and this represents a great improvement over past systems, in which the private sector was virtually excluded, except for isolated instances. The NHP provides land and off-site infrastructure at a reduced cost in the new towns, and developers are to construct units according to the standards of the NHP (units must be of 63 square meters or less) in one of two options: either 50% or 100% of the built area of the project must be devoted to subsidized units. If developers choose to build on 100% of the land, the basic land price

[40] World Bank estimate as of February 2008.

charged is LE70 per square meters. If developers opt for a mixed income development, the 50% of the land on which to build affordable core housing is allocated at LE 70 per square meter, whereas the remaining 50% of the land earmarked for market housing is allocated at LE 333 per square meter. If developers request large land areas (200 Feddans and above), the land price is discounted in steps (LE 35 per square meter, declining further with larger land areas). Private developers were invited to express interest in either 100% affordable housing developments or in mixed income developments (50% affordable and 50% market rate housing) under NHP. As of May 2008, a total of 105 companies have registered for the program and 288,500 housing units have been programmed under this private sector channel. By May 2008 a total of 13,324 units were under construction. Upon completion of the NHP units within a maximum permitted period of three years, the developer will market these units to families which meet the NHP criteria. The up-front subsidy of LE 10,000 per unit for private developers and of LE 15,000 per unit for public developers is contributed to reduce the purchase price for the qualifying household.

In addition, upfront subsidies are lower than for previous subsidy schemes -- roughly 30% subsidy as compared to the Mubarak Youth Housing which required 67% of subsidies. However, additional subsidies need to be taken into consideration, such as the opportunity cost of infrastructure and land subsidies, likely cost overruns on construction expenditures which have to be compensated for by the state, and hidden subsidies by government lenders on interest rates (a below-market interest rate of 10.5% applied to the LE 2 billion committed by the three public banks relative to market rates today of 14% or more). In present value terms the interest rate subsidy alone would require an additional cash subsidy of LE 5,850 on a mortgage of LE 30,000, which would raise the upfront subsidy to LE 20,850 on a LE 50,000 unit or 41.7% of the nominal cost.

However, the program did not find many takers in the first year. Multiple advertisement in the newspapers of the basic model only resulted in 110,000 applications by interested beneficiaries. The low level of response prompted MHUUD to examine other options.

Several other products have been proposed including expandable core houses, sites-and-services and most recently rental units.

- **The most significant new product introduced under NHP is a public rental program, which currently is estimated to amount to a total of 211,500 units, or 26% of the expanded NHP target.** The product was introduced at the request of Governorates, which identified a great need for small rental units at affordable terms without any down payment. The basic unit is a 40 square meter unit comprising of one bedroom, a living room, a bathroom and a kitchen, and is intended at the poorest segments of society. Developments are built and owned by Governorates. The construction cost is estimated at LE 30,000 per unit. The financing available for this purpose includes: (a) a LE 15,000 subsidy extended to Governorates per eligible unit; and (b) a LE 10,000 soft loan at 6% extended to Governorates per unit[41]. Governorates are left with a LE 5,000 gap to finance from their Economic Housing Funds. The rent level is calculated at around LE 160 per month with the aim to repay the LE 10,000 loan in 15 years. For poor households unable to pay that rent, the Ministry of Social Solidarity will examine these cases to set the affordable rent level, with the balance to be covered under the Ministry's social safety net programs. Protocols were signed with 14 Governorates for the delivery of 25,500 units, and the MHUUD views that as much as 100,000 units can be delivered through this program (75% in Governorates and 25% as worker housing in new towns). In light of the popularity of the rental model, it was also decided to provide 63 square meter units under similar arrangements. Three protocols were signed for a total of 8,500 units, with the plan set at

[41] The funding comes from a soft loan of the National Investment Bank to the GAHBC at 5% with terms of 30 to 40 years, and which the MHUUD channeled to the Housing and Development Bank to administer.

20,000 units. Against the history of Egyptian public housing programs, this move can be seen as a major programmatic shift away from finished housing ownership and back to a structure that is likely to better match low-income household demand. This point is underlined by the fact that rental was reintroduced primarily at the request of Governorates, which identified a great need for small rental units at affordable terms and without the down payment requirement. Still, there may be problems, such as the nature of the rental contract – will it be time-bound and could tenants be evicted? Additionally, unless governorate rental housing projects include a range of unit sizes and types, there is a danger of creating residential ghettos of very poor households, which occurred in the 1970s and 1980s in governorate emergency housing (*masakin eiwaa'*) projects.

- **A core housing option, entitled *Beit Al-Ailaa* (family house), was announced in May 2006**. Land and an expandable core house are made available to beneficiaries by NUCA. Plots are between 100-120 square meters. The core unit comprises of one bedroom, living room, kitchen and bath, built on 40 square meters. Depending on plot size, beneficiaries can themselves construct one or two additional rooms using their own financing, up to a maximum plot coverage of 50%. An additional floor can be built in the future. Construction must follow standard plans provided by MHUUD for free. Payments of LE 80 per month would be charged to households for the 40 square meter model.

- **The sites-and-services model, called *Ibni Beitak* (build your own house), was announced in November 2006.** MHUUD advertised the delivery of 20,000 small land parcels (of 150 square meters each) in 18 new towns. Households are allowed to build on 50% of the land a maximum of ground plus two floors (MHUUD provides building plans/designs to interested beneficiaries). The ground floor needs to be built in year one. The serviced land price asked of households is LE 70 per square meter (compared to an average of LE 140-150 as indicated by MHUUD for infrastructure cost recovery). The land price is payable over 10 years, with a 10% down payment, a 3- year grace period, and the balance in installments over 7 years without interest. This implies a net present value of LE 49 per square meter. The LE 15,000 upfront subsidy is disbursed in three stages, tied to construction progress. As many as 110,000 applications were received, a much stronger than expected demand for this product. The President instructed MHUUD to increase the supply of this type of product; and there are currently 90,800 lots in the pipeline. As of May 2008 a total of 1,437 lots had been planned and serviced.

As a result of the introduction of these new housing options, there is now enhanced "market" diversification/ segmentation within the NHP. The 35m2 rental units are targeted at the lowest income groups who do not have savings for down payment on a homeownership unit and are very income-constrained. The larger 63m2 rental units attract moderate income groups with a preference for a starter home with 5-10 year lease duration and/or who do not have sufficient funds for a down-payment. Moderate-income groups with preference for homeownership and with the ability to provide a down-payment have options in the NUCA and Governorate 63m2 ownership units. In addition, moderate-income households can seek a subsidy from the GSF coupled with a mortgage (that the GSF facilitates) to purchase a new or used unit, so long as the purchase price is less than LE 75,000 (as an alternative to the 63m2 size restriction that MHUUD relies on). Finally, middle-income segments with the ability to raise higher down-payments and secure larger loans would be catered to under *Ibni Beitak* if they desire building their own unit or could acquire existing units developed by the private sector. Those willing to build a second unit for a qualifying household could access a second NHP subsidy. Higher income households also have the ability to purchase private sector-developed units on the open market using mortgages not linked to a government subsidy program.

2.0 Main Issues with the NHP

There is a large gap between household income and housing supply cost, even under the cheaper housing options promoted by the National Housing Program (NHP). Table 8 shows the maximum affordability for the median household in each quintile based on a 20 year subsidized or market loan whose repayment equals 25% of the reported, the required down-payment, and the NHP subsidy if eligible. Households in Quintiles 1 through 4 are eligible for the LE 15, 000 subsidy and below-market interest rate (10.5%) loan. Households in Quintile 5, however, are not eligible for the upfront subsidy or the below-market interest rate loan; the loan amount is based on a market interest rate of 13%.

Table 8: Large Gap between Greater Cairo Affordability and NHP Housing Supply Cost

Quintiles	**Q1**	**Q2**	**Q3**	**Q4**	**Q5**
Median Monthly HH Income by Quintile in	**400**	**600**	**750**	**1,000**	**1,750**
Affordability (loan, down pmt & subsidy)	**30,016**	**35,024**	**38,780**	**45,041**	**46,679**
Economic Hsg (63+5 m2, 35% land cov,					
Total unit cost (excl. block offsite land/infra)	49,140	49,140	49,140	49,140	49,140
Purchase price gap	**(19,124)**	**(14,116)**	**(10,360)**	**(4,099)**	**(2,461)**
Low cost/Rent (40+3 m2, 35% land cov,					
Total unit cost (excl. block offsite land/infra)	31,200	31,200	31,200	31,200	31,200
Purchase price gap	**(1,184)**	3,824	7,580	13,841	15,479
***Beit Al-Ailaa* (120m2 lot, 40m2 core, 50%**					
Total unit cost (excl. block offsite	39,066	39,066	39,066	39,066	39,066
Purchase price gap (note upfront subsidy	**(14,050)**	**(9,042)**	**(5,285)**	975	2,613
***Ibni Beitak* (150m2 lot, SS, 63m2 unit, 50%**					
Total unit cost (excl. block offsite	49,167	49,167	49,167	49,167	49,167
Purchase price gap	**(19,151)**	**(14,143)**	**(10,387)**	**(4,127)**	**(2,489)**

* Income is based on the results of the TAPRII Housing Demand Survey in Greater Cairo.
** Based on NHP guidelines: For eligible households (Q1-Q4), LE15,000 subsidy, LE5,000 down payment and 10.5% interest rate loan for 20 years; Q5 households, no subsidy, 20% down-payment, market interest rate (13%).

Some NHP products require a beneficiary contribution that is beyond low-income households' means. Of specific concern is the escalating beneficiary contribution required to purchase the privately developed ownership units. Mortgage loan amounts are constrained by a stipulation in the Mortgage Law that restricts monthly repayment to 25% of household income. Plus, the original payment can only be LE160 under NHP. Although some mortgage providers have created loan structures that expand the mortgage amount such as reliance on annual bullet payments, the maximum loan amount ranges from LE 30,000 to LE 45,000. In an environment of increasing construction costs, private developers have raised the sales price of units. These two elements combined have forced beneficiaries to make down payments of between LE 29,000 to LE 40,000, significantly above the LE 5,000 envisioned in the NHP. The *Ibni Beitak* program has also proved to be an expensive endeavor for beneficiaries. While the down payment of LE 1,050 is quite low, completing has an estimated cost to the beneficiary of about LE 53,000.

Unless the affordability constraint is released, it is likely that there will be leakage of units to higher income households. In the case of *Ibni Beitak*, there is anecdotal evidence that this is already occurring by means of selling the serviced lots to higher income buyers even before starting construction of the unit. In regard to the privately constructed ownership units, it is likely that beneficiaries may have significant undocumented earnings that allow them to make the substantial down payments and enter into mortgage loans with large early-term principal repayments. As credit conditions are expected to tighten (likely rise of mortgage rates from the current 12%-14% range) along with steep inflationary trends in 2007 and 2008, especially in building materials, there is pressure on lenders to increase down-payment required from households, and on the NHP to provide additional subsidies. Unlike public developers, private developers capture subsidies without sale price limits, so their margins are less affected than those of public providers. The analysis of both the direct and indirect subsidy levels of the existing NHP program and the potential implications of building material price hikes reveals high fiscal costs (in terms of accrued subsidies per unit), particularly for the public sector delivered component financed by public lenders (even before taking into account any additional credit loss).

While the NHP includes housing models that depart from the classic 60-75 square meter unit in walk-up housing blocks, and this represents a welcome move towards a greater mix of affordable housing products, there is still concern about the location of the units. The core housing and sites and services schemes, and smaller units in classic housing blocks are to be located in the New Towns, and allocated areas within the New Towns will tend to be in the furthest, most remote sites where land is available. Both the core housing and sites and services schemes are attempting to attract the same kinds of household investors who currently are so prominent in informal urban areas. However, it will be difficult to attract this target groups to these remote areas far away from their source of employment, livelihoods, and social networks. In addition, NHP standards of low plot coverage and low exploitation ratios which mean low densities and high on-site infrastructure costs, as well as high off-site infrastructure costs typical to new towns, will mean that either affordability for these schemes will be problematic or indirect subsidies will be costly. The resulting neighborhoods will also be difficult to serve with convenient transport and other services. Addressing the issue of poor location of subsidized housing is imperative, and one way of rectifying the situation is to identify publicly owned and underutilized parcels of land in urban areas that could be used for low-income and mixed-income housing.

Most housing "demanders" have low incomes relative to housing payment, limited relationship with banks and perceive the new National Housing Program as expensive. The majority of TAPRII Survey respondents who are seeking housing are young men who plan to marry, and 61.2% of them prefer a long-term lease. Of the families who are looking for housing, 54% also prefer a long-term lease. The high demand for rental is reflected by the fact that 82.2% of households chose rental housing between 2001 and 2006 versus only 17.8% who bought their units.[42] Respondents who did not borrow from a bank cited the cost of a bank loan, the need for collateral and cultural barriers. Few households have dealings with any financial institution[43]. The TAPRII Survey also found that there was limited awareness or understanding of the NHP options. Yet, once NHP options were described, the overwhelming sense was that they are not affordable though widespread comments about loan terms, purchase price, and rents rated as "too high." Another issue, not specifically addressed in the TAPRII Survey, is that many low income households have informal incomes which bar them from entering the program.

In addition, the savings ability of lower-income households or their capacity to mobilize funds for the down-payment in other ways is limited, although less so than in many developed and developing countries. Raising funds necessary to pay either the whole cash price of a unit for sale, the down-

[42] Other survey findings include: (i) most (81%) households looking for housing have incomes less than LE 1,000 per month; (ii) young households (between 20 to 30 years of age) are more accepting of the concept of mobility than older households; (iii) demand for serviced land represents only 3.8% of total demand; (iv) both singles and families currently looking for housing overwhelmingly prefer Greater Cairo, 71% and 67% respectively; and (v) only 3.8% of the surveyed households who bought their housing unit between 2001 and 2006 bank-financed the purchase of their home.
[43] 78.9% of surveyed households have no dealings with banks, financial corporations, or mortgage companies.

payment portion of the sales price required by developers or under government schemes, or the advance payment which is commonly required to rent a unit, is a major other affordability constraint. The majority of units for sale on the private housing market require full cash payments. This has been the norm for decades. Some units in both the formal and informal private sectors are offered with installment plans, but these rarely amount to more than 30 to 40% of the total price and must be paid in 3 to 5 years. As such, Egyptian families have had to mobilize significant amounts of funds to acquire housing. Households do this through personal savings, borrowing from friends and family, revolving credit groups, and/or conversion of other assets. The TAPRII Housing Survey allows a look at the ability-to-pay for rental housing advance payments and equity down-payments for purchase. Housing demanders expressed their ability to mobilize surprisingly significant amounts. Indeed, the median overall response was LE 7,000, the median amount of LE 10,000 was considered “getting expensive,” and the median response for what is considered “too expensive” was LE 12,000.

The large gap between affordability and the NHP housing supply costs as currently envisioned can be addressed using a two-pronged approach of (i) removing regulatory impediments that increase the cost of housing supply (see Section 3), and (ii) expanding access to housing finance, with a focus on mortgage finance for middle-income households and micro-finance and other innovative approaches to address the needs of the lowest income deciles. For each income segment (quintile, family composition, age, etc.), Government should identify necessary real estate development regulatory reforms, provide incentives for mortgage and non-mortgage lenders to expand lending to addition income segments, and finally plug the gap between affordability and supply cost through subsidies when necessary.

3.0 Improving Affordability in the NHP

3.1 Making Housing Finance Accessible

Mortgage finance should be an integral part of the NHP because greater access to housing finance will augment the ability of middle income households to purchase housing and allow the GOE to focus on implementing housing programs for the low-income. Mortgage lending is critical to reach NHP housing targets because there is potential for the private mortgage market to serve a large portion of the middle and lower/middle income households with much less subsidy than traditional government housing programs. This allows the government to concentrate its limited resources on those who need them most.

