Strengthening the Capacity of the Housing Sector in Iraq

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Introduction

The UN Iraq Trust Fund has funded the Strengthening the Capacity of the Housing Sector in Iraq project and it seeks to build capacity among Iraqi central and local authorities to address the housing problems of the country.[1] Phase I of the project started in mid 2004 and is due to be completed in June 2006.

Should additional funding become available, Phase II needs to make an important contribution towards transforming the crude reality of Iraq's housing sector. The Iraqi government will be required to introduce good governance and adopt best practices releasing the necessary resources, from both the public and private sector, to rehabilitate the country's existing housing stock while developing an efficient market for housing and finance products for Iraqi households requiring housing solutions.

This paper explores how the private, public and non-profit sectors can collaborate with Iraqi authorities to enhance financing and construction of housing for all incomes with special consideration for middle and low-income urban poor. The following urges that the Iraqi Housing Fund should act as the driving force for institutional and policy reform in housing and finance, by channeling public resources, through private intermediaries, to offer mortgages and home-improvement loans.

Implementation should focus on a bottom-to-top approach by designing a series of urban pilot projects in planning, financing, and home construction with an eye to building institutional and human resource capacity. This approach should allow the government to continue operating while adopting a systematic approach to combating housing problems.

Background and general trends

While reconstruction challenges seem overwhelming, Iraq's biggest challenge is to return to the levels of economic prosperity and political stability that the majority of the population enjoyed in the late 1970s. However, the means through which such goals can be achieved need rethinking and reform.

Over the past 30 years, the Iraqi central government controlled all aspects of planning, administration, and delivery of services – including finance and development. Once the country reaches national unity and stabilization, Iraqis will likely want more participation in the decision-making processes as well as an increased access to the benefits of urbanization. They will seek a more efficient delivery of services—to include increased access to finance, wider opportunities for economic development and wider participation of all stakeholders. It makes sense that after years of a highly state-oriented and centrally commanded economy, Iraqis will move towards a market-driven and more socially responsible global economy.

Housing sector

The housing backlog in Iraq is estimated at 1.6 million units and is steadily increasing with the influx of returning refugees. With the population growing at a 2.7 percent a year, the shortages will continue to deteriorate unless there is a major expansion of the housing stock.

Demand Side

The housing backlog in Iraq is estimated at 1.6 million units and is steadily increasing with the influx of returning refugees. The Iraqi population is estimated at around 26 million. According to the 2004 Living Conditions Survey in Iraq (UNDP), the size of the Iraqi household ranges from 6.0 and 9.0 persons. The housing stock is estimated at between 2.8 to 3.5 million units. According to this UNDP survey, at least 10 percent of the nation's total dwellings are

[1] The United Nations Development Group (UNDG) Iraq Trust Fund is administered by the United Nations Development Programme on behalf of itself and Participating United Nations Organizations. This is the first time that the UN is administering a multi-donor reconstruction trust fund in a joint partnership with the World Bank. This is also the first time that the UNDG organizations, pursuant to the Secretary General's reform agenda, have adopted common planning, funding, coordinated implementation and reporting arrangements for such a large scale operation, which is referred to as the "UN Cluster approach". Most importantly, this arrangement assists key Iraqi ministries such as the Ministry of Planning and Development Cooperation to work with UNDG as one entity, facilitating coordinated, collaborative joint programming.

overcrowded – which means a deficit equivalent to more than 400,000 units. In addition, it is estimated that 63 percent of some 2.5 million dwellings are units that are totally or partially destroyed, or in poor condition with limited electricity, water and sewerage. More than 3,500 new units a year will be required to accommodate people who would otherwise have to stay in emergency shelter or move in with friends and relatives. With the population growing at a 2.7 percent a year, the shortages will continue to deteriorate unless there is a major expansion of the housing stock.

Supply Side: Housing finance

The Iraqi government continues to view housing as social service expenditure and not as an investment. This position needs revisiting. Housing is a key engine for economic growth, creating jobs, generating wealth and promoting individual investment. Housing and basic infrastructure are expected to emerge in Iraq as important investments (rather than just expenditure) leading to a greater role for the financial services sector, the building and construction sector and individual private investors.

