The Critical Importance of Housing Finance in Solving Persistent Housing Problems

World Bank GSUURRR Knowledge Forum

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The Scale of the Problem and the Opportunity
The Challenge
How to Build a Billion New Houses
By 2025?

• >50 million new urban dwellers each year
• Grossly inadequate stock
• Rising housing demand with rising incomes
One Third of Urban Population in Slums Number is Growing!

Proportion of Urban Population Living in Slums

<table>
<thead>
<tr>
<th>Region</th>
<th>Population Living in Slums (% Urban Population)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Northern Africa</td>
<td>10%</td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>60%</td>
</tr>
<tr>
<td>Latin America and the Caribbean</td>
<td>20%</td>
</tr>
<tr>
<td>Eastern Asia</td>
<td>30%</td>
</tr>
<tr>
<td>Southern Asia</td>
<td>40%</td>
</tr>
<tr>
<td>South-Eastern Asia</td>
<td>25%</td>
</tr>
<tr>
<td>Western Asia</td>
<td>15%</td>
</tr>
<tr>
<td>Oceania</td>
<td>10%</td>
</tr>
</tbody>
</table>

Total Developing Regions (32.7%)

Source: UN Habitat Global Urban Indicators 2010
Virtually All Population Growth until 2050 Will Happen in Emerging Market & Developing Countries


SOURCE: PRB, 2011
Think About Impact on Scale and Type of Real Estate Development

Young and Growing ↔ Aging and Stable

By the numbers

43% Population <15, sub-Saharan Africa
3% Population 65+, sub-Saharan Africa
16% Population <15, Europe
16% Population 65+, Europe

SOURCE: UNPD, 2011
Urban Growth Fastest in Least Urbanized Countries, African and Asia

Urban Population as % of Total Population (2015)

Source: www.hofinet.org
Asia and Africa Face the Biggest Urban Housing Challenge

Between 2010 and 2025, Asia alone will add 700 million people to cities

Global urbanization – 2010 vs. 2025

Billions of Residents

<table>
<thead>
<tr>
<th>Region</th>
<th>2010</th>
<th>2025</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asia</td>
<td>1.86</td>
<td>2.56</td>
</tr>
<tr>
<td>Africa</td>
<td>0.39</td>
<td>0.66</td>
</tr>
<tr>
<td>South America</td>
<td>0.47</td>
<td>0.57</td>
</tr>
<tr>
<td>Europe</td>
<td>0.54</td>
<td>0.56</td>
</tr>
<tr>
<td>North America</td>
<td>0.28</td>
<td>0.33</td>
</tr>
<tr>
<td>Oceania</td>
<td>0.03</td>
<td>0.03</td>
</tr>
</tbody>
</table>

Level of Urbanization

- Asia: 45% 54%
- Africa: 38% 45%
- South America: 78% 82%
- Europe: 73% 76%
- North America: 81% 83%
- Oceania: 71% 71%

Note: Urban vs. rural defined according to the criteria used by each area or country
Source: UN Department of Economic and Social Affairs – Population Division

Challenge: Urbanization Happens at Lower Per Capita Income Levels then in the Past
(GDP per Capita < USD 5,000)

From: Glaeser, E. A World of Cities, NBER 2013
Challenge: Investment in Housing is Lagging Behind Urbanization (Dasgupta et al)

- Housing Investment takes off at GDP per capita levels of $3000 (PPP constant dollars)
- And tapers off at $36,000 GDP per capita
- Investment generally follows growth in urbanization with some lag
- In Asia and Sub-Saharan Africa investment in urban housing lags demand (GDP/cap increase) by many years!
- Messy urbanization process
What Can Be Done To Break the Cycle of Informal => Upgrading

• Expand private housing production for lower-middle and middle income households, e.g. teachers, nurses, clerical staff, traders
• This group can pay for ownership if access to long/med term loan is available
• Can pay for formal rental
• Frees up govt. funds for housing programs for lowest income groups, e.g., upgrading, core housing + subletting, rental PPPs
Why is Housing Finance So Critical in Solving the Housing Problem?
It All Begins with Finance!

Incremental housing cannot reach required scale (or density) in rapidly urbanizing countries

Mortgage loans allow buying a house now and pay for it over a long time

Increasing affordability

Security of (lien on) property makes mortgage loans cheapest form of credit

Access to mortgages makes formal private sector mass housing production possible – for ownership or renting

Developers will not enter mid-market if clients cannot access mortgage loans to pay for the house upfront

Mortgage systems develop with growing GDP

But urbanization does not wait for this process to happen

Active policy support is needed
Scale of Mortgage Sector is Small in EM and Developing Countries

Mortgage Loans Outstanding as a % of GDP (2015)

Source: www.hofinet.org
The Size of Mortgage Systems as % of GDP Increases with GDP, but with considerable noise.