A challenge for the NHP is the eligibility of the beneficiary households to contract and repay 20-year mortgage loans. So far, three public banks (National Bank of Egypt, Misr Bank, and Housing and Development Bank—HDB, and a public Mortgage Finance Company Taamir) have pledged together LE 2.3 billion for the program at a fixed below-market interest rate of 10.5% (market priced mortgage loans would be at 13-14%). This pricing raises sustainability concerns for a large scale program, notably for the HDB which has less core deposits, and could undermine the current broader efforts to restructure the banking sector and lead to adverse soft loans or other forms of unwelcome additional subsidies. The new liquidity facility, the EMRC, has helped the banks deal with the mismatch (margin between the fixed below-market rate and the market rate) and provides a better basis for using the lower interest rate.

In order to make the mortgage loan more affordable for NHP beneficiaries in the initial years, a GPM instrument is envisioned with a 7.5% annual increase of the monthly installment in order to minimize the initial monthly payment (LE160 in year one) and boost credit affordability. One concern is possible negative amortization in the first few years, depending on the level of the supply subsidy and down-payment together. This added risk is shunned by the banks. The credit risk would also be higher because the annual increase of 7.5% is considered high, and is based on a recent annual civil servants’ wage increase (about 10%) which is not necessarily the norm for households employed outside of the public sector and does not represent a long-term floor for future wage appreciations of civil servants.

The NHP income limits and payment to income ratios stipulated by the Mortgage Law, greatly constrain household purchasing power. Mortgage loans from the MFCs at market interest rates have repayments that are limited to 25% of household income, and therefore the maximum loan amount under an amortizing loan (as specified under the NHP) is around LE 30,000 assuming an interest rate of 13% per annum. Because of inflation pressures, interest rates are likely to increase to at least 14%, thus reducing the maximum loan amount. To expand the purchasing power of homebuyers, the MFCs have developed creative loan structures. Structures currently in the market include introductory teaser rates that increase during the term of the loan (such as 12% in year 1, 13.5% in years 2-6, and 14.5% in years 7-20, in the case of the largest MFC Tamweal) and obligatory bullet payments (early-term principal repayments). In the case of one MFC, these bullet payments consist of annual payments equivalent to 10 monthly payments for the first 10 years, over and above the monthly payments on the amortizing loan that has a 7.5% escalation per annum. Using this structure, the MFC is able to increase the mortgage loan by about 50% to about LE 45,000. Yet, all what the use of such creative and risky instruments can do is offset the recent increase in unit prices due to construction cost increases, leaving the households to come up with very large down-payments, averaging around LE40,000 in private sector-built units. If the initial NHP target for the level of credit repayment is not adjusted to market realities, lenders would have to introduce riskier amortization schedules (negative amortization in the early years, very long terms, or large yearly bullet payments) that increase credit risk. Both increased riskiness of mortgage lending and implicit funding subsidies to banks would be undesirable consequences that could set back efforts to normalize the mortgage market.

To induce lenders to participate in down-market lending including for the NHP, the GOE may consider providing other types of incentives. For example, NHP funds could be used to support risk sharing or to cover additional transaction costs arising from underwriting and servicing small loans. Part of the upfront subsidy offered under the program could be used for interest buy-down for a limited period to reduce monthly payments. In brief, a mortgage buy down is an initial lump-sum payment that enables the lender to lower the interest rate for a given duration on a fixed rate mortgage. A home purchaser buys down a mortgage by providing a higher initial payment to the lender in order to decrease the interest rate for a specific period of time. This would assist income constrained households who can accumulate down-payments from savings and family sources, but who cannot make the monthly payments warranted in a high interest rate environment. A mortgage buy-down is transparent means of augmenting affordability in a high interest rate context. Additionally, should the qualifying buyer be able, the NHP should allow the option of increasing the equity down payment to further reduce the required monthly installments.

There is a need to harmonize the GSF with the NHP. The main difference between the GSF approach and the NHP is that the former is not a government housing supply program, but is available for any household that needs financial assistance to acquire a housing unit on the market (thereby relying on private developers and private lenders). The unit can be newly constructed or a resale unit available on the market, on condition that it is registered (or “capable of being registered”) at the Ministry of Justice’s Real Estate Publicity Department. Although the GSF has a somewhat different client base, confusions and distortions could arise from having both NHP and GSF operate under the new and rapidly evolving mortgage finance structure unless subsidy amounts, terms and conditions are harmonized. Besides the cash subsidy differential, mortgage finance companies and banks operating under Law 148/2001 and wishing to participate are funding themselves through deposits and on-lending them as mortgages at between 13% and 14% annual interest. By contrast, under NHP, mortgage loans are extended by public banks that have access to soft loans from the National Investment Bank, and can therefore on-lend at a rate of 10.5%.

Recognizing the magnitude of the problems arising from tougher market conditions, and the poor targeting of the NHP subsidies for finished housing through developers, the GOE should develop a new scheme of upfront household subsidies that would be part of a comprehensive package to finance the unit including mortgage credit and a household down-payment. It is recommended that the program of credit-related subsidies be implemented and operated by the GSF, on behalf of the MHUUD and MOI, as the GSF has already established experience and credibility in administering a similar program with various mortgage lenders, albeit at a lesser scale. The establishment of the main features of the program - including targeting criteria but also a regulatory and budgetary framework – as well as any later related adjustment - would not be decided by the GSF but by higher-level policy making authorities within the context of the broader housing policy.

The advantages of such a program are that: (i) the subsidy benefits the consumer directly, rather than indirectly through a subsidy to developers, which generally improves the efficiency and transparency of household subsidies; (ii) it allows a broader range of options of houses to be included in the overall package of subsidies (e.g., unfinished houses and existing houses); (iii) it increases the ability of middle and lower middle income group to access credit and hence lowers the amount of needed subsidy, all else being equal; and (vi) it allows expanding mortgage markets to play a pivotal role in increasing the production of housing, which would gradually contribute to the improvement of mortgage finance terms associated with the reduction of risk and going to scale.

Mortgage linked transparent upfront subsidies and/or buy-down subsidies allow lenders to make loans at market conditions and allow for better targeting through lenders' underwriting systems and through implementing a subsidy system progressive with loan size and house value/size. However, mortgage linked subsidies are only feasible for households who are creditworthy and for properties trusted as collateral by lenders. In the Egyptian housing market this means that a large proportion of households deserving of a subsidy cannot be served through such a program, even if over time the program is adjusted gradually to reach lower income groups. A mortgage-linked subsidy is therefore always only one part of an entire subsidy package. It needs to be complemented by alternative subsidy programs that cater to those households excluded from mortgage lending. For example, site and services projects that combine a serviced land subsidy, self-help and access to micro-loans, subsidized rental housing, as well as such instruments as guarantees and contractual savings for access to mortgage finance by qualifying households with undocumented/irregular income.

Shifting from a supply-side dominated subsidy system to a demand driven mortgage-linked subsidies would need to occur in a gradual fashion. Private developers who are accustomed to receiving heavily subsidized land upfront would need to adjust to a system in which all the subsidy comes in upon the sale of each individual housing unit. The current pipeline of NHP allocations will facilitate this transition. Moreover, the transition period will allow MHUUD and the GSF sufficient time to fortify their monitoring and evaluation capabilities.

The introduction of the new subsidy program would have consequences for the governance structure of the GSF. The first requirement is the separation of the subsidy and guarantee functions, which should be reflected by a legislative amendment to the Decree establishing the GSF. The separation should be complete, including products, corporate governance, operations, and financial management (beyond the current administrative and accounting separations). Managing a guarantee program requires an independent decision process based on prudent risk management principals prior to the consideration of subsidies, even if the guaranty is used to promote a social agenda and if insurance premiums are reduced for that purpose. The second requirement is the reconfiguration of the (to be renamed) Subsidy Fund's Board of Directors to reflect the role of the MHUUD in policy development, which could be achieved by decree.

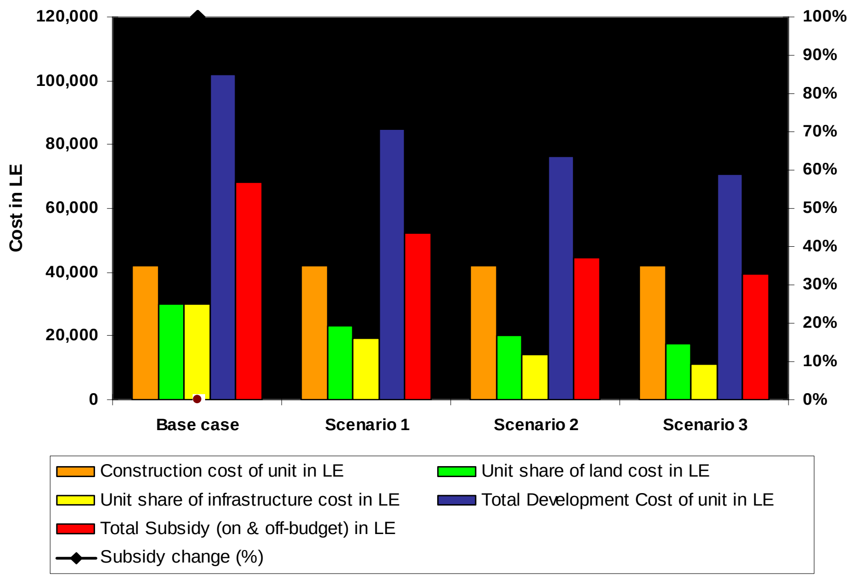
The NHP should require all housing units to be registered by the beneficiary at the REPD. This has not been always the case, as this process requires first the housing project block to be entered into the title or deed register, then to be divided into individual titles. For the new towns only, a protocol was signed in September 2006 between NUCA and the MFA in order to facilitate the registration process and create a legal framework acceptable by mortgage lenders. It is too early to assess the effect of this protocol; it is nonetheless expected to have an important impact, even though the process of subsequent registration is likely to be fraught with many complications as it falls back into the jurisdiction of MOJ and ESA, which have no role in the block and first registration. In NHP projects executed by private companies, the title transfer to the developer can occur in a sequential manner, provided the land cost has been paid in full.

MFH loans could be of meaningful assistance for home improvement, finishing dwellings that have not been completed, or expanding of existing dwellings; it is inadequate to finance a new dwelling. MFH loans could also be the "first" loan in a cycle of loans used to build modest dwellings incrementally, as in the core housing program of the NHP. Also, MHF loans could be used to finish off and rent/sell units on the market, thus establishing the traditional link in microcredit between the loan and income generation. Promoting MFH in Egypt could have two important roles. First, MFH could serve as long-term provisions of finance to assist poor households improve their dwellings, including unfinished units. Second, it could serve as a possible addition to NHP subsidy programs, to assist households that cannot quality for, or who are not a part of NHP. For example, for households in the first quintile, no current NHP program may be affordable, including the low cost rental. Households in the second and third quintiles can afford the rental program, but none of the others, even with the subsidy, including the *Beit Al-Ailaa* program. Only households in the fourth quintile can afford the *Beit Al-Ailaa* program. In addition, the affordability assumptions are quite generous: they are based on a 20 year loan with a payment to income ratio of 25%, at a concessionary interest rate of 10.5%. In contrast, the households who are the prime candidates for obtaining MFH loans generally cannot qualify for formal mortgage loans, either because of low income or because of variable income from informal sources.

3.2 Reducing the Supply Cost of the NHP Housing

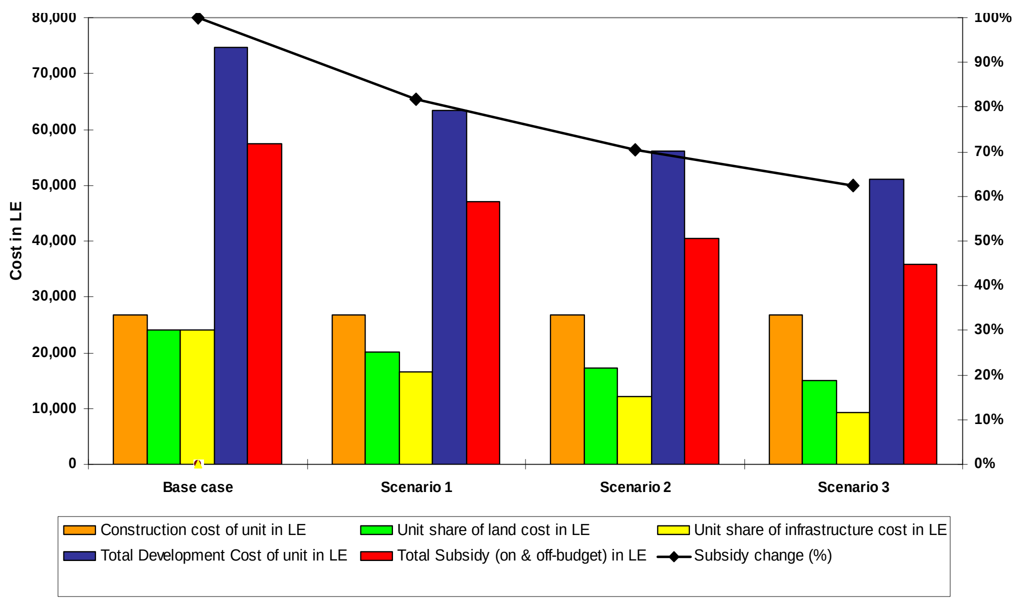
To reduce the cost of affordable housing programs in Egypt, the GOE must consider relaxed land development and building standards for NHP housing. For example, more efficient land coverage (increased from 50% in the base case to 60% in Scenario 1, 70% in Scenario 2 and 80% in Scenario 3) in the *Ibni Beitak* program decreases subsidy burden cumulatively by 42% (see Figure 14). Reducing land coverage and increasing the FAR also yields large reductions in the subsidy amount for the *Beit Al-Ailaa* program as well (see Figure 15). In short, higher density development allows for more units to be built on less land. This lowers the amount of subsidy required by reducing the total development cost. Conversely, reducing the quantity of land needed to construct a set number of units would also facilitate the use of more expensive, but better located parcels of land for the same level of subsidy.

Figure 14: Effect of More Efficient Land Utilization on Public Subsidy Needed in the *Ibni Beitak* Program



Source: World Bank, April 2007

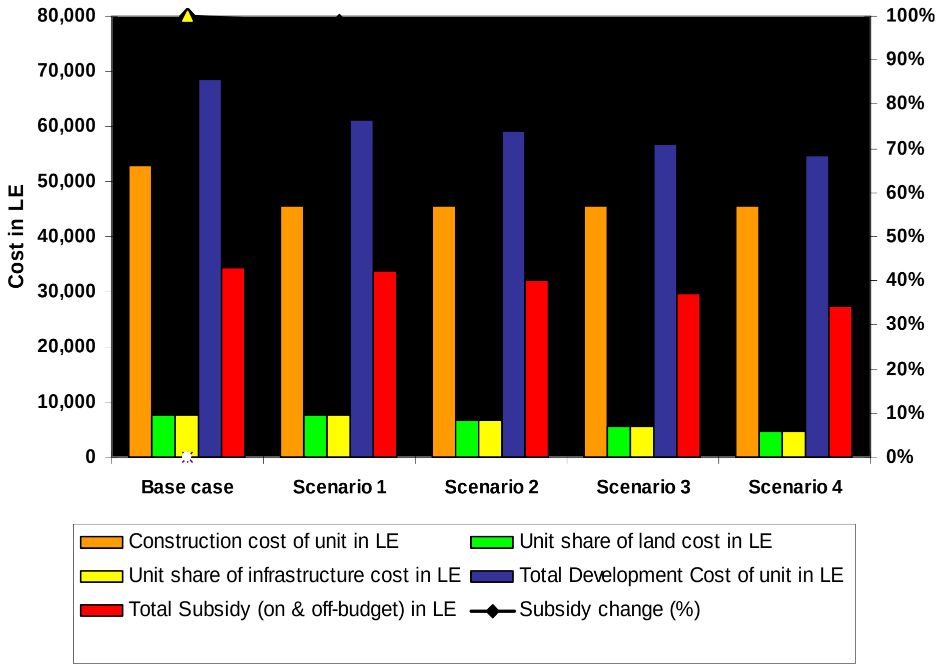
Figure 15: Effect of More Efficient Land Utilization on Public Subsidy Needed in the *Beit Al-Ailaa* Program



Source: World Bank, April 2007

Another means of reducing the overall cost of supplying affordable housing, as well as the public subsidy burden, is to promote the development of NHP housing by the private sector. Figure 15 demonstrates the potential gains of coupling efficient use of land with private development in NHP Economic Housing. The shift to private development reduces the total development cost by approximately 14% and reduces the public subsidy burden by 16 – 20%. In the base case, the housing is developed by the public sector and has a maximum floor-area-ratio (FAR) of 1.75 and lot coverage of 35%. Scenario 1 shows the savings to the total development cost realized through production by the private sector based on prevailing cost differentials. Scenarios 2 through 4 highlight additional saving under private development with increased lot coverage and allowable FAR (40% lot coverage and 2.0 FAR in Scenario 2, 48% lot coverage and 2.4 FAR in Scenario 3, and 60% lot coverage and 3.0 FAR in Scenario 4).