A preliminary assessment of the financial service in Iraq reveals that both public and commercial banks have hardly extended credit to the corporate sector. Public and private banks rarely offer mortgages and only offer expensive short-term loans, which are beyond the means of moderate and low-income households.

It is necessary to engage both public and private financial institutions in home lending. The government should facilitate building capacity among formal finance institutions and help local community banks to operate in the mortgage market. Competition among providers will stimulate innovation and cost-saving, thus making loans more affordable to more customers. The beginning of the change in housing finance and housing delivery in Iraq should start with a solid partnership between the public and private sectors. For example, in a pilot-limited size intervention and relatively secure locations, HSBC as Dar Essalaam Investment Bank and Standard Chartered are currently operating in northern Iraq.

Currently there are three obstacles preventing the development of a dynamic housing finance market in Iraq. First, the housing market is hampered by limited capacity and inadequate production. Second, banks are not issuing enough long-term loans, thus preventing the growth of a secondary market. Third, the country's prudential and regulatory framework governing real estate transactions is underdeveloped, preventing private investment in the housing sector.

The first problem identifies the needs of the growing and more urbanized population. Access to adequate and affordable housing and inexpensive financing for those with moderate and low-incomes, can prevent the proliferation of slums and improve the quality of life of many Iraqis.

Resolving the second problem is less complicated, but still a challenging task. Iraq, an oil-rich country, requires long-term investment to develop a dynamic housing market. To boost retail long-term lending, commercial and specialized banks in Iraq will require additional funding. At least for a couple of years, a prudent increase in lending will not endanger or overexpose financial institutions to a dangerous imbalance in the assets to loans ratio. Mortgage capabilities need to be expanded among commercial banks as well as the development of affordable financing for the urban poor – steps that are vital for creating the primary mortgage market.

Iraq needs to channel as much of the investment and savings that arise from local economic activities into the housing sector. Savings reduce the need for additional credit to purchase a house. Governments should undertake policies to stimulate savings for housing (equity as opposed to debt finance) and provide intelligent subsidies that improve the housing solution for lower-income households within their domestic budget constraint; any gap in funding should target priority groups with demand-side subsidies designed to achieve social equity while enhancing market efficiency.

The ability to access long term funding through the issuance of mortgage securities can enhance the supply of funds and facilitate improved risk management by lenders. A targeted objective of the Iraqi Housing Fund should be to reduce the liquidity risk and provide together with the Central Bank the ultimate backstop for liquidity. A liquidity facility is a second floor finance institution that provides loans to lenders and funds itself through bond issuance.

The objective will be to design for Iraq an efficient liquid market that treats mortgages as commodities. Funding long-term assets will mean a larger, more stable and affordable pool of resources, a bigger investor base and more money for homeownership. It is necessary, however, first to build a robust primary market.

Finally, in order to attract private capital investment the third problem requires macroeconomic stability and an effective legal framework for property ownership, mortgage lending and real estate transactions. It also requires adequate laws, property title systems and judicial processes allowing households to establish ownership and pledge collateral. For investors, property rights registration recognizes that investment in the private corporate world has a sole objective: selling or transferring ownership to a buyer as an exchange for a return, be it social or economic.

The Iraqi Transitional Government in 2004 created the Iraqi Housing Fund (IHF) on the assumption that banks do not have sufficient capital to fund long-term mortgages and that the lack of a secondary market prevented retail banks from selling their loans and recovering their capital.

The Iraqi Housing Fund (IHF)

The purpose of the IHF is to provide financial resources to undertake housing programs. The Fund is intended to have a two phase development: First, providing resources needed to implement housing projects; reviewing housing projects and making recommendations to the Board of Trustees; introducing and sponsoring necessary legislative reforms and new regulations in the housing and housing finance sector; partnering with the private sector to develop implementation capacity among other stakeholders different to the government; and building and strengthening the institutional capacity of the Ministry of Construction and Housing, other ministries and local authorities to coordinate, supervise, evaluate and fund the projects. The second phase of development sees IHF as a liquidity facility, issuing bonds.