Source: www.hofinet.org
Even in Countries with High Urbanization Level
One Reason for “Messy” Urbanization

Urban Population as % of Total vs. Mortgage Loans as % of GDP (2015)

- Latin America
- Sub-Saharan Africa

Source: www.hofinet.org
Outcomes: Big Formal Supply Gap in Broad Middle-Income Segment

<table>
<thead>
<tr>
<th>Mkt Segment</th>
<th>10th</th>
<th>20th</th>
<th>30th</th>
<th>40th</th>
<th>50th</th>
<th>60th</th>
<th>70th</th>
<th>80th</th>
<th>90th</th>
</tr>
</thead>
<tbody>
<tr>
<td>Formal Housing with Mortgage</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
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<tr>
<td>Formal Housing Subsidized loans</td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
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<tr>
<td>Social Programs Upgrading/New</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
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<tr>
<td>Substandard/Informal Housing</td>
<td></td>
<td></td>
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</tbody>
</table>

Recipients are only a small proportion of households in these categories
Focus HF Policy Measures on the Expansion of Mortgage Coverage to Urban Median Income

Covered by mortgage: formally empl. and creditworthy; informally empl; with mortgage-able house. Medium term, secured. May need lender and developer incentives and/or hh subsidies initially

Gradually expand access to mortgages to 50% of urban income distribution

Microloans for others; +supply-side subsidies?

Supply-side Subsidies blending upgrading, new LIH

If middle/low income households cannot be served by mortgage- and developer market, housing problem is near unsolvable

+ Pension backed loans
Installment loans
What’s Special about Housing Finance Systems?

• Social and Economic Factors
  o Big in personal budgets and personal balance sheets (assets/liabilities)
  o Housing is one of the biggest investment and consumption items in economy
  o Politically sensitive (key barometer of social welfare, often a channel for redistribution)
# Housing-related Entries in U.S. National Income Accounts – 2003 (pre-bubble)

<table>
<thead>
<tr>
<th>Category</th>
<th>$billion</th>
<th>% of GDP</th>
<th>$ per person</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Domestic Product</td>
<td>10988</td>
<td>100.0</td>
<td>37784</td>
</tr>
<tr>
<td>Consumption</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>durable goods</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>furniture and household equipment</td>
<td>334</td>
<td>3.0</td>
<td>1149</td>
</tr>
<tr>
<td>services</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>housing services</td>
<td>1199</td>
<td>10.9</td>
<td>4121</td>
</tr>
<tr>
<td>(rental amount,</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>imputed rental value of owner-</td>
<td></td>
<td></td>
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<tr>
<td>occupied housing)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>household operation</td>
<td>426</td>
<td>3.9</td>
<td>1465</td>
</tr>
<tr>
<td>(electricity, gas, other)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>residential</td>
<td>562</td>
<td>5.1</td>
<td>1934</td>
</tr>
<tr>
<td>structures</td>
<td>554</td>
<td>5.0</td>
<td>1906</td>
</tr>
<tr>
<td>single family</td>
<td>302</td>
<td>2.8</td>
<td>1039</td>
</tr>
<tr>
<td>multi-family</td>
<td>34</td>
<td>0.3</td>
<td>118</td>
</tr>
<tr>
<td>other</td>
<td>218</td>
<td>2.0</td>
<td>749</td>
</tr>
<tr>
<td>equipment</td>
<td>8</td>
<td>0.1</td>
<td>28</td>
</tr>
<tr>
<td>Total of housing related entries</td>
<td>2521</td>
<td>22.9</td>
<td>8669</td>
</tr>
</tbody>
</table>
Housing is a large proportion of total household assets/wealth in advanced economies.

Source: OECD and Reserve Bank of New Zealand; in Herring 2011
What’s Special about Housing Finance Systems (2)?

• Technical Factors
  o Affordability increases with length of term, so emphasis on long term lending
  • The alternative of relatively short installment sales or micro-credit limits affordability
  o Difficulties of consumers to bear financial risks, so want to shift these to other parties
  o Mass product (needs for simplicity and consumer protections)
Housing Finance Expands Both Demand and Supply

- Private developers need to off-load housing upon completion; will not build without end-user finance
  - If building for ownership; access to mass mortgages required for targeted income group
  - If building for rental; rental investor needs access to mortgage loan – often most difficult part of housing finance (not in this course)
- Plus: Developers require short term construction finance
Alternative Secured and Non-Secured Housing Finance Products Are Important to Expand Access to Improved Housing

• Alternative secured loans for housing ease legal requirements for registration of mortgage
• Micro-finance for housing does not require lien-based collateral
• Still require macro stability and competitive markets
• ...and regulatory system and legal infrastructure
• This workshop will cover different types of housing finance product
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Housing Finance Information Network
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