Figure 16: Effect of Private Development & Efficient Land Utilization on Subsidy Amount in NHP Economic Housing

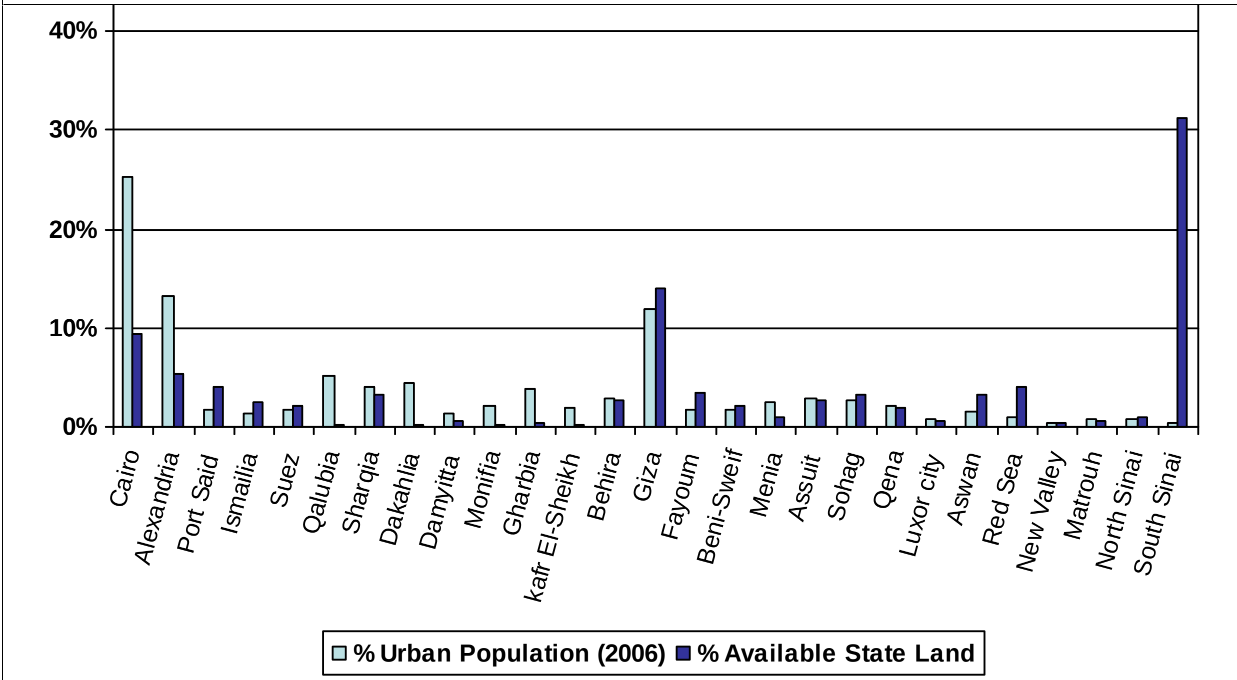


Source: World Bank, April 2007

*The reliance on State lands (mostly desert and remotely located) remains a challenge for the NHP***.** Past public programs led to poor matching of geographic supply with demand on the macro level and serious location problems at the micro or metropolitan level. Although the NHP claims to have sufficient land available for its five year production targets, such massive amounts of land can only be found in the most remote expansion areas of new towns and in governorate desert sites, which, to be unencumbered and free of previous land assignments to sectoral agencies, can only be located far from existing towns. A total of 3,167 feddans of land are available for the NHP in the new towns and 7,171 feddans in the governorates. This means that respectively 105,763 units and 320,376 units can be accommodated on these lands. This produces a national total is 426,139 units, which means that, on paper at least, there is just enough land to meet the NHP target of 500,000 units in six years.) As shown in the Figure 16, there appears to be a mismatch between the governorates where urban land is available and existing population centers (a proxy to demand). Of the major population centers, only Giza seems to have balanced available land and projected housing needs, and it thus redresses some of the imbalance in Cairo.[44] In the Delta governorates, very little if any State land is available, and in Alexandria the lack of land relative to need is pronounced. By contrast, a large portion (32%) of all public land available for NHP is found in the South Sinai governorate where barely 0.3% of Egypt's urban population lives.

[44] Whereas New Cairo, one of the most promising New Towns, is excluded from the NHP for unclear reasons.

Figure 17: Governorates' Share of Urban Population in 2006 vs. of State Land Available for the NHP



* Public land made available for the NHP in new towns was added to the Governorates in which they are spatially located (even if the new towns are administratively independent).

Given that land availability has bedeviled past programs, it must be questioned whether all these lands can be made available clear of encumbrances, and can be provided with trunk, off-site, and on-site infrastructure within the various planned budget lines and timeframes. Hence the recent announcement of using Awqaf land in the NHP may provide a promising element of answer to this location challenge.

Under NHP land and infrastructure continues to be offered to executing agencies as well as private sector companies at a reduced price that is below infrastructure cost recovery levels. The costs and therefore the effective additional subsidies carried by the State for housing infrastructure under NHP may increase in real terms over time. As both governorates and NUCA scramble to identify and rapidly service vast new areas in remote desert sites to meet the NHP targets, off-site infrastructure costs will increase as well as the need to construct or expand system elements such as treatment plants and booster stations, implying tremendous amounts of additional fiscal resources. In addition, all new housing areas under NHP need the package of public facilities such as schools, youth centers, public parks, clinics, and fire and police stations, which are especially needed since the NHP program consists of large scale developments with almost no reliance on infill housing (which can rely on existing services). The costs of these many facilities are unknown but substantial, and will require large investments by NUCA in the new towns and line ministries in the governorates.

There may be opportunities for housing authorities and private sector companies participating in the NHP to develop housing projects with an eye to recouping some of the subsidies inherent in housing units by profiting from other aspects of the project (forms of internal cross-subsidy). For example, units on the ground floors could be sold at market prices and authorized for use as commercial spaces, since in reality these units in housing development have proven to be desirable for commercial uses, often traded for over five times their costs because of their potential for conversion. Some units could be larger and sold at market prices, which would achieve two important objectives of income-mixing and cross-subsidization. Finally, through clever land use planning, large profits can be made by the sale of well-located parcels (e.g. well located and corner lots, some larger parcels) on the open market. Such arrangements which can significantly reduce overall housing subsidies have not been attempted at any scale in past and current government housing programs, and to date the NHP has not articulated such a strategy despite its great potential to reduce the overall subsidy envelope.

4.0 Targeting in the NHP

Section 4 of Part III provides a more detailed description of the challenges to targeting subsidies in Egypt and provides recommendations for improving the overall system. This section focuses specifically on targeting with the NHP and recommended pilot projects.

Targeting and affordability are key elements of the NHP that need to be revisited. The NHP relies on the usual application regime, with basic information such as age, address, occupation, and a self-reported statement of monthly income. Qualification criteria are that the household cannot own another unit, must be at least 20 years old, and proven family income cannot exceed LE 1,500 per month.[45] Basically, the NHP is open to any adult who does not already have full control over his existing unit, has not or is not seeking other subsidized housing, and whose income is not above a certain limit that hardly excludes anyone but the very rich. The income limit is also based on proven salaries, which implies that all undocumented income from second jobs and informal/self-employment is not taken into account. The pool of potentially eligible participants is vast, and could encompass any applicant under the 80th percentile of the urban income distribution. According to the TAPRII Survey, the first year payment would be affordable to most families in Greater Cairo, except the three lowest deciles.[46] Yet there is a need to introduce varied options to improve affordability such as rental housing (in light of the high demand for long-term leases) and a higher down-payment in return for lower monthly repayments.[47] Even in rental housing, a prevalent practice from the rent control regime, but which has persisted afterwards, is the use of a large down-payment (key money) to access a long-term lease for a housing unit at a much reduced monthly rental rate, which further reinforces the likely success of a higher upfront payment option.

Recent major changes in the NHP programs, however, will greatly increase reliance on rental programs. This will certainly facilitate self-targeting, as poor and modest income households seek this option. This is an important step forward, especially as the TAPRII Survey demonstrated many of those now looking for housing prefer to rent. Rental tenure is mostly self-targeting – given the high preference of Egyptians for homeownership and the zero down-payment need, demand can be expected to be concentrated among younger, elderly, and poorer households. This complements the typical self-targeting mechanism of NHP and earlier program via size restrictions of the units produced. Rental programs also allow more flexibility for income changes. If the financial situation of a tenant changes, the public subsidy donor can usually either terminate the contract or increase the rent in order to reduce the mistargeting. This is usually not possible under ownership programs. Under a rental contract, as opposed to a subsidized ownership unit, the recipient has little incentive to keep the unit vacant. Even if this results in a subletting practice that is

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[45] Through self-declaration since the time and cost of an administrative, manual cross-check of past unit distribution is high.

[46] The poorest 30% of households would represent over a million families in Greater Cairo and over 2.5 million families in urban Egypt.

[47] Notably as past studies show that housing acquisition in Egypt is in large part financed through sale of jewelry and agricultural land and property assets, savings including remittances and inheritances, gifts and zero-interest loans from family or friends, etc.

illegal under program guidelines, an occupied unit secures a welfare gain for the Egyptian society. Finally, rental stock can usually also be produced in larger and more standardized schemes, as individual preferences for design, size and other features will be less pronounced than under ownership programs.

Although the introduction of low income rental programs under NHP will greatly increase self-targeting, targeting within the homeownership programs needs much refinement. Because of the possible link between leakage from past government programs – in this case subsidizing those who already own, or have control over, a housing unit – it is recommended that the homeowner programs take priority in putting improved targeting in place. Information from the TAPRII Survey indicates that many "demanders" – those currently looking for housing – are young single men, with low income or no current source of income, coming from households with moderate or higher income and having adequate space. Subsidizing these types of demanders essentially puts the family in control of more units than just the nuclear family's residence. In contrast, the survey suggests that numerous other "demanders " are nuclear families living with extended families in crowed and poor conditions. Better targeting could serve those in most need to alleviate inadequate housing conditions, and avoid the problem of households owning multiple units, including subsidized housing.

NHP provides an opportunity to pilot the approaches discussed in Section 4 of Part III to reduce abuse and leakage. It is recommended that a revised system should first be pilot-tested under NHP. The group of most concern would be those applying for subsidies for the homeownership programs under NHP. It is recommended that a compromise position be adopted: (i) test a pilot process involving a much expanded application form, and screening and verification process on a sample of households (say 5-10% through actual residence visits); (ii) monitor/inspect subsidized units for a sample of applicants to examine vacancies and leakage (say 10-20%); and (iii) manage this process in a new/expanded monitoring unit recommended to be established in MHUUD. Thus, for a trial period, MHUUD would use a much longer application form. This form will "test" applicants from several angles, and maybe unearth inconsistent answers and reasonable proxy variables for income and current housing status. The pilot test process would entail the following two components:

- **Pilot Test and Analysis of Expanded Application Form**
  - require greatly expanded information during the application process (see below);
  - do not attempt to verify all information for all applicants but rather develop a sampling plan for verifying selected information for selected households;
  - computerize the sample data and conduct analyses of the verified data and application data, including correlations among the various types of data;
  - utilize the TAPRII Survey data on income, expenditures, and assets to try to determine correlations and under-reporting, disaggregated by type and location of household;
  - attempt to determine the best proxies for income and housing condition;
  - revise (and shorten) the application form as a result of the analysis, including only variables that seems to best identify key target groups.

For example, application forms should state: (i) MOSS status and food ration status; (ii) a complete description of current household and housing status (housing size, location, housing expenses, along with an affidavit that the head of household does not own another house; (iii) electricity Kwh per month for previous year; (iv) all income, social and household variables needed to for Proxy Means Testing; (v) income tax information (and lack of it would indicate something?); (vi) a request for real estate tax bills; and (vii) assets, including a car, and more expensive consumer durables.

This process would be carried out by an expanded Monitoring Unit within MHUUD. The application data should be computerized for a sample of households on a trial basis. One goal is to try to correlate stated income, other variables, and "actual" income; determination of actual income would probably require a household visit and conduct of an expenditure analysis, such as that in the TAPRII Survey. The income tax data would be used where possible. Trial runs for Proxy Means Testing could be conducted. Informal screening could result before computerized systems were established. The end result would be to redo the application form after finding out which data most usefully describes household eligibility. Finally, even if these tests do not turn out to be as precise as desired, perhaps the detail of the application might make "ineligible" households think twice about applying.

Monitoring Subsidized Units for Leakage and Vacancies. Another step in this process would be to conduct a survey of subsidized housing units to determine occupancy status and legitimacy of occupant. This too should be done on a pilot and sample basis, as a full survey would be expensive. This could be done in relationship with the vacant unit survey recommended earlier. Vacant subsidized units could be required to be occupied by their owners (on some terms to be defined, allowing for work abroad, etc.) or to be formally rented or sold. Vacant, subsidized units subsequently found to be unoccupied, or occupied by ineligible households, could remit to the state.

In sum, these recommendations are designed to serve three inter-related goals in the NHP: (i) delivering subsidies to the identified priority households based on clear parameters for eligibility and priority; (ii) discouraging leakage to third parties, especially ineligible households; (iii) and minimizing ineligible applicants from securing subsidized units, especially if these are multiple units, thereby exacerbating the vacancy problem.

5.0 Strengthening the NHP Rental Program

The rental program should allow for variation of unit sizes and rent levels, according to local demand and land price/construction cost profile. It is recommended that the strict program constraints of a 'cost rent' of LE 160 and square meter constraints be reconsidered in favor of a maximum cost/subsidy per square meter approach. In combination with the total cost constraints per unit limiting overall fiscal exposure this would leave Governorates greater freedom in construction design, e.g. to address areas where demand from larger families is greater, or where affordability is higher in absolute terms (not relative to area income levels). The rental tenure constraint itself reduces the need for imposing a maximum unit size, which in turn limits the future marketability of the units – should the government decide to sell. A certain flexibility in rent setting – e.g. between 140 and 250 LE – could also limit the gaps between public and local market rents in different locations (i.e. different land values), limiting the amount of rent seeking by higher income households in good locations and improving targeting.

Private sector collection and property management should be the standard. While Governorates and MOSS remain in control of origination and termination of contracts, it is recommended that collection to be outsourced to third parties (following the case of HDB in rent collection in the Alexandria Governorate), ideally via management contracts that include maintenance. Such a move could also provide further stimulus to a national collection industry that may also be able to service private rental and mortgage contracts.

Improvement of targeting, stock management. To improve targeting of the rental units, MOSS should be integrated into the monitoring of tenant's income. Helpful in that regard could be rental contracts with terms limited to 3-5 years that will automatically roll over if the eligibility criteria are still fulfilled. Tenants who gain increased financial stability while occupying the unit, however, should not be evicted because a tenant income mix may socially stabilize and enrich the developing neighborhoods. Rather, a system of moderate 'misallocation fees' for those whose incomes exceed the limits should be designed.

6.0 Diversifying the Delivery Channels of the NHP

Alternative objectives can be reached through the application of NHP subsidies. For example, the NHP subsidy pool could be used to help qualifying buyers purchase resale units or to help finish units to be completed and put on the market. Additionally, the NHP subsidy could be used as an eviction guarantee by an eligible household to rent a vacant unit.