Order (11) for 2004 Housing Fund commits the IHF to support private banks and private construction companies. During most of 2005, with little administrative capacity and logistics, the IHF continued to make direct retail efforts to public officials for building a house in individually owned plots of land. The IHF needs to reform its bylaws to allow the establishment of a more flexible, executive and mandate-driven institution, capable of designing resource mobilization strategies. Such strategies would include voluntary and compulsory saving schemes, and government issued securities and bonds fully engaging the private and public banking sectors.

Response Strategy: Agreements between the Ministry of Construction and Housing (MoCH) and UN-HABITAT

For housing to fulfil its potential in social and economic development, it is important that the Iraqi Government makes housing a priority. Iraq's housing policy requires a deliberate and embracing strategy to assess the market; adopt long term planning and growth management; mobilize private capital for mortgage financing and; engage the private sector and community based organizations to improve delivery of housing and infrastructure.

UN-HABITAT under the Iraqi-Trust Fund and within the project to strengthen the capacity of the housing sector in Iraq in response to a clear demand from the Ministry of Construction and Housing (MoCH) to prepare an action and implementation plan, focuses on a number of pilot urban projects covering four strategies below:

1. Increase land availability and manage urban growth

Planning. The reconstruction in the housing sector will be tied closely to policy decisions regarding decentralization, land management, planning and popular participation. Iraq requires a stronger regional planning strategy that views affordable housing as a foundation for community growth, and requires local authorities to explicitly assess their housing needs. An institutional framework has to be created with residents, advocates, community groups, and local planners meeting and discussing needs.

Like others countries around the world, Iraq will require municipalities and governorates to adopt housing elements in their mandatory general and strategic plans. Among other things, each local authority must develop plans and programs, and identify sites, to accommodate a "fair share" of its region's new growth for all kinds of housing, affordable and market-rate housing alike.

Officials must adopt growth management approaches instead of growth control policies. Growth control policies are usually implied in rigid Master Plans, and are designed to limit the growth of the housing stock. Growth management policies on the other hand, accommodate future growth and projected development. Growth management planning usually focuses on increasing density, mixing housing types, and promoting regional fair shares of housing.

Strategic objectives:

- Initiate a 20-year planning program for land supply (large mixed use development) including provision for basic services.
- Ensure the participation of communities and the empowerment of women in decisions affecting their well-being.
- Ensure a long-term scenario to secure new housing and land lots to adequately address population growth.
- Initiate pilot public/private partnership programs in land supply and basic services.

2. Housing finance to increase affordability and the role of the IHF

Housing finance plays an important role in improving the housing markets of a country. Housing finance around the world has moved from subsidizing the cost of very few low-quality housing, to a more enabling finance market providing capital requirements for corporate and individual investors. Greater availability of resources will allow for a more competitive and productive market, delivering better and more affordable housing units. Housing finance can also boost production of more diverse units, developed by the private sector and community based organizations.

What is needed is an inclusive and participatory policy enabling and empowering poor people. This policy should involve these beneficiaries and capture their initiative and solidarity to leverage social capital, inexpensive labour and underestimated savings. The first step will be to incorporate the assets of the poor into formal city economies by securing tenure and property titles for those in the informal sector.

A second step needed is to approach not only the private sector but also to include community groups and non-governmental organizations in home delivery and micro-financing. New housing finance, in both the primary and secondary markets, can provide a relatively safe alternative for foreign investors or local non-traditional sources.

Since Iraq is now more urbanized, the country will need to adopt a third step to develop housing finance mechanisms for poor people. Financial assistance could help banks and lending institutions build, improve or add to their existing housing unit. An alternative vehicle for affordable housing finance is microfinance (e.g. revolving loans). Compared with traditional financing, the loan to value ratio of micro-financing is smaller. If run by the community, costs will be lower and expensive foreclosures will be rare.