- **Purchase of resale units**. There are two possible approaches. (1) *Contractual savings for qualifying applicants which, after a certain period, allow the applicant to qualify for a cash subsidy*. The applicant would find the unit, negotiate the price, and allow an inspection of the premises and the seller's documentation. Upon signature and exchange of standardized civil contracts, the contractual savings plus cash subsidy, plus perhaps a further down-payment, would be handed over and the unit possessed. This approach could be made more flexible if part of the subsidy could be used for the buyer of an unfinished unit to make it livable or some of the subsidy could be used for a contract with the seller to complete an unfinished unit. Incentives for owners of unfinished stock will need to be designed (e.g. exemption of fess if rented to a low income household) so that the owners would bring the units to the market by registering with MHUUD. (2) *Loans secured through traditional means topped up with the cash subsidy and a down-payment*. This scheme would operate much as described above. Traditional loans involve a range of possible guarantees (such as signed checks, personal guarantees, registered property guarantees, employer guarantees, etc.). However, there are two main issues: (a) loans for home purchases are by definition not productive, so repayment could be a serious obstacle (or at least will be perceived so by lending banks), and (2) a large portion of target households will not be able to secure loans through traditional means. Thus such a scheme might only find a niche market where the purchaser will turn around and rent the acquired unit to pay off the loan.

- **Completion of unfinished units, e.g. for rental.** As an example, assume that completion costs for an unfinished unit in Cairo lies in the range of 100-200 LE/m2, which would result in completion costs of 6,000 – 12,000 LE for a 60 square meter unit. This is a fifth of new construction costs in a New Town, while the existing unit is usually better located. Low income landlords with qualifying units could be provided with an NHP subsidy if they accept the unit to be rented out (see Box 5 below). If costs are such that a loan is also required for completion, a GSF-guarantee of a market-rate loan could be considered. For a mortgage loan, the land would need to be registered or become registered throughout the construction phase. Construction progress, and loan disbursement, would be monitored by a team of program officers/engineers. The cost of this inspection program could be largely borne by the MHUUD to incentivize owners.

- **Eviction guarantee for rental.** Term rental contracts under such an agreement could be endowed with a GOE eviction guarantee upon contract termination, and in cases of violation of contract conditions by the tenant. For cases where a completion loan is also involved, the rental contract terms could match the term of the loans, with an option to roll over both – financing and rental contract once (depending on scale of investment).

Box 5: Rental Subsidy Programs

There are two basic types of subsidy programs for rental housing:

Landlord Subsidies. A subsidy is given to the landlord in exchange for providing housing to a low-income or social tenant. Landlord subsidies can also be in the form of a soft loan that finances the improvement or construction of the unit. The loan is then amortized over the occupancy period.

A second form of landlord subsidy is an up-front cash amount that 'buys' the occupancy period. In Egypt, this type of subsidy would be similar to key money.

Tenant Subsidies. A rental voucher covering the difference between (a publicly determined, fair) market rent and the affordable rent during the occupancy period. The beneficiary of the rental voucher has the freedom to choose the location of the rental unit, so far as the landlord is willing to participate in the voucher program.

The Section 8 Program in the United States is an example of a subsidy program that offers both landlord- and tenant- based subsidies. Investment support to landlords is provided via project-based vouchers (the subsidy is directed to a specific unit for a restricted term, usually 20 years). The Housing Choice Program, on the other hand, provides support to tenants via vouchers that the tenant can use to rent a unit from any willing landlord. Moreover, tenants with vouchers can move freely between neighborhoods and even between cities. It is important to note, however, that a system like the Section 8 Program requires significant administrative capacity and the availability of up-to-date rental housing market data.

7.0 Enabling the NHP Housing Delivery System

7.1 Expanding the Role of the Private Sector

Under the NHP, the private sector is primarily engaged in development and lending. There are steps that could be taken immediately to expand and better define the role of the private sector within NHP that would simultaneously work towards the goal of redefining the GOE as an enabler of a well functioning housing system.

Advantages currently favoring public developers need to be removed to create a level playing field for private sector participation in the NHP. Currently, public developers receive an upfront subsidy of LE 15,000 per eligible household, whereas private developers receive *ex ante* (upon completion of construction) only LE 10,000 per household. Meanwhile, both are still required to provide the units at a maximum price of LE 50,000 per unit to adhere to the program guidelines. According to MHUUD, the reason why private developers are interested in this scheme is their ability to access public land for mixed income developments at below-market price under the 50-50 regime (market rate vs. affordable housing). The LE 333 per square meter charged for the remainder of the land for market rate housing is estimated by MHUUD to represent about 50% of the market price in the better located new towns around Greater

Cairo, which in light of the recent practice of NUCA of auctioning land to developers, appears to be the reason why private developers are interested in this model.[48] Developers opt for the 100% affordable housing option if there are no real financial gains from obtaining the marketable land at a discounted price. The initial objective was to pass on the marketing risk to developers, but the analysis of model contracts reveals that developers can hand over the units to MHUUD which will be responsible for allocating them to beneficiaries from its waiting lists. If this is the case, then developers may be choosing the 100% affordable housing option as a low risk (and likely low return) alternative because they are certain that the government will take over the units. As of May 2008, some 288,500 units have been earmarked for developers that expressed interest in the NHP.[49] One private developer, Orascom Hotels and Tourism, has acquired a site in Sixth of October City for the construction of 50,000 subsidized units.

To strengthen the growing mortgage market, subsidized lending should be curtailed under NHP. As more fully described in Section 3.1 of Part III, it is advisable to stop providing below-market interest rates (10.5%) coupled with the NHP subsidy, thereby allowing private banks to provide mortgage loans under NHP at market interest rates. If the goal of the below-market interest rate is to make the loan more affordable for low income households, then alternative measures could include interest rate buy-downs or the introduction of a guarantee program like FOGARIM in Morocco.

7.2 Rationalizing the Institutional Framework and Introducing Missing Functions

A host of long-term reforms to the institutions governing housing in Egypt were put forth in Part III, Section 5.2, however there are steps that could be taken immediately under the NHP to begin rationalizing the institutional framework and introducing missing functions. In the long run, the management of Egypt's overall housing policy needs a high level apex body/authority which can function as the housing sector coordinator. In the short-term, an inter-ministerial working group, backed by a monitoring and research unit located in the MHUUD, could be formed. Tasks of this working group would include the following deliberations and actions over the next four years:

Legal/Regulatory:

- **Private sector support and facilitation**, to give private sector developers a much greater role in housing production, both as part of the NHP and in the wider housing market. A regulatory framework, including laws/bylaws and a regulatory authority is needed to provide an even playing field for private sector participation.

- **Define better targeting and screening mechanisms**, to ensure that NHP subsidized units are going to families most in need of them.

Institutional/Procedural:

- **Streamlining and reducing duplication of agencies**, including the amalgamation of the numerous housing production agencies which exist under the umbrella of MHUUD at the national level.

48 An auction in May 2007 resulted in a price of LE 4,000 per M2 for well located land in one of the new towns around Greater Cairo.

49 In May 2007, 2,000 acres of land in Sixth of October were allocated to a private developer, Orascom, to construct 50,000 homes under the NHP. Orascom has opted for 100% of the units to be subsidized.

- **Strengthening governorate capacities**, especially the management and financing of housing projects through housing directorates and the economic housing funds.

M&E/Support for Policy Making:

- **Creating housing monitoring, evaluation and feedback capacities**: As a first step, the NHP itself needs to be well monitored. The full current costs and related subsidies of NHP projects need to be calculated on a regular basis, including land and infrastructure costs. Also, NHP products need to be monitored and evaluated as they are produced, including beneficiary take-up, payment, vacancies, and satisfaction (especially for innovative products such as *Ibni Beitak* and rental units). Also, monitoring success of the first mortgage packages, both under the NHP and GSF, will be essential.

- **Creating housing research capacities of wider housing markets**, both through investigations of secondary market and statistical data and through carefully targeted surveys of key housing issues, such as vacancies and affordable rental markets. Actions taken under NHP to begin data collection and organizing its analysis can work towards the establishment of a complete housing information system.

It is an open question as to who would undertake the important new functions suggested above and what might be the operational setups and information management systems. Some external technical assistance to the NHP would go a long way towards helping to establish these functions.

V. PRIORITIES AND FEASIBILITY FOR THE FRAMEWORK

Many of the suggested reforms for the housing and mortgage market are deemed to be high priority with a rapid pay off; others will take longer to address, or may encounter constraints on administrative feasibility, political feasibility, or relative cost. For example, improved regulation of the rental sector is very high priority, and is likely to be both administratively and politically feasible. It should also have a very high pay-off – with a positive impact on utilization of vacant units, on rental sector efficiency, and on the long-term prospects for accelerated rent decontrol. Similarly, addressing the problem of vacant and unfinished units is seen as extremely high priority, and has the potential for very high pay-off in terms of utilization of the vast capital stock of housing now sitting idle. The first recommendation here – a vacant unit survey – is needed to catalogue the wide variety of causes underlying the high vacancy rate.

On the other hand, one of the most important recommendations for the long-term health of the housing sector is acceleration of rent decontrol**.** This is categorized as a moderate priority/long-term endeavor because of expected problems in administrative and political feasibility.

Some of the highest priority suggestions build on reforms already in progress, simply suggesting that progress be intensified, given their importance to the market. These reforms include, for example, the ongoing efforts to develop the mortgage finance sector, increased involvement of the private sector in construction and mortgage finance under NHP, implementation of the registration system, and reform of the real estate law (important to the vacancy problems). Table 9 provides an overview of the criteria as related to each reform suggestion.

Table 9: Priority and Feasibility of Recommended Reforms in the Housing and Mortgage Markets

Recommended Reform	Potential Results And Pay-off	Administrative Feasibility	Political Feasibility	Relative Cost to Implement
Highest Priority Recommendations, with an expected rapid pay off				
Rental Market Regulation	High: rental market efficiency Utilization of vacant stock	Yes, but involves improved civil contracts and setting up contract registration facilities	Likely	Modest, includes training
Utilization of Vacant Units	High: efficient use of the capital stock; match demand/supply	survey yes, but tax policies/ incentives will take more time	Likely	Modest
Intensify Mortgage Market Development	High: supports both housing market and financial sector growth	Yes - ongoing	Yes	Low
Mortgage Credit Enhancement	Medium: expanded down-market	Yes - ongoing	Yes	Low

	mortgage lending			
Relaxed Land Use & Building Standards	Medium: Cost-effective means of increasing affordability	May find resistance within MHUUD	Design issues may arise?	Modest
Institutional Development	High**:** Crucial to undertaking comprehensive reforms	Difficult: inter agency collaboration	Likely	Minimal
Microfinance for Housing	Medium: Lending to lower income, support informal sector	Yes	Yes	Low
Priority Recommendations, which will require a medium- to long-term horizon				
Accelerate Rent Decontrol	High long-term: greatly improved efficiency of rental sector	Difficult	Difficult	Relatively high
Private Sector Rental Market Development	High long-term: increased private sector rental development	Modest: need tax policies	Likely	Modest
Greater supply of well located land	High long-term: better located land for housing	Difficult: inter-agency cooperation	Difficult	Relatively high if purchase
PPP Regulations in Housing Development	Modest: better cost and risk sharing in government housing projects	Might require new legislation	Should be acceptable	Modest
Speed-up registration work	Modest: efforts are already underway	Yes - ongoing	Yes	Modest
Informal Sector Development	High**:** integration of major portion of the housing market into the formal sector	Very difficult: informal areas not recognized or regulated	Difficult	Could be modest if largely undertaken by private sector

Table 10: Evaluation Criteria for NHP and Future Housing Program Reforms

Reform	**Program Efficiency**			**Distributional Impacts**			
Evaluation Criteria	**Cost per unit**	**Subsidy dependency**	**Admin simplicity**	**Down-market push**	**Targeting efficiency**	**Location impacts**	**Tenure choice**
Highest Priority Recommendations							
Private sector role via PPPs	Should fall	Will fall	Could worsen?	Could impro	n.a.	n.a.	n.a.

				ve			
Utilize vacant units in NHP	Should fall	Will fall	Could worsen	Could impro ve	Could improve	n.a.	Could impro ve
Better located land supply	Could rise	n.a.	n.a.	n.a.	Could improve	Will improv e	n.a.
Improve targeting	n.a.	n.a.	Could worsen	Will impro ve	Will improve	Could improv e	Should impro ve
Increase affordable mortgage lending	n.a.	Will fall	n.a.	Will impro ve	Will improve	n.a.	n.a.
Develop micro-finance for housing	Fall for self-build?	Will fall	n.a.?	Will impro ve	Will improve	n.a.	n.a.
Streamline NHP management	Could fall?	n.a.	Should improve	n.a.	?	?	Could impro ve
Improve location policies	Could rise	n.a.	?	n.a.	Could improve	Will improv e	n.a.
Provide additional affordable options	Should fall	n.a.	?	Should impro ve	Will improve	n.a.	Could impro ve

VI. SUMMARY OF RECOMMENDATIONS

Table 11: Summary of Reforms to Develop a Well-Functioning Housing System

WELL FUNCTIONING HOUSING SYSTEM REFORM RECOMMENDATIONS	
Issue/Reform Type	***Summary of Recommendations***
Address the Excess Vacancies Problem	
Unlock Vacant Units *Goal: Better Use of the Housing Stock, both Government and Private Housing*	• Conduct a vacancy survey to determine vacant unit status and causes • Consider tax incentives linked to utilization of vacant units • Utilize streamlined lease and eviction procedures to promote rental utilization • Link disincentives to holding vacant units to the improvements currently underway in the real estate tax system
Improve Rental Market Regulation	
Improve Rental Market Regulation *Goal: Rental Market Efficiency and Reduced Vacancies*	• Define model rental contractual agreements governing the rights and responsibilities of tenants and landlords and related issues (termination, rent adjustment, etc) • Develop an ombudsman or other out-of-court mediation to lower the costs of dispute resolutions • Establish low or no-cost windows for registration of rental contracts • Streamline eviction procedures and offer education of judges, as for mortgage sector • Provide consumer education and publicity campaigns on rent reforms
Rent Decontrol and Rental Market Development	
Accelerate the Rent Decontrol Process *Goal: Efficiency and Equity in Rental Housing*	• Review international models of rent decontrol to further strengthen Egypt's approach to grandfathering • Condition right to bequeath to acceptance of rent increases, or limit tenure right of heirs (e.g. to 2, 5 years) • Support low income tenants with rental allowances in this process
Continue Reforms to the Mortgage Finance Sector	
Continue Mortgage Market Reforms *Goal: Fully Functioning Mortgage System*	• Continue efforts to improve legal framework/ revise tripartite contract • Develop credit and housing market information systems
Develop Credit Enhancement Policies in GSF *Goal: Risk Sharing in Down-market Lending*	• Develop new credit risk sharing programs with GSF, including mortgage guarantee insurance, to encourage expanded and down-market lending • Stop current GSF "3-month payment" guarantee • Promote GSF's credit enhancement roles • Separate guarantee function from subsidy role • Develop pre-titling guarantee by GSF for mortgage loans until registration
Develop Microfinance for Housing	
Expand Housing	• Provide support (e.g., product information, credit information, liquidity

Microfinance *Goal: Housing Finance for Low Income Households*	support) for development of low income housing loan products • Explore credit enhancement systems for housing microfinance through GSF
Land Use Planning and Building Standards	
Strengthen Land Use Planning *Goal: Reduced Development Costs*	• Increase the land development ratio (both land coverage and maximum permissible development) • Streamline land subdivision and building permit systems • Make use of well locate public land for affordable and mixed-income housing: o Evaluate the public land holdings of sectoral ministries, SOE and decommissioned land uses o Repossess undeveloped public land (post contract period)
Adjust Building and Land Use Regulations *Goal: Improved Affordability*	• Authorize subdivisions and affordable building and infrastructure standards in specified special "popular" neighborhoods with local government regulatory control • Provide incentives for mixed-income housing developments • Provide regulation for mixed commercial/residential use; end restrictive zoning • Modify regulations on building height, floor-area-ratios, and land for services
Enhance Supply of well-located Land *Goal: Better Located Housing Developments*	• Develop regulations for development of private land for affordable housing, including "special zones" • Inventory public lands in cities and new towns and investigate use of *Awqaf* lands • Review ban on conversion of agricultural land for urban use in special zones, especially the agricultural land pockets (*mutakhalellat*)
Continue Reform of Land & Property Registration Systems *Goal: Increased Registration of Property*	• Enhance ongoing efforts in improving land registration • Consolidate survey and registry in one institution • Harmonize registration laws • Discontinue/regulate proxy registration and loopholes • Conduct major public awareness campaign
Improve Targeting	
Improve Targeting of Low Income Households *Goal: Decrease Leakage and Increase Equity*	• Better enforcement of existing criteria to help limit vacancies and speculation • Streamline targeting methods for all federal subsidized housing programs • Consider additional targeting criteria to improve accuracy
Government as a Housing Market Enabler	
Institutional Reform *Goal: Improved Policy Development*	• Establish high-level inter-agency "policy" council with a strong technical secretariat • Provide proposed National Housing Authority and high level policy council with greater policy-making and investigation/evaluation/monitoring

	resources • Merge/streamline public housing supply institutions to reduce duplication • Develop rental sector regulatory agency • Help strengthen the capacity of Governorates and their economic housing funds
PPP Models *Goal: Better Sharing of Risk*	• Enhance role of the private sector in servicing and collection of rents in government projects

Table 12: Summary of Improvements to the NHP

FOCUSED IMPROVEMENTS TO THE NATIONAL HOUSING PROGRAM	
Issue/Reform Type	***Summary of Recommendations***
Utilize Existing Housing Stock under NHP	
Vacant and Unfinished Units *Goal: Leverage NHP to Active Vacant Housing Stock*	• Use NHP subsidy for qualified buyers for unfinished units (possibly link to mortgage or consumer loans) • Use NHP subsidy for qualified owners to complete units (possibly link to mortgage or consumer loans) • Use NHP subsidy as an eviction guarantee, thereby enabling recipients to use it for rental units • Use subsidy to assist down-payment (key money) for rental units • Investigate feasibility of transportation subsidy for New Town residents
Expand Affordable Mortgage Lending	
NHP Mortgage Lending *Goal: Support Development of the Growing Housing Finance System*	• End below-market interest rates (10.5%) for NHP linked loans; banks to provide mortgage loans under NHP at market interest rates • Explore using interest rate buy-downs to assist affordability • Consider provisional registration or post-construction permits to allow eligibility for mortgage loan • Register properties built on State land
Credit Enhancements *Goal: Broaden down market lending via risk sharing*	• Consider, in the medium term, to pay for future GSF mortgage guarantee insurance, for NHP-eligible households
Develop Microfinance for Housing and Integrate with Affordable NHP Programs	
Provide Microfinance lending in NHP *Goal: Assist Lowest Income Households to Improve their Housing Conditions*	• Develop a more affordable core housing scheme that is based on the beneficiary acquiring a microfinance loan. • Build on current lending in microfinance for housing by NBE, Bank Alexandria, and Banque du Caire)
Establish Housing Savings Accounts	• Use savings as a rationing device and underwriting tool for housing microfinance

Goal: Improve Savings Levels and Use of Banking System	
Improve Land Supply and the Location of Land for NHP projects	
Better Located Land Supply for Subsidized Sousing *Goal: Better Supply of Well-located Affordable Housing*	• Make land for NHP projects available to match employment, transport, and education opportunities/needs of low income households • Allow use of NHP subsidies for housing on non-State land
Additional Housing Typologies/Programs *Goal: Improve Reach of NHP to Lower Income Households*	• Relax land and building standards for the *Beit Al-Ailaa* (family house) and *Ibni Beitak* (build your own house) programs • Introduce mixed-use residential/commercial development to allow cross subsidies to operate at the project level
Improve Targeting under NHP, especially of homeownership programs	
Improve NHP targeting *Goal: Decrease Leakage and Increase Equity*	• Pilot new targeting methods using existing mechanisms ("piggy-back" approach) o Proxy income eligibility using MOSS or food ration programs o Consider test of Proxy Means Testing o Consider use of electricity usage or car ownership as income proxy • Consider additional targeting criteria to improve accuracy o Over-crowded and/or poor living conditions; single parent families o Residents of informal areas and slums o "Group" applications for extended family moves to New Towns or other areas
Improve Rental Programs under the NHP and Consider Additional Ones	
Rental Program Improvements *Goal: Liquid Rental Market*	• Relax unit size constraints (to address local demand, cost differentiation) while keeping overall cost limits
New Rental Programs *Goal: Modernization of Stock and Activation of Vacant Housing*	• Subsidies to landlords to provide housing to a low-income tenant
Increase the Private Sector's Role in NHP	
NHP Private Sector Role *Goal: Level Playing Field for Private*	• Engage more private lenders via market-based lending and credit enhancements

Participation	
PPP Opportunities *Goal: Broaden the Scope of Possible PPPs*	• Develop PPP policies in NHP projects that entail private sector risk sharing in completion costs, timing, and marketing goals • Utilize private collection services such as those of the HDB • Revise contractual agreements for NHP housing projects to increase risk sharing between private developers and the Government
Rationalize the Institutional Framework	
NHP Management *Goal: More Efficient Delivery of Services*	• Initiate a high-level inter-agency working group • Increase outreach/public awareness of NHP options • Improve budgeting by accounting for land and infrastructure costs • Monitor post delivery of NHP units for vacancies, resale and rent to third parties

VII. ANNEXES

Annex 1. Summary of Previous Studies and Reports

Over the last year, four studies on housing in Egypt were conducted. The first is a ***Housing Supply Analysis Note*** (World Bank), which analyzes the situation of urban housing supply in Egypt, including the study of existing formal and informal mechanisms to deliver for urban housing, institutions responsible for supply and regulation, the characteristics of the formal and informal housing, and the institutional and regulatory framework governing land use planning and development. The second study is a ***Housing Demand in Greater Cairo*** (USAID TAPRII), which uses data surveyed in December 2006 and yields results on the housing demand and household characteristics. The third is an ***Analysis of Subsidized Housing Programs*** (USAID TAPRII), which assesses past, existing and pipeline subsidy programs in Egypt to draw lessons learned. Finally, ***International Best Practices*** were presented at a workshop held in April 2007 with the intent of assessing different schemes of housing subsidies and reforms used in other emerging markets, in order draw lessons pertinent for Egypt.

The following sections summarize the main findings of the three documents. The key messages from the International Best Practices presentation are summarized in Annex 3.

1.1 Housing Supply Analysis Note

Due to a large number of vacant units, the total urban housing stock exceeds the number of urban households. The government must address distortionary regulations in order to unlock the vacant units to accommodate new housing demand. The average annual growth rate of the urban housing stock in Egypt (3.6%) far surpassed that of the urban population (1.9%) during the inter-census period (1986-1996). By mid-2005, the total number of housing units in urban areas in Egypt reached close to 9.49 million units. By contrast, in January 2005, the total number of urban households was estimated at 6.84 million units. The result is that in 1996 there were 1.4 housing units per urban household and 2.64 million housing units that were vacant or unused. Taking into account multiple unit ownership (10% of urban households owned/controlled 20% of the total housing stock), there still was in 1996 about 20% of the total urban housing stock that could be considered to be available on the market, whether units ready for occupancy, that are still under construction or which remain unfinished for a long time.

Almost 40% of new urban housing is produced by the informal sector. During the inter-census period (1986-1996), the total urban housing stock grew by an annual average of 241,916 units, of which 151,896 units (62.8%) were formal and the remainder (90,021 or 37.2% of total) were informal. In the 1986-1996 period, the public sector built 29.5% of all new (formal and informal) housing units built in urban areas during this decade and 47% of the formal housing stock, with the private sector responsible for 33.3% of total housing stock and 53% of formal housing stock. The largest producer of urban housing during this period was the informal sector, conservatively estimated to have delivered 37.2% of all new units (the ratio would be higher if we account for replacement units).

Over the past 25 years, the public sector has built as much as 36% of all formal housing units supplied in urban areas, which came at a significant cost of LE26.4 billion to the public coffers. A plethora of public agencies and programs for direct of supply of affordable housing exist in Egypt today. These include Governorates, housing and development companies, the Joint Projects Agency, the General Organization for Housing Construction Cooperatives, the Housing Finance Fund, the Housing and Development Bank, development agencies, and the New Urban Communities Authority. Together, these entities have delivered 1.26 million public housing units during the period 1982-2005 (36% of all formal housing units built during this period in urban areas) at a total cost of LE26 billion, excluding the cost of land and off-site infrastructure. By and large, the largest supplier of public housing was the Governorates, which were responsible for the supply of 44% of the total public sector-built stock in urban areas during this period and mostly targeting low- and moderate-income households. This shows the extent of local government contribution to public housing supply, an impact that could have been even greater had they not had limited local revenues and had their mandate evolved to enabling access to affordable land and housing within their jurisdiction instead of direct supply. The Housing Cooperative system delivered as much as 22% of the total public stock provided in the 1982-2005 period, although it is increasingly seen as out of favor with the General Organization for Housing Construction Cooperatives' budget falling to less than one-fifth of its peak of over LE1 billion in the 1995-98 period. Finally, NUCA was responsible for 20% of the total public stock, but similarly its total investment has fallen to about 5% of its peak of about LE1.1 billion in the 1997-99 period.

There has been a steady increase in the private sector's share of annual formal housing production over the past decade. With respect to the formal sector, the private sector contributed 64% of all formal housing units built in urban areas between 1982 and 2005, with the total investment having exceeded LE60 billion. The 1992-99 period was the only trough observed in the private sector's performance, where its share of the formal housing stock was less than half (ranging between 33-48%). Since then, a positive trend has been the steady and significant increase in the private sector's contribution, which reached 88-90% of all new formal units since 2002 with an average of 145,000 units per year. At the same time, the public sector's annual average fell to a little over 18,000 units, which points to public sector withdrawal from direct supply and an invigorated private sector playing an increasingly important role in housing supply.

The urban housing crisis in Egypt is not a quantitative/scarcity problem but distortions to the housing market caused by an accumulation of ill-conceived and inadequate policies that led over time to creating a mismatch between supply and demand and to severely curtailing private sector investment in housing supply. The problem manifests itself among other things in a large share of the existing urban housing stock being kept vacant and under-utilized, and in private sector withdrawal from investing in the rental housing sector to focus instead on the upper segments of the market catering for homeownership (which is simply unaffordable even for middle-income groups in the absence of housing finance). It is also argued that there was, and still is, a mismatch between housing demand and supply, with on the one hand an oversupply of formal housing for upper-middle and high-income groups (at the same time as demand was dampening due to weakened purchase power), while on the other hand there is a shortage of supply for low, moderate and even middle-income groups, leaving the informal sector to meet their needs.

Limited income groups, unable to afford formal housing or adequately located and serviced land upon which to build especially in large cities, found that they had no option but to seek shelter in informal and squatter settlements. Construction costs in the informal sector, even with a 20-30% cost add-on in extra-legal payments to circumvent problems with local authorities and utilities and navigate the bureaucracy associated with informality, are still more affordable than formal housing supply. The end housing product is more suited to people's needs and the progressive construction method is more adapted to their priorities and affordability level. What is interesting is that even in the informal sector, there is an oversupply of housing units, estimated in the GCR at 500,000 units and in a sample of three informal settlements at 15-20% of the total stock.

There is a large stock of formal and informal housing units that are vacant and which could be brought back to the market if an appropriate regulatory framework and incentives to owners/developers could be secured and effectively implemented/enforced (including enhancing the security of property rights to land and real estate, and ensuring when needed expeditious court-administered tenant eviction procedures in case of end/breach of contract terms and conditions).

The positive trend of increased private sector participation and investment in housing supply needs to be capitalized upon, and obstacles facing the private sector need to be removed, if it is to play the lead role in housing supply. Adequate (supply-side and/or demand-side) incentives will need to be provided for the private sector to cater to the needs of low and moderate income groups, including making available well located and serviced land, streamlining bureaucratic procedures for land subdivision and building permit issuance and property registration, and enhancing the end-users' affordability levels through among other things enhanced access to housing mortgage finance.

The main challenge today is to devise affordable housing policies and strategy that address the distortions that to date constrain the housing market from functioning efficiently. The first critical steps in this regard were the abolition of the rent control legislation in 1996, after five decades in which it severely distorted the housing market, and the set up of the regulatory and institutional frameworks governing housing mortgage finance. The key remaining challenges that the new affordable housing policy will need to address are to: (i) put in place the institutional and regulatory frameworks and incentive structure needed to enable an expanded private sector role in the delivery of affordable housing in a competitive and transparent framework; (ii) rationalize the subsidies provided to limited-income groups by eliminating distortionary and off-budget instruments and developing efficient targeting instruments that could be easily administered; and (iii) ensure that the regulatory framework and incentives allow the development of a viable rental market to serve the needs of the lowest income groups in conjunction with some homeownership opportunities (which are more expensive and thus less scalable).

1.2 Housing Demand in Greater Cairo

As requested by the Ministries of Investment and Housing, TAPR II completed a comprehensive and in-depth empirical analysis of the demand for housing in the Greater Cairo area. The analysis used data collected from December 2006 to January 2007 under the TAPR II 2007 Housing Demand Survey. This survey uses the same representative sample that was employed by CAPMAS in its 2004–05 HIECS survey for Greater Cairo and covers 9,082 households. To collect the housing data, TAPR II drafted a questionnaire that took into account comments and inputs of principal stakeholders of the Egyptian housing sector. The TAPR II 2007 Housing Demand Survey is the first comprehensive housing demand survey carried out in the last 30 years. It yields results that shed interesting light on the housing market, especially demand characteristics, in the Greater Cairo Area. These results are summarized below.

The majority of the TAPRII survey respondents who are seeking housing are young men who plan to marry –61.2% of the demand is for long-term lease; 54% of families currently looking for housing prefer a long-term lease. It is estimated that there were 603,701 housing demanders in Greater Cairo in 2006. In other words, the percentage of demanders among households was 17.5 percent of 3,452,679 households. Cairo City had 341,492 demanders while 217,022 demanders were in Giza City and 45,187 demanders were in Shobra El-Kheima. The vast majority of those who are currently seeking housing are male (93.1%), and 46% of them are in the age range of 20 to 30. 56% of respondents have indicated marriage as reason for needing a housing unit. Other reasons cited include small size of current units (16%) and seeking independence (8.8%). The high demand for rental housing is clearly reflected by the survey finding that the majority of households who acquired their units between 2001 and 2006 chose rental housing (82.2%). Indeed, only 17.8% bought their units.

The majority (81%) of households looking for housing have incomes less than LE 1,000 per month. The higher demand for lease is for units of 63 m2 with rent values not exceeding LE 200. Demanders are ready to pay advance payments up to LE 12,000 for a rent of LE 100. Demand for larger units of 100m2 for rent is much lower with rent ranging between LE 200 and LE 400. Demanders are ready to pay advance payments up to LE 24,000. The low-income categories prefer a lower down payment and higher installment value. In regard to homeownership, 93.9% of demanders are in favor of installment payments. The preferred mean installment value is LE 332 per month and mean down payment LE 13,101. But, among the offered models, demanders picked the option of paying a down payment of LE 5,000 for unit sizes 63m2 to 90 m2.

Young households (between 20 to 30 years of age) are more accepting of the concept of mobility than older households. They accept the idea of starting with a small rented unit and then moving to larger one as soon as need arises and financial capability improves. Older respondents reject this idea. Indeed, 58.7% of demanders (who have not yet been married) intend to move alone to new unit. However, demand for units below 40m2 is very low, and 60% of families looking for housing want 80m2 or more. Demand for serviced land represents only 3.8% of total demand. The demand is mainly in new communities where land is currently available. Land demanders' affordability levels are as follows: 31.6% have monthly income between LE 500 and 1,000; 31.6% have monthly income between LE 1,000 and 2,000; 10.5% have monthly income between LE 2,000 and LE 3,000; and 19.3% have monthly income of more than LE 3,000.