The Iraqi Housing Fund (IHF) should adopt a new set of written operational procedures following international standards in corporate governance and personal accountability and should design an operational strategy that includes inter-institutional agreements. The IHF should be the driving force behind institutional reforms in the housing sector in Iraq.

There is a need to engage old and new parties in housing finance. The expansion of mortgage capacity should not just be with existing banking institutions, but should also boost a new industry of regulated institutions that specialize in local housing finance, including savings and loans.

The IHF should play the role of a good partner and a strong player in the housing market promoting proper laws and procedures (such as foreclosure laws) that are conducive to the private sector – especially to banks interested in operating mortgage finance instruments. The IHF should aim at developing specialized lending products for low-income populations that do not meet the conditions of conventional lending (collateral, credit history, tax payments, etc).

Fund monies shall be maintained and managed separately from other general government accounts, and project-based and financial operations shall be transparent, with annual external, independent audits. Procedures awarding housing and infrastructure projects under the fund should adhere to high international procurement standards of transparency, accountability and fair competition. There should be procedures built into the Fund's operation to ensure that program goals and activities are well-planned and executed according to internationally accepted development standards.

To leverage resources into the mortgage sector, the IHF can issue bonds in capital markets to raise money to loan to lenders. So rather than local banks relying exclusively on commercial loans and personal savings deposits to fund loans, the IHF can supplement these sources with capital, loaned or "advanced" to local lenders leveraging resources through bonds backed by the government.

Finally, the IHF has to build confidence in the housing market by setting up accounting and auditing mechanisms for transparent and correct management of resources, assets and subsidies.

Strategic objectives:

- Initiate a 10-year program for short and long-term financing of housing.
- Initiate a 20-year program to open Housing Savings Accounts and other incentives to mobilize private savings for short term funding to the housing sector. Through savings, Iraq will establish a new group of bankable clients and a collection of geographical information regarding the needs for housing and capacity among households to take loans.[2]
- Provide technical assistance for policy and regulatory reform focusing on private/public partnership finance systems – to provide a front line of community-based finance and micro-finance providers. This effort will also handle property registration and asset valuation, construction finance, long-term finance, risk insurance, foreclosure and repossession, underwriting, loan management, securitization and capital markets.
- Provide technical assistance to the Iraqi Housing Fund as a housing promoter and liquidity facility. Reform the Iraqi Housing Fund, with the aim that the Fund be responsible to ensure that enough urban land is available for private housing development, and to guarantee that enough and affordable financing is available through out the country.

  At least initially, it will be desirable to reach an agreement indicating that resources budgeted for housing, land management, and basic infrastructure from existing budgets of the relevant Ministries will be transferred or allocated to, and spent through, the Iraqi Housing Fund.

  A 3 percent maximum administrative fee will be charged to help supplement the IHF functioning and supporting the Boards, project Committees, IT and procedures, external audits and capacity building among the fund and related ministries.

- Within the IHF establish one or more Project Committees representing Ministry of Construction and Housing (MoCH), Minstry of Finance (MoF), Ministry of Planning and Development Corporation (MoPDC), and relevant regional and local authorities.
- Define sustainable and better targeted subsidies.
- Closely follow policy and regulatory reform of the Real Estate Bank and the deregulation of mortgage financing in Iraq.
- Closely follow policy and regulatory reforms to the pension and insurance sector in Iraq to help attract institutional investors in order to build a secondary market in Iraq.
- Closely follow larger reforms in the financial sector.
- Initiate pilot public/private partnership programs in mortgage lending to purchase, construct and rehabilitate housing units.

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[2] Usually governments make sophisticated calculations to estimate housing needs. Suppliers, public and private, limit their development to large cites were there is a working housing market. By opening accounts in the place of their preference, demand is decentralized and in favor of a more regional approach to housing delivery instead of focusing in the capital and main cites.

3. Improving productivity and affordability in the construction sector

Housing Delivery. Iraq's response to the current housing crisis has been and continues to be state-driven with very limited involvement by the private sector. The state has assumed the responsibility of providing housing and has not adopted an enabling strategy engaging both the private sector and local communities and their organizations. The country lacks an enabling legislation to facilitate private sector investment in housing and basic service. Also constraining private participation in the housing market are the legal rent restrictions, weak financial services, and the rising costs of construction.