Only 3.8 percent of the surveyed household who bought their housing unit between 2001 and 2006 bank-financed the purchase of their home. The median market price per square meter during that period was LE 666.7. Moreover, prices per square meter (at current prices) were stable during that period, as they had exhibited no consistent trend either upward or downward. Among these households, 76.9 percent paid in full while 23.1 percent paid in installments. Only 3.8 percent (of the 160 buyers) had taken a bank loan to partially finance their housing purchase. The majority of buyers had used their regular income savings to finance their housing purchase (65.0 percent of purchases), or proceeds from sales of their property (45.0 percent of purchases), or contributions and loans from relatives and friends, and loans from workplace. Among borrowers, the preferred loan period was 3 years and monthly installment payments commonly ranged from LE 500 to LE 1,000. Respondents who did not borrow from a bank cited the cost of a bank loan and the need for collateral as the reasons they did not turn to this financing source. Some respondents also cited cultural barriers for not acquiring bank loans. More generally, few Greater Cairo households have dealings with banks. Survey results show that 78.9 percent of surveyed households have no dealings with banks, financial corporations, lenders, or mortgage companies.

Both singles and families currently looking for housing overwhelmingly prefer Greater Cairo, 71% and 67% respectively. For singles, New Cairo is the top choice among the New Towns, and 6th of October is the top choice among families.

The survey found that there was very limited awareness or understanding of the National Housing Program options. Moreover, once the NHP options were described, the overwhelming sense was that they are not affordable. There were widespread comments on loan terms, purchase price, and rents all being "too high".

The demand study concludes that the GOE needs to better align housing programs with the needs of those who are looking for housing. Across all income groups, the greatest demand is for rental housing while most of the NHP offering are for homeownership. The Government has increased rental housing in the public supply pipeline, including 100,000 units to be provided on *Awqaf* land, but more rental programs should be considered including options for renting from private owners. Another significant finding of the demand study is that most households who are currently looking for housing prefer to stay in Greater Cairo. Extrapolating this finding to the national level, it could be assumed that households prefer to live close to where they are currently living. Converse to this finding, the NHP plans to build one-third of the 500,000 unit goal in New Towns.

1.3 Analysis of Subsidized Housing Programs

In Egypt, overwhelmingly the predominant form of housing subsidies are found in the various government-financed and government-implemented housing programs which are ostensibly aimed at lower-income households. These government programs are under different authorities; however, the housing models and payment conditions have remained remarkably similar. Government-provided, subsided public housing in Egypt has a long history, starting in the early 1950s. The serviced land upon which this housing has been built is, almost without exception, provided at no cost by the State and thus represents a subsidy element in addition to the construction cost which is subsidized mainly through low installment payments and the infrastructure cost which comes from various State budget lines. Since the 1980s practically all housing programs have been for home ownership.

Other forms of housing subsidies in Egypt are not considerable in value or coverage, especially compared to those operating within government housing programs. First, State land (usually desert land) has been and continues to be allocated to authorities at zero cost or at prices that are below the costs of servicing these lands with infrastructure. These mechanisms represent a direct financial subsidy, although recently government agencies controlling State land have sometimes been imposing acquisition prices that tend to cover at least some fraction of the infrastructure costs. Second, In the 1970s and 1980s key building materials such as cement and steel rebar were sold at official prices through the building permit regime which were considerably lower than prices on the open market. However, this practice has been discontinued for roughly 20 years. There are currently no known subsidies operating in housing construction. Third, although infrastructure and public services are loaded with direct and indirect subsidies, they tend to apply to all consumers and are not specifically targeted at the poor or the beneficiaries of housing programs. For example, practically no one in Egypt pays the full cost of water and wastewater services. Last, the implicit subsidies which housing can enjoy through tax breaks and holidays are few, simply because in Egypt housing is little exposed to tax regimes. The property tax imposed by the Ministry of Finance is universal on all residential properties (even that of squatters!) and is thus neutral, except for the fact that it is always behind in evaluation, in collection and in geographical application. In any event the annual effective property tax rates are extremely low.

Over the period 1952-1982 MHUUD records show that a total of 1,118,000 units of government housing were built, at an average annual rate of 37,790 units. Over the 1982 – 2005 period production ranged from 14,000 to 100,000 units, with an annual average production of 54,700 units. Most recently, in the 2001-2005 period, annual production has been way below the average (only 15,000 to 35,000 units annually). The largest portion of total government housing was produced by local government, i.e. governorates, (44% of the total for the 1982-2005 period). However, from a high annual production rate of almost 50,000 in 1992-93 governorate housing production has declined fairly steadily, and in the 2002-2005 period such production averaged only 12,000 units per year. The second most important type of government housing production was by housing cooperatives, with 22% of total production over the 1982-2005 period. However, from a high rate of production up until 1997, cooperative housing has declined dramatically, so that in the 2002-2005 period the annual rate was less than 3,000 units. The third most important type of government housing production was in the new towns, with 20% over the 1982-2005 period. In the 1997-2002 Five Year Plan period annual new town housing production averaged 25,000 units or 45% of the Government total, but in the 2002-2005 period production fell dramatically to less than 2000 units annually (9.4% of the Government total for that period). Other forms of housing production (by Government housing companies, the joint projects agency, the housing fund, the housing bank, and tamiir agencies) represent only small contributions to the total production of Government housing (less than 14% over the whole 1982-2005 period). It should be noted, however, that there have been extensive amounts of public housing built over the years by the armed forces and Ministry of Interior for their personnel. Unfortunately there is no information about this housing.

Although theoretically government housing is aimed at households with limited income, as far as is known there have been no attempts to target beneficiaries based on income or wealth thresholds or means tests. In fact, in most government housing programs the required qualifications are of the most rudimentary, with available units being distributed by lottery if demand exceeds supply. Over decades the Egyptian government has relied on a standard application process to begin the housing unit distribution process. National level housing authorities and governorates announce that there is a housing program and accepts filled in applications (istimarat) from citizens. In the governorates, citizens in need of housing can apply at any time at the housing directorates. These applications are usually very straightforward, and require payment of a nominal fee.

- Although targeting and distribution of units varies from one governorate to another and even within a governorate from one year to the next, the following can generally be said to apply: Citizens wishing to acquire government housing units purchase applications from the Housing Directorate (usually LE 5 to LE 20). It is usually required that an applicant be living in the governorate (as recorded on the ID card) and that he/she be married. Other criteria might apply, such as a statement that the applicant has no residential property. In any event the submitted application is screened and if considered accepted it is put on the waiting list. When a number of units (usually a phase of 250 to 1000 units in a particular site) are completed, either: (1) the oldest applications are picked by their date of submittal; or (2) all qualifying applications are submitted to a lottery and applicants are picked randomly until the required number is reached.

- Applications for units in the new towns are either filed with the particular new town agency or at one of MHUUD's national housing authorities, with new town preference indicated. As with governorate housing, the submitted application is screened and if considered accepted it is put on the waiting list. When a number of housing units near completion, either: (1) the oldest applications are picked by their date of submittal; or (2) all qualifying applications are submitted to a lottery and applicants are picked randomly until the required number is reached.

In 2001 MHUUD developed a basic point system under which beneficiaries qualify and units were to be allocated, but the logic behind the point structure seems a bit confused, since higher points are given for applicants which are older and have higher education levels. It also puts an emphasis on those who are married and have more than one job, and gives considerable weight to those working in new towns. Whatever the merits of this point system, it is understood that it has very rarely been used. In effect, since most MHUUD housing is in very remote desert locations where there is little urban life, practically anyone can qualify for the purchase of units if they meet very simple requirements and can come up with the reservation down-payment.

In all programs the allocation of units in a particular housing project is random, with valid applicants assigned units through lists. That is, there is no means for a group of families to acquire units in the same building or area, and thus they cannot hope to bring with them even a fraction of the social networks and capital embodied in extended family or co-worker relationships. (Such is extremely important for those of limited income.) This stands in stark contrast to how general housing markets, including those of the informal sector, work. In these cases one knows exactly the unit being purchased or rented, including the pros and cons of the neighborhood and who will be neighbors. In new, especially informal, residential areas there is thus the ability to re-produce at least some of the "social glue" upon which livelihoods of the poor depend. In new public housing, by contrast, one will be living with complete strangers. (It is no accident that theft is a common complaint in some new public housing estates.)

Government housing programs in Egypt provide very high direct and indirect subsidies, estimated at 60 – 75% of the unit cost. Taking the 63m2 unit of the recent Mubarak Youth Program as the base case and assuming a discount rate of only 9%, results show that the smallest unit in the Mubarak Youth Housing Program has an extremely high subsidy cost in terms of the State budget. At least 68% of every pound directly invested by the State in such housing is never recovered. There is also a loss of potential land revenues, which raises the total subsidy to at least 75% of full costs per unit. And the true subsidy element is much higher, since calculations assume perfect repayment, no cost overruns, rapid construction and timely allocation.

Land for government housing must exhibit one key attribute: it must be State land. There is no budgeting for land acquisition in government housing. Thus planners of any government housing scheme must seek locations where the land is owned by the State and whose acquisition is costless. The result is that almost all government housing is located either in the new towns in remote desert locations or on local government desert lands which are also far from existing urban agglomerations. This results in a miss-match between geographical supply and demand and makes it difficult for beneficiaries, especially those of limited income, to pursue normal livelihoods. It is no wonder that in more recent government housing programs vacancy rates always exceed 50%.

Most observers would agree that Government housing is, in general, of good structural quality. Under the Mubarak Youth Housing Program, finishing quality improved noticeably (but then so did the comparable cost per unit).

In volume terms, government housing production does not begin to address the housing needs of lower income families. In the last 25 years the government has been producing an average of 50,000 subsidized units per year. And recent trends show that this volume is decreasing. Compared to the annual national need for new low cost housing units, such direct provision of housing can at best only meet a fraction of gross need. And, whereas the annual need for low income housing is increasing every year, historically the supply of subsidized housing units is decreasing.

Given the high subsidy element in past government programs, both the down payments and installment payments could be considered affordable by over 80% of urban households. But are lower income households the main beneficiaries of government housing programs? It is extremely difficult to answer this question because the targeting/assignment system is rather random, depending on an “application regime” which is executed partly on a lottery basis, and partly “rationed” by the small size of the unit and unattractiveness of certain locations. Certainly a portion of those gaining new government units will turn around and sell them, thus enjoying a once-off windfall financial gain, which if they are truly poor could be seen as a kind of un-intended income transfer. There is no information on the incomes of beneficiaries (and no attempt to distribute units on an income means basis).

Annex 2. International Best Practice: Lessons for Egypt

A set of international best practices were presented in the April 2007 ministerial working session with the intent of outlining the types of housing subsidy being used in emerging markets worldwide, the advantages and disadvantages of each, and the lessons learned that can assist Egypt improve and broaden its National Housing Policy. Among others, the experiences of Chile, Jordan, South Africa, and Morocco were used to illustrate (i) homeowner demand subsidies, (ii) homeowner supply subsidies, and (iii) rental programs. Additionally, system-wide delivery mechanisms in the financial sector and public institutions were addressed. These included financial institutions designed to address risk and liquidity in the mortgage finance system and public institutions, such as housing banks, used to deliver subsidies.

Overall, approaches to creating housing subsidy policies have become more comprehensive and cross-sectoral, taking into consideration the real sector (land, infrastructure, and construction) and the financial sector (institutional support and private sector delivery). A broad mix of subsidy policies has developed with improved income targeting (supply, demand, owner and rental, and financial sector). The role of the private sector has increased substantially, with private companies serving as low cost developers and providing mortgage finance, including micro-finance. At the same time, governments have moved towards serving as an "enabler" of the housing system, rather than a direct participant. There is a clear and necessary role for government in the development of the legal and regulatory framework (mortgage finance, tenant landlord regulations, and rent decontrol), legal Institutions, and land delivery and titling systems. For the lowest income groups, where private sector participation is limited, the government may serve as a housing provider. The policy trends in regard to providing housing to the lowest income groups focuses more attention on targeting, location, and preventing pockets of poverty. Additionally, more attention has been directed to core housing, progressive housing, and micro-finance for housing. Importantly, there has been a rise in conducting independent evaluations of housing subsidy programs and policies to ensure that they are operating effectively and producing the desired results.

2.1 Overview of Subsidy Options

Down payment grants are quite common in Latin America (Chile, Peru, Columbia, Mexico, Ecuador, Guatemala, El Salvador, and Uruguay), and are usually coupled with a mortgage loan and household savings or down payment requirements. Down payment grant programs may include both formal sector and progressive/self-build housing. The down payment grant approach has tended to focus on higher income households, but this is changing (Mexico now targets to about the 36th percentile of income; in Chile, 84% of resources now go to the bottom quintile). Key advantages of this type of subsidy program are that (i) it reduces the housing deficit by supporting affordability; (ii) it is efficient – reaches household directly and relies on the private sector; (iii) it allows for a private sector role – usually involves credit form a private institution and stimulates private sector housing supply; (iv) it often allows choice of location; and (v) it is often linked to a mandatory savings programs. However, there are also some significant disadvantages. For example, because targeting is a critical design issue, it is administratively demanding to structure and manage eligibility systems that include means tests, monitoring of savings, and tracking regional housing prices. Additionally, for down payment grants to provide the desired result, the country must have a housing market that works well. Indeed, the elasticity of supply must be adequate or down payment subsidies merely raise prices or benefit developers. The mortgage finance system must be able to finance a large numbers of beneficiaries. Finally, it is difficult to address the needs of the poor because they likely cannot access the required credit component, and an attempt to reduce the cost of the unit to one that is affordable for the poorest will likely lead to extremely small and poorly located housing solutions.

Chile provides a great case study of the classic three-part approach to down payment subsidies. The Chilean program worked well for middle-income households, and effectively engaged private developers and private lenders. Low-income households, however, required public loans and publicly led development. While the Chilean model achieved high quantities of production, it did so at the expense of neighborhood and housing quality. Indeed, the need for developers to find cheap land for development pushed new neighborhoods to the fringe of cities, concentrating the poor in areas where there was a lack of access, jobs and transportation. Additionally, the need to minimize construction costs led to small, poor quality units in some cases. Recent housing policies have aimed to fix these issues. Mortgage credit has been removed from the programs for the lowest income households, and replaced by a grant from a new social fund and the private sector has taken over nearly all functions. An international design competition was held in 2003 to find creative progressive housing solutions that would enable the development of high density, in-fill housing for the poor. Partnerships with NGOs to help organize groups of applicants and provide social support. Targeting was refined to provide variation for regional price differences, and subsidies, savings requirements, and unit size. Location subsidies were added to help pay for higher cost land near transportation. Evaluation of Chile's program led to major changes. A key lesson from the Chilean experience is that mortgage loans may not work for lower income groups – alternatives include savings programs and grants. Innovations in expandable core housing found a better match for preferences. The importance of appropriate locations and coherent neighborhoods was a key lesson for Chile, and as such, the location subsidy became a key add-on to the program. The private sector increasingly took over construction and lending. Subsidy targeting takes into account income, savings, region, and urban versus rural contexts. The Chilean targeting system is highly efficient but requires extensive administration.

Internationally, there are three basic types of credit subsidies for housing – interest subsidies, special savings-loan circuits, and interest tax deductions. Examples of interest rate subsidies include interest rate buy-downs (Poland, Czech Republic, Hungary, and Chile), subsidized borrowing/lending by public lenders with pass-through to private sector (almost global), and fixed-rate lending without benchmark, hedge (Russia and Mexico). The advantages of interest rate subsidies are that they are simple to understand and the costs of some forms (buy-downs) can be efficiently controlled. On the other hand, a hazard of interest rate subsidies is that future commitments are usually not budgeted, lifetime subsidy volume can become excessive, and liabilities may explode. Additionally, fixed-rate lending without hedging may mean high interest rate risk. Special savings-loan circuits can be mandatory or voluntary. Under mandatory schemes (Brazil, Indonesia, Mexico, Philippines, and China) members receive low interest rates. Slovakia, Hungary, Czech Republic, and Tunisia have created voluntary contractual savings plans for housing in which participants are incentivized with a savings subsidy. They are simple to understand and a cheap subsidy source, but if weakly regulated they may create a lottery which discourages savings. Voluntary contractual savings plans are often highly subsidized. Finally, interest tax deductions are common in the United States, India, Morocco and Algeria. In these countries, households can deduct the interest paid on their mortgage from their income tax. These deductions are also simple to understand, but it is clearly biased toward homeownership. The fiscal costs of interest tax deductions are typically large and highly regressive, depending on formality levels, tax rates, and limits.