A short-term objective should be to raise equity capital. However raising equity capital to develop housing projects is more costly and problematic for affordable housing due to the greater perceived risk. That does not mean private equity cannot finance large affordable housing developments. If Iraq adopts some of the prudent measures suggested in this document, equity investors will supply operating capital and supply affordable products to the low-income housing market. Nevertheless, it is also true that in other countries non-profit organizations, community based groups and charitable foundations provide some of the funding. Hence the importance of engaging local community groups to deliver affordable housing.

Strategic objectives:
- Initiate a 10-year housing program at market rates with special emphasis (25%) addressing the needs of vulnerable groups.
- Initiate a 15-year urban upgrading program addressing the needs of low-income social groups living in sub-standard neighbourhoods.
- Provide technical assistance for policy and regulatory reform, focusing on a private/public partnership as well as delivery systems, self-help programs, building materials, construction technology and building codes and standards.

4. Institutional and human resource capacity

Capacity Building. While human capital, in the form of trained experts and professionals far exceeds that of many developing countries, the institutional framework is quite weak and not well oriented for addressing the housing shortfall and improving the quality of the existing housing stock.

Strategic objectives:
- Reform the institutional framework to manage the housing sector. Change the role of the public sector from being the supplier of housing to being an enabling body that regulates the market, encourages others' participation and ensures affordable and quality housing.
- Restore central and local authorities' institutional capacity to manage the sector and implement reform.
- To improve housing finance and banking the Ministry of Construction and Housing and Ministry of Finance need to be re-examined.
- Reform the Iraqi Housing Fund, and form an ad-hoc housing board that will bring together government, financial institutions, developers and NGO's.
- Build capacity among policy makers to analyze housing and urban data and deliver support policies and strategies.
- Upgrade the cities' planning departments and set up a specialized training program for participatory planning.
- Training of technical professionals to work in real estate development.
- Build capacity among the private sector to manage and run the mortgage sector.
- Organize training, workshops and study tours for added exposure to international practices.
- Introduce office administration, business information, and communication technology to better manage sector data and enable the design of an urban observatory in Iraq.
- Introduce privatization measures over a period of 5-10 years.
- Open up the construction and building material industry to private sector competition, in a manner that maintains present levels of productivity.
- Build capacity among state-owned companies to run as private enterprises.

Conclusions

The financial services industry in Iraq is only partially developed and does not provide housing finance, other than through one national housing bank. The National Real Estate Bank has been the sole service provider of mortgages and home loans but there is a well functioning and extended network of private finance institutions. State-owned corporations in Iraq need to focus on a more regulatory and policy-making role and leave to the private sector to leverage and channel the enormous amount of resources needed for the housing sector. It is key to note that most needed resources will come from the local market, and only some foreign seed capital (grants or loans) can be expected to boost financing activities.

As public resources are limited and Iraq's priorities focus on achieving security, macro economic stability and increasing revenue through oil production the housing sector needs to rely in the internal market.

The country needs to develop a sound and strong housing finance market. A better housing market can encourage saving and creates wealth. Improving delivery of housing will reduce the impact of squatter settlements – something the country needs to address as soon as possible as displacements have worsening since the war. It also means releasing state owned land to the market. Privately owned land should be easier to assemble and construction fees and standards should be kept to a minimum to keep housing affordable.

Finally, the government should avoid distorting the market and encourage the private sector to participate in the housing finance and housing market. As macro stability and security is achieved in the country and competition increased affordability will be achieved. At the beginning housing finance will probably only benefit a small proportion of the population. But as in many other countries around the world, competition and global capital markets should pass on benefits to those households with limited income.

It is expected that the housing sector in Iraq will lead to improved cities. Building and infrastructure construction can contribute to create jobs and generate most needed income to poor households. A functioning housing market will contribute to bring security to the country, enhanced economic development and macroeconomic stability.