In 2000, Jordan replaced implicit interest rate subsidies provided by the government housing bank with a budgeted interest subsidy scheme. The program provides a 5% reduction from the market rate set by a private lender that is applicable for the entire term of the loan. In regard to public accounting, the full present value of future payments is budgeted as subsidy. Returns of a special fund endowed with privatization proceeds funds the program, which implies a need for rationing because there are a fixed number of subsidies per year. The program targets households using a transparent point system for eligibility with binding limitations on income and house prices. The program serves government employees only.

Credit subsidies lessons for Egypt. The ‘simple’ solution, e.g. public fixed-rate loan with low interest rates, may be risky and cause market distortions. Budgeted interest buy down of market-rate financing makes subsidy explicit and involves the private sector. A loan lifetime subsidy is wasteful, especially in a declining interest rate environment where borrowers can refinance. It is more efficient to focus subsidies on helping to overcome affordability constraints in the first years of the financing.

Supply-side ownership subsidies are the most common type of housing subsidies worldwide. Supply-side subsides directed at households can include “standard” housing, core and self-build housing, sites and services, and lease-to-buy programs. Supply-side subsidies targeted at housing producers include construction subsidies, construction loan subsidies, construction loan guarantees, exemption from VAT/local taxes, and lower rates. Currently, these programs usually involve both the government and the private sector, but need to determine roles and risk sharing. Programs for titling, tenure security, and property rights are important elements. Supply-side subsidies are useful when the private sector supply is not responsive, including inputs of land, infrastructure, and materials. They are easier to administer than down payment subsidies. Location specific subsidies can benefit community development. Good programs can develop private sector capacity and public/private risk sharing frameworks. Finally, they are politically convenient because they provide visible results. However, a disadvantage is that too often inefficient public developers dominate these programs. Overall, they are less efficient, as subsidies may be captured in developer margins. Poorly located housing can lead to underutilization, lack of job opportunities and services, high transport costs, and pockets of poverty. Full costs are not transparent because the opportunity cost of land and infrastructure are not recorded. It may be hard to privatize infrastructure delivery.

South Africa housing subsidies had to address a rather a unique situation. In 1994, there was a political imperative for massive housing supply to be delivered as fast as possible. South Africa tried to implement a down payment subsidy program, but it failed because of the unwillingness of banks to provide loans to the poor and township residents. Thus, a supply program was implemented, but it lacked both bank loans and a household savings component. Developers delivered 2.2 million units as of September 2006, but there have been major problems. For example, poor and distant locations have adversely affected employment opportunities. Additionally, because households had no equity in their homes, they abandoned units to seek employment. A major policy revision began in 2004, and now programs include mandatory savings, improved locations, and support to micro-finance for housing for upgrading of core housing, and a higher income eligibility requirement. There is also an increased focus on rental housing, densification (high-rise), leasing to buy, and major efforts to reach an accord on risk sharing between the Government and the banks. Analysis has led to corrective actions and policy changes. Among corrective measures, key lessons are that targeting proper locations is vital and a risk-sharing framework must be developed to help banks to lend to the poor. Similar to Chile, South Africa’s analysis of program results led to corrective actions and policy changes. The quantity of housing produced is still a priority, but location issues loomed as important, and the program moved to focus on better human settlements. The previous 100% give-away has now added household savings. Government and banks are still working on their accord, but banks have now set lending targets ($7 billion by 2008). Still, micro-finance for housing is also needed for upgrading and expansion. A new rental subsidy adds flexibility, but South Africa faces implementation problems in social rental housing.

Indonesia, Thailand, Morocco, Tunisia, India and Brazil offer good examples of slum upgrading approaches. Upgrading programs can target the poor and specific locations, and provides labor force for formal and informal sectors. Best practices in upgrading join public subsidies with private developers and lenders, include cross-subsidization and mixed-use elements, and involve community-focused NGOs in the implementation process. Additionally, successful programs require household savings, offer micro-finance for housing, and facilitate in-situ or nearby relocation. Governments are recognizing that providing 'standard' housing for all citizens is not affordable, so there has been an increasing shift towards core and self-built housing solutions. A pilot project in Mumbai, India provided in-situ upgrading had cross-subsidization, included a private bank construction loan/partial donor guarantee, and NGO/CBO participation. In Morocco, a recent pilot project brought in private banks offering mortgages and micro-finance for housing. In Brazil, municipalities adopt comprehensive plans to integrate slums into city fabric. The Kampung Improvement Program (KIP) in Indonesia was managed by local government, and included community involvement and private micro-finance. Egypt is fortunate to have dynamic informal areas and a lesser slum problem than elsewhere, but informal areas could still benefit from up-front planning and infrastructure provision, access to finance (including micro-finance for housing), tenure security, and titling and registration (which provides incentives for housing improvement). Additionally, slum-upgrading efforts would benefit from the legalization of mixed-use development, which could help support cross-subsidization.

Private rental needs a supportive investment environment (Morocco, Russia, Latvia, South Africa, and Colombia). A key advantage of rental housing is that it provides affordable housing to poorer households and supports mobility and labor market flexibility for the young. Legal issues affecting the vitality of a private rental market include rent decontrol, rent setting and adjustment rules, and contract enforcement options/rental mediation. A tax system that permits full capital expenses and maintenance cost deductions rather than taxing gross rents will catalyze rental market investment.

Financial sector subsidies. Financial sector subsidies, internationally, are used to respond to one of four specific problems, including: (i) regulating the allocation of credit, (ii) permanent subsidies/regulatory incentives, (iii) risk-sharing between private lenders and government, and (iv) subsidies targeted to cost elements of lending. Examples of systems to regulate the allocation of credit include institutional investors in India, China, and the Philippines to buy bonds and depositories in Brazil to originate and hold mortgage loans. Regulating the allocation of credit may have the advantage of helping to kick-start a mortgage market (India), but there is a risk of degeneration (Brazil). 'Social contracts' with bottom-up savings banks, cooperative banks and micro-finance (Spain, Peru) are examples of permanent subsidies. An example of a regulatory incentive to help meet the credit needs of all income segments is the Community Reinvestment Act (CRA) in the United States. The CRA and its implementing regulations require federal financial institution regulators to assess the record of each bank and thrift in helping to fulfill their obligations to the community and to consider that record in evaluating applications for charters or for approval of bank mergers, acquisitions, and branch openings. A social contract/commitment may work if local lenders exist, and mandate performance is controlled. However, if there are no local lenders, it may fail. Additionally, it may be costly (no performance review), and commitment insufficient if credit risk is high (South Africa). Risk sharing between private lenders and government can occur as joint ventures (Bangladesh, India, Pakistan) and public-private risk-sharing mechanisms (Morocco and Mexico). Risk-sharing can enhance private sector risk-taking and develop new market segments, but may lead to high fiscal costs if downside risk is not contained – private sector risk is minimal. Chile has a subsidy program targeted to the cost elements of lending in the form of a small loan origination cost subsidy. Cost subsidies increase administrative capacity with lenders, but must be sunsetted to avoid the risk of excessive administration costs.

FOGARIM: Morocco's Low-Income Loan Guarantor for Informally Employed Households. In 2004 the Government of Morocco initiated a comprehensive reform program in an attempt to address both the supply and demand side of the housing sector. The new strategy is based on the willingness to let the private sector play the lead role in housing supply, to improve the institutional and regulatory environment of the housing sector, and to increase affordability of housing to low-income households via better targeting and market-driven interventions. As part of the reforms, a mortgage guarantee fund

(FOGARIM) was established for households with irregular or informal sources of income. This guarantee fund, targeting households employed in the informal sector, has been very successful at attracting borrowers. Approximately 15,000 mortgage transactions have taken place, and there is currently MDH 2.11 billion in guaranteed loans outstanding. Its success can be attributed to the fact that it is responding to a market niche with great demand, but also that it had a strong experience base from which to build. At the time of its inception, Moroccan banks had already acquired solid experience with upper income mortgage transaction, and were looking to expand their market. FOGARIM provides access to otherwise unqualified homebuyers by assuming 70% of the credit risk of the mortgage from the lending banks. There are currently four banks using the program, including CIH. The program allows up to a 100% loan-to-value ratio with a capped purchase price of MDH 200,000. Since its inception, average loans have been around MDH 168,000 each. Most borrowers tend not be not poor, they just work in the informal sector. Indeed, less than 10% of the outstanding loans are at the MDH 100,000 level (slum dwellers).

Mexico's Housing Finance Agency SHF. SHF was created in 2001 to catalyze the development of a secondary mortgage market in Mexico by guaranteeing credits and creating a central database on borrowers, loans and mortgage-backed securitizations. SHF serves as a financial guarantor for securitizations/bond issues in lower middle-income (government backing phases out by 2013). Additionally, it guarantees risky finance company construction loans (SOFOL). As a mortgage loan insurer and swap provider for lenders (min. wage vs. consumer prices), SHF helps to protect consumers against payment shock. SHF introduced a credit scoring mechanism and consumer information on market loan offers. Finally, SHF co-develops the legal-regulatory framework for mortgage lending. Key advantages of establishing an agency like the SHF is that it is a flexible approach that addresses developer finance. A constraint is that it only serves the lower-middle income market, rather than the low-income market.

Financial sector subsidies lessons for Egypt. Partnerships with the private sector should be explicit, with clear program design and contracts. Subsidies should be focused to address specific cost or risk issues. Private sector should take some of the credit/collection risk (not only lenders, also developers). Programs should attempt to reach out to lower-income, informal groups rather than serving those who already have access to finance (developer or bank). Program and mandate performance should be regularly reviewed.

2.2 Rent Decontrol Policies

International experience suggests several lessons for reforming Egypt's rent control system. First, residential and non-residential rent controlled stock should be treated differently. Second, rent adjustments should be introduced gradually to converge toward market rents (sometimes in a two-step approach of rapidly covering operating cost at first followed by quid-pro-quo rent adjustments against landlord investments). Third, a subsequent indexation of rent increases in implemented. Finally, effective and efficient dispute resolution/mediation mechanisms are established. Spain's case has several interesting lessons for Egypt including an option for accelerated de-grandfathering. In effect, tenants of pre-1964 rent-controlled units who choose to subrogate their right to bequeath the contract (called mortis-causa) are entitled to retain a low rent level for the life of the contract. Additionally, unfavorable tax treatment for rental investors appears to be an additional constraint to investment in the rental market in Egypt. What is clearly needed is a study to better understand the characteristics of rent-controlled units, their tenants, and their uses in order to inform policies aiming to accelerate rent decontrol in an effective and politically feasible way.

Recent rental reforms in Morocco encompass the entire rental stock (no grandfathering), rationalize the inheritance of rental contracts using the Spanish approach (if the tenant opts to bequeath contract, a rent rise must be accepted), and indexed rent increases. A mandatory mediation step is required prior to court intervention. Russia, Latvia, East Germany and Poland are starting rental market reforms. In the first phase, existing contracts are swiftly moved to operating cost coverage (including repairs and capital return). Rent allowances are used to support tenants with excess burdens. In the second phase, there are further rent adjustments based on landlord investments (East Germany). In a third phase, a reference rate system is established (East Germany).

2.3 Rental Sector Programs

Private rental needs a supportive investment environment (Morocco, Russia, Latvia, South Africa, and Colombia). A key advantage of rental housing is that it provides affordable housing to poorer households and supports mobility and labor market flexibility for the young. Legal issues affecting the vitality of a private rental market include rent decontrol, rent setting and adjustment rules, and contract enforcement options/rental mediation. A tax system that permits full capital expenses and maintenance cost deductions rather than taxing gross rents will catalyze rental market investment.

Investors in public or non-profit housing may include public agencies, local governments or housing associations. In some cases public-private partnership schemes share risk between public and private actors, like collection risk from social tenants (Poland proposals). There are also cases of non-profit investors (Poland TBS scheme). Public rental is a complex and risky subsidy strategy. It requires public investment support (land and infrastructure, land-to-housing swaps), rental allowances for poor tenants, and rent differentiation by income. Additionally, a long-term funding strategy needs to be put in place. An example is the two-tier model of central government funding agency and local government rental associations in Finland and the United Kingdom). Legal goals ('right to housing') may create fiscal risk. This approach is mostly pursued in transition countries, where there is a special historical legacy of large rental stock and dense cities.

2.4 Comprehensive Housing Reform: Morocco

Population Growth. Morocco, with a population of 30 million and an urban population increase of about 3-4% annually, has suffered from a housing deficit of as much as 50,000 units per year. The number of urban primary dwellings was estimated at around 3 million in 2000. 62% of households own their dwellings, 28% are renters, and 10% have other tenure status. The formal housing stock represents 80% of the total.

Housing Stock Condition. It is estimated that about one-third of the urban population lives in sub standard housing. This consists of: (i) Housing units illegally built but of appropriate building quality (540,000 households); (ii) Slum dwellings of very poor quality sited on un-serviced land, (270,000 households, of which 212,000 live in urban areas); and (iii) Units threatening collapse, mostly concentrated in historic urban cores (90,000 households). During the past 20 years, informal housing has developed at a faster pace than formal housing, and slums have increased at a rate of 4% per year.

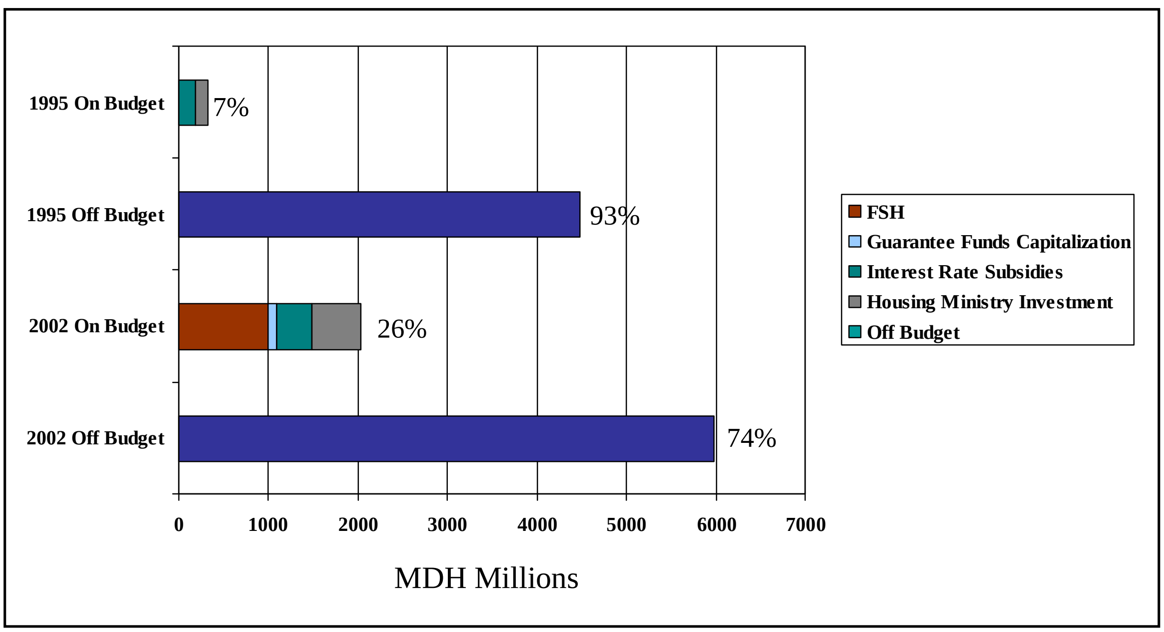
Tenure. Rental housing represents 28% of the housing stock. 73% percent of rental units are self-constructed, and consist of rooms or floors let to tenants by homeowners. 90% of landlords are households who directly manage the relationships with tenants, often with direct, non-written arrangements. The current legal framework applying to the rental sector has constrained the market because of the perceived imbalances in favor of tenants. A draft rental market reform law is currently under review by the Minister of Housing, which aims to address issues for the entire rental housing stock.