Egypt: Overview of the Housing Sector

By Stephen Everhart, Berta Heybey, and Patrick Carleton, OPIC[1]

Housing investment is a key component of economic development, both because housing is a basic social need and because private home ownership is often an important source of capital for entrepreneurship at the grass roots level. A fully functioning housing market, including clearly defined titles to privately owned property, is an important element in the construction of a dynamic market economy.[2] Developing mortgage finance helps low- and middle-income citizens to acquire ownership of housing and enables these citizens to turn housing assets into a source for financing small business activities.

Currently, there is little to no mortgage financing in Egypt. Though Parliament passed a Mortgage Law in 2001, there have been a total of only 16 mortgages completed since that time. Without a broad access to mortgage financing, low- and middle-income households cannot afford to buy housing in the formal sector. Consequently, most of this part of the population lives in public housing or informal housing units with no clear legal title. The biggest obstacle to mortgage finance in Egypt is property registration, a cumbersome process with high registration fees, as well as the lack of critical legal infrastructure, particularly in terms of contract enforcement, to support it. Other issues include restrictions on extending bank credit to the housing sector; lack of valuation information; lack of credit risk information; and complex regulations.[3]

Potential investors should be aware of these structural challenges before investing in the housing market in Egypt. However, despite these issues, there are still substantial opportunities for foreign investors in housing finance, construction and infrastructure projects. Such opportunities could be significantly enhanced by further legal reforms. In recent years, Egypt has passed a number of laws helping to establish a legal framework for housing finance, though a number of shortcomings remain. International and bilateral organizations are also working with the Egyptians on legal reforms. USAID, for example, has a $35 million project to assist with the development of a mortgage finance system, while the US Appraisal Institute is helping to train and certify appraisers.

The following sections expand on the topics discussed above:

- The importance of housing finance in economic development
- Structural challenges to mortgage finance in Egypt
- The current state of the housing market in Egypt
- Opportunities for foreign investment/ involvement in the Egyptian housing sector

THE IMPORTANCE OF HOUSING FINANCE IN ECONOMIC DEVELOPMENT – OVERVIEW

Improving housing finance supports economic development through several channels: increasing saving, investment and employment; strengthening and deepening the financial sector; and reducing poverty. In many developing economies, including Egypt, the lack of a fully functioning mortgage market constrains the development of the housing sector. Without financing options, low- and middle-income households cannot afford to purchase homes. Since a house is often the primary investment and savings vehicle for those groups, a lack of housing finance also constrains overall saving rates. Low saving and investment rates restrict economic growth and limit economic development. Egypt would benefit from boosting both saving and investment rates.

International experience suggests that living standards increase when there is widespread availability of home mortgages because mortgages have a positive impact on the quality of housing, infrastructure, and urbanization. Mortgage availability for low- and middle-income groups encourages investment in both residential property and other real estate (such as retail shops and other small businesses). This, in turn, encourages medium- to long-term growth. New construction also provides jobs for

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[2] de Soto (1997).

[3] More details on these issues will be provided in the next pages.

low- and middle-income workers, which certainly are needed in Egypt.

Housing finance also encourages the growth of the financial services sector, which studies have also shown to be a key factor in economic development.[4] If consumers begin to save for down payments and loan repayments, these actions increase both the assets available to the financial services sector, and the demand for more financial services. Additionally, financial markets and intermediaries act as a lubricant in well functioning economies. They perform the crucial task of mitigating information and transactions costs and provide a needed bridge and filter between economic agents of information that otherwise would not be shared. This enables firms to allocate their resources more effectively and increase their productivity, resulting in greater overall economic growth.[5]

Finally, empirical studies show that there is a positive relationship between land distribution equality, poverty reduction and economic growth.[6] More accessible housing finance could lead to more ownership by low and middle income households. Low and middle income households are the most limited in financing options, both because of an inability to afford down payments and also an inability to access capital markets for long-term loans.[7] At the same time, housing is often their biggest expense, accounting for 50 to 70 percent of their budgets. If housing finance can be made more affordable, that will free up resources that the poor can then use for other opportunities, such as starting small businesses. Therefore, improving access to housing finance for low-income households will help reduce poverty, and serve as another channel to increase economic growth.