Housing Finance. The home mortgage market accelerated starting in 1999 when interest rate subsidies provided by CIH (state-owned housing bank) were extended to other public and private banks – outstanding mortgages increased from 3% of GDP in mid 1990s to 7% in 2004, mortgage interest rates fell from 12.5% in 1995 to about 8% in 2004, and loan-to-value ratios increased from 70% to 90%. However, access to housing credit is limited by the lack of financial services and limited outreach of the banking system to low-income groups. Until 2004, mortgages were typically available only to households with regular (public or private sector) salaries. Significantly, 40% of the labor force is employed in the informal sector, and hence were not. The recent introduction of a mortgage guarantee fund focused on household employed in the informal sector has helped to extend housing finance to the previously underserved portion of the population.

Affordability. Formal houses built by developers are priced out of the reach of low-income households. As a result, it is estimated that more than 50% of new construction is self-construction (formal and informal). Moroccan households typically construct their homes one floor at a time, and generally without recourse to formal housing finance.

Subsidies. Subsidies to the housing sector are a drain on Morocco's budget, growing from about 1.5% of GDP in 1995 to 2.6% in 2002. Most subsidies to the sector are in tax incentives to developers and households. Other important subsidies include: a) public land for social housing programs; b) the investment budget of the Ministry of Housing and Urban Planning; and c) interest rate subsidies on mortgages. Hidden, or off-budget, subsidies mask the total State expenditure (see Figure). Indeed, only 7% of the housing subsidies were on-budget in 1995, growing to 26% by 2002.

Figure 18: Morocco 1995 and 2002 – On-Budget and Off-Budget Subsidies



Source: Based on MFP and MHU data for 1995 and 2002

Targeting. The allocation of subsidized public land has not exclusively benefited low-income groups. In 1998, it was estimated that only 24% of land subsidies benefited households in the three lowest deciles of the income distribution, in the form of serviced land parcels. Interest rate subsidies on mortgages were not well targeted and *de facto* excluded households from the informal sector, usually the lower segment of the income distribution.

Institutional Setting. The responsibility for housing policies and low-income housing programs is shared by the Ministry of Housing and Urban Planning (MHU) and the Ministry of Finance and Privatization (MFP). The MHU is in charge of the definition and oversight of the social housing programs. The MFP is responsible for direct housing subsidies, tax policies relevant to the sector, and the management of housing finance instruments. Under the oversight of the MHU and the MFP, a group of parastatal companies (OPH) is in charge of land servicing and implementation of the social housing programs of the MHU. In the past, housing policies and programs have suffered from insufficient coordination between and within ministries. Policy instruments were developed independently by institutions in charge of different parts of the system, and the oversight of public programs was insufficient.

Land Management. Land titling is regulated by a legislation that ignores customary registers, and establishes ownership rights through a complicated system of land surveys and public hearings. This time-consuming formal land registration process encourages the creation of more informal settlements. Urban planning and zoning practices are governed by several laws, decrees and ministerial instructions which lack coherence and impose heavy urban development costs. Planning and construction regulations impose high land reserves and infrastructure standards. Regulations for social housing developments impose costly building standards. Building permits are expensive, time consuming to obtain, and subordinated to the possession of official title deeds. The economic consequences are a reduced formal market for urban land, high land development cost and land prices, and long delays between project design and delivery of housing units.

New Strategy. In 2004 the Government of Morocco initiated a comprehensive reform program in an attempt to address both the supply and demand side of the housing sector. The new strategy is based on the willingness to let the private sector play the lead role in housing supply, to improve the institutional and regulatory environment of the housing sector, and to increase affordability of housing to low-income households via better targeting and market-driven interventions. The Government goal is to produce 100,000 social housing units and serviced land plots annually.

Objectives. The Government's primary objectives in the housing sector are: (i) To strengthen the institutional, regulatory and fiscal environment of the housing market to provide incentives for market-based solutions for the country's housing sector, and; (ii) To increase the access of low-income and severely disadvantaged households to affordable and higher quality housing.

Approach. The Government is taking an integrated approach to addressing the housing sector issues, which includes three strategic reform areas:

1) Reforming the legal framework of urban planning to reduce the costs of serviced land and to promote orderly urban development, creating a legal and fiscal environment for the rental market, and reforming real estate taxation and housing subsidies;

2) Designing and implementing a new approach to social housing involving a nationwide program of slum upgrading and development of low-cost serviced or semi-serviced plots;

3) Improving access to housing finance for low-income groups, especially households with irregular or informal incomes.

Table 13: Main housing sector policy reform actions taken by the Government of Morocco

POLICY AREAS	OBJECTIVES	REFORM ACTIONS/ OUTCOMES	STATUS
Housing Subsidies and Finance	• Rationalize housing subsidies • Improve targeting of subsidies • Increase access to housing finance for low income and households employed in the informal sector	• Termination of interest rate subsidies • Introduce targeted subsidies (VSB and FOGARIM) • Solid experience with upper income mortgage market • FOGARIM (informal sector) • FOGALOGE Public (civil servants) • FOGALOGE Prive (formal, private sector) • Micro-finance institutions (MFI) to lend for housing • Contractual savings program	Complete Complete Complete Complete Delayed Delayed Complete Delayed
Rental Housing	• Stimulate rental market • Increase vacant unit occupancy	• Draft rental law under review • Fiscal and financial reforms	In Progress Delayed
Urban Planning Standards and Regulations	• Establishing land development control mechanisms and simplification of approval processes	• Reduce delays in plan approvals process • Reduce land allocation standards for public facilities • Adapted construction standards on social housing • Unified urban planning code	In Progress Complete Complete In Progress
Institutional Setting	• Increase private sector participation in land and housing developments • Restructure institutional framework	• Creation of HAO • Parastatals merged and transformed into economic authorities • Recapitalization of 4 regional OPH in debt • Reimbursement of the OPH debt to the CIH	Complete Complete Complete Complete
Urban slum upgrading	• Improve living conditions for 212,000 households • Prevent the establishment of new informal settlements	• Endow FSH with substantial long-term resources • Flagship slum upgrading program *VSB → 2010* • Release large tracts of public land for residential development and slum upgrading and prevention	Complete Sat. Progress Sat. Progress

Housing Finance Reforms. The objective of the housing finance reform is to increase access to financing for low-income households. The reform consists of three main components: (a) establishment of mortgage guarantee funds, (b) extension of micro-finance services to housing; and (c) establishment of contractual savings schemes for housing.

The GOM created three mortgage guarantee funds: (i) FOGALOGE Public for public sector employees; (ii) FOGALOGE Prive for formal sector employees; and (iii) FOGARIM for households with irregular or informal sources of income.

Only one of mortgage guarantee funds has been capitalized and implemented to date – FOGARIM. This guarantee fund, targeting households employed in the informal sector, has been very successful at attracting borrowers. Approximately 15,000 mortgage transactions have taken place, and there is currently MDH 2.11 billion in guaranteed loans outstanding. Its success can be attributed to the fact that it is responding to a market niche with great demand, but also that it had a strong experience base from which to build. At the time of its inception, Moroccan banks had already acquired solid experience with upper income mortgage transaction, and were looking to expand their market.

FOGARIM provides access to otherwise unqualified homebuyers by assuming 70% of the credit risk of the mortgage from the lending banks. There are currently four banks using the program, including CIH. The program allows up to a 100% loan-to-value ratio with a capped purchase price of MDH 200,000. Since its inception, average loans have been around MDH 168,000 each. Most borrowers tend not be not poor, they just work in the informal sector. Indeed, less than 10% of the outstanding loans are at the MDH 100,000 level (slum dwellers).

As part of the 2004 set of housing finance reforms, micro-finance institutions were authorized to lend money for housing. The intent was to open access to capital to very low-income households. The initial ceiling on loans was MDH 35,000; this was recently increased to MDH 50,000. Given the size of the loans, however, they are most appropriate for housing improvements, not housing purchases.

The final component of the housing finance reforms was the establishment of a contractual savings plan in which clients regularly deposit an agreed amount for a set period of time. At the end of the period the client withdraws the funds, and uses it towards the purchase of a home. In some cases, contractual savings plans are accompanied by a grant from a Government agency that serves as an incentive for saving. Currently, this component of the reform has not moved forward.

Urban Planning Standards and Regulations. The goal of this reform is to simplify current urban planning regulations in order to increase the efficiency of land utilization and hence reduce the cost of legally developed land. To this end, in 2004 the Government initiated major reforms in three areas: a) strengthening control of land development and reducing delays in the approval and processing of urban planning documents; b) reducing land allocation standards for public facilities, and c) lowering construction standards for social housing units. The MHU estimates efficiency gains of about 25 percent on land-use ratios and construction costs from the new framework.

Currently, a unified and modern urban planning code is underdevelopment, and expected to be enacted sometime in 2007. Approval of plans is being decentralized, and some operational regulatory instruments (local area plans, overlay plans, and conservation plans) have been introduced.

Gains have also been made in streamlining the plan approval and land titling process. For example, the titling of large tracts of subdivided land is now being permitted at the subdivision level, rather than each purchaser applying for title individually. Overall, blockages are being removed, which is having a strong preventative effect on informal settlements.

Institutional Reform. Recognizing that their management and organizational structure were inadequate to support the new program for social housing, the Government restructured the OPH (public housing operators). A new structure, Holding Al Omrane (HAO), was established in 2004 to absorb the existing OPH, eliminate redundancies and overlaps among their missions, mandates and territorial coverage, consolidate their financial and human resources, and eliminate the outstanding deficits. The mandate of Holding Al Omrane is to: a) increase the supply of serviced land for social housing and new residential developments; b) promote partnerships with the private sector for the provision of low-cost housing and upgrade of sub-standard housing; and c) implement Government programs for slum upgrading in partnership with local governments and the private sector.

Financial and institutional restructuring of the remaining seven regional ERAC (regional agencies for land development and construction) is being studied in terms of their regional coverage and of their adaptation to the new mandate, limited to the provision of on-site infrastructure and the implementation of the social housing programs. The integration of the ERAC into HAO will be the final phase of the restructuring of the parastatal companies, and GOM has recently approved the creation of two additional shareholding entities to expand the regional coverage of HAO. The reform will include implementation of an adequate governance and oversight structure, along with the upgrading of accounting systems of the OPH, improvement of commercial practices and a new staffing strategy.

An indicator of the significant impact of the new institutional focus on private sector participation in housing development is that in 2005 and 2006 annual housing supply was greater than housing demand.

Two-Part Program. In 2003, the Government introduced a new strategy to provide low-income groups with housing accommodation. It is a two-pronged approached composed of:

1. A nationwide program called *Villes sans Bidonvilles* (VSB) to upgrade all existing urban slums (originally to include only the 212,000 urban slum households; later expanded to all 270,000 slum households) by 2010; and

2. A prevention policy, aimed at increasing the supply of low-cost serviced or semi-serviced plots by the OPH by opening up large new residential areas in partnership with private developers, to be entrusted with the construction of housing units.

Multi-Agency Contracts. The VSB program is a city-wide approach to slum upgrading. All slums in a given urban area are included in an upgrading program, agreed to between the MHU, the deconcentrated regional authorities of Governorates, the Local Authorities or Municipalities, and the parastatal companies in charge of its implementation. These agreements are defined by "city contracts" among the parties. While remaining a program of the MHU, the VSB is presented as a partnership with all the major stakeholders, most notably the local and regional authorities, the public and private sector housing developers, as well as the slum inhabitants. The program's Operating Manual lays out the rules for this implementation approach and defines which responsibilities are to be covered by the different parties involved. On a city-by-city basis, contractual agreements clarify and document the responsibilities of the different public actors on national and local levels.

Serviced Land. Slum and sub-standard housing prevention is based on facilitating the delivery of low-cost serviced or semi-serviced land plots to low-income groups. Large new areas called *"zones d'urbanization nouvelle"* (ZUN) will be opened up for residential development. Contrary to past practices, the OPH will only be in charge of land development, including off-site and on-site infrastructure, which will then be sold to developers on a competitive basis to build housing units for low-income groups, or directly for individuals.

Basic Principles. The basic principles of the strategy include: a) the integration of single operation at a city-wide level; b) contractual engagements of private and public actors in the slum eradication efforts; c) increased provision of social housing by private developers; and d) the involvement of the slum population through a process of social support and participation.

Quantity Targets. The VSB program sets ambitious targets for the Government, as it is expected to be fully implemented by 2010. It encompasses all slum upgrading projects that were on-going before 2004, covering about 68,000 households. By March 2005, 24 slum-upgrading city contracts had been finalized for another 103,000 households. The city contracts are followed by agreements with the OPH for the implementation of the projects.

Table 14: Number of households by type of intervention in the VSB program

	In-site upgrading	Fully serviced lots	Semi-serviced lots	Fully finished housing units	Sub-Total
Commenced before 2004	16,834	34,930	1,306	15,211	68,290
Engaged in 2004	20,873	26,555	1,584	13,148	62,460
After 2004	24,792	12,553	28,757	15,768	81,870
TOTAL	62,508	74,038	31,647	44,127	212,320
	29 %	35 %	15 %	21 %	100 %

Source: MHU, Programme VSB, Orientations stratégiques et programmation, September 2004

Land Contribution. The amount of land needed to implement the program is estimated at about 5,200 ha by the MHU. To ease the land constraint, the Government has implemented two massive transfers of publicly owned land to the MHU. Of the 70 cities covered by the program, 35 are concerned by the transfers of lands from the public domain, out of which 19 show public land availability in excess of the slum eradication needs, and 16 show an allocation sufficient for half of the program needs. However, "city contracts" are signed only when all land needs for the program have been met. If public land is insufficient, local governments contribute their own land reserves and in some cases private land is acquired.

Budget and Financing. About MAD 17 billion is needed to implement the VSB program. The State will provide around 30% of the financial needs, while the rest will be contributed by the beneficiaries themselves. In general the Ministry of Housing and Urban Planning will be the only public contributor to the program, while the municipalities may contribute land, if available, and also have to commit to preventing the formation of new slums in their jurisdiction.

Table 15: Costs, financing and subsidies in the VSB program

	Number of Households	Area of urban land needed (ha)	Cost (million MAD)	Subsidy (million MAD)
Commenced before 2004	28,290	1,663	6,537	1,818
Engaged in 2004	62,160	1,411	4,882	1,564
After 2004	81,870	2,106	5,700	2,035
TOTAL	**212,320**	**5,180**	**17,119**	**5,417**

Source: MHU, Programme VSB, Orientations stratégiques et programmation, September 2004

The Housing Solidarity Fund (FSH) is a dedicated fund directly assigned to the MHU to finance social housing programs. The Fund is replenished from a dedicated 2% tax on cement. Given current cement sales, the tax is expected to generate over MAD 1 billion per year. The FSH fund is managed by Ministry of Housing with oversight by the Ministry of Finance, and is also used to support FOGARIM and upgrading of historic areas where there is residential use.

Table 16: FSH and BGE projected expenditures for social housing programs 2005 -2010

(in MAD million)	2005	2006	2007	2008	2009	2010	TOTAL
REVENUES	**1,520**	**1,456**	**1,496**	**1,536**	**1,636**	**1,736**	**9,380**
Housing Solidarity Fund (FSH)	1,184	1,120	1,160	1,200	1,300	1,400	7,364
Budget transfers	336	336	336	336	336	336	2,016
EXPENDITURES	**1,520**	**1,456**	**1,496**	**1,536**	**1,636**	**1,736**	**9,380**
Villes sans bidonvilles	818	744	1030	1080	620	420	4,712
Other housing programs	702	712	466	456	1016	1316	4668

Source: Ministry of Finance and Privatization, May 2005

Implementation. The Government has taken steps to expedite the implementation of the program by mobilizing stable and substantial resources by: a) increasing the resources of the Housing Solidarity Fund (FSH); b) mobilizing large tracts of public land located around major cities, a significant part of which will be transferred to VSB, and; c) restructuring of the parastatal companies to improve their performance while relying on the private sector for the construction of low-cost housing units.

Institutional Reform. A division was established within the Department of Social Housing of the MHU with the mandate of overseeing the signing and administrative processing of operational MoUs with public and private operators, to carry out monitoring and evaluation functions for the program, and to manage an information system for tracking informal housing in Morocco. It has 5 staff members.