The main challenge facing the housing sector in Egypt and other Middle Eastern and North African countries is the lack of affordable housing, not a lack of available housing stock. The lack of efficient financing options is a large component, and the single most correctable component, of these high housing costs. Since housing policies affect the entire economy – influencing saving, consumption, financial depth, employment (construction and homes used as a place of business), and government budgets[8] – improving the availability of housing finance would go a long way towards furthering overall economic development and reducing poverty.

STRUCTURAL CHALLENGES IN THE EGYPTIAN HOUSING MARKET

Implementing a fully functioning mortgage market often requires structural reforms that may take a long time to implement. Mortgage finance is not possible until property rights and land registration rights are enforceable, for example. In Egypt, estimates are that over 90 percent of urban housing is in the informal sector – that is, without a formal title. Because the residents do not have a formal title to their property, they cannot use their houses as collateral for other investments, such as building small businesses, limiting economic growth. The lack of formal titles also limits infrastructure development. Since it is not possible for utilities to know who owns the properties using their services, and therefore who is responsible for paying for them, there is a disincentive to develop these services fully.[9]

As already mentioned in the introduction, the lack of mortgage lending in Egypt is due in part to the following issues:

- **Inadequate legal infrastructure:** The lack of well-defined legal procedures for enforcing claims, curing defaults and evicting former owners of foreclosed property has limited the willingness for providing housing finance. Similar reasons limit the availability of mortgage and property insurance. The inadequate infrastructure forces interest rates on secured loans to increase, approaching the level of unsecured loans. Although the Real Estate Finance Laws of 2001 (much of which were put into operation in early 2004) attempt to address this problem, their effectiveness is still unproven.

- **High registration fees, taxes and inefficient property registration procedures:** The regulatory burden is such that much of Egypt's housing is in the informal sector. In comparison to neighboring countries, the percentage of housing in the informal sector in Egypt is much higher. (In Tunisia, for example, only 29 percent of housing is in the informal sector.) Some progress has been made in this area, reducing property registration fees from 12 percent to 3 percent with consideration to further reducing the fees to the administrative cost of registration (less than 1,000 Egyptian Pounds (about USD 173).

- **Restrictions on bank credit to the housing sector:** The Central Bank has imposed a 5 percent ceiling on real estate lending, which local analysts suggest may be raised to 10 percent in the future. This limit applies cumulatively to both the supply and demand side of the market: residential and commercial real estate loans, as well as loans to individuals and housing developers.

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[4] See Beck et al (2000).

[5] See Schumpeter (1912) and Diamond (1996), among others.

[6] Galal and Razzaz provide detailed information on the empirical literature. For example, Alesina and Rodrik have shown that reducing inequality in land ownership across income levels by one standard deviation increases economic growth by more than one percentage point (Alesina and Rodrik, 1994).

[7] Erbas and Nothaft (2002).

[8] World Bank (2003).

[9] de Soto (1997).

- **Lack of risk information for lenders:** There are no credit bureaus in Egypt, though one is currently in development by a group of Egyptian banks and financial institutions, meaning lenders have no way of assessing credit risk of the borrower. Quite often lenders mistakenly assume that low-income people are poor credit risks and so do not tend to lend to them. Instead, lenders assume the rich are a better risk, so that there tends to be a good supply of high-income housing, but a shortage of low- and middle-income housing. Absent this sort of information, potentially creditworthy borrowers (for example the self-employed) often go without funding. In addition, the informal sector—with little incentive to report income to the tax authorities—will be missed by credit agencies as well.

- **Inconsistent approach to property valuations:** The lack of valuation information makes the effective use of financing very difficult, as lenders have very little idea of the true value of property that they will recover in the case of default. A program to train and certify appraisers is currently under development with assistance from the US Appraisal Institute.

STATE OF THE EGYPTIAN HOUSING MARKET

All of the issues discussed above contribute to inefficiencies in the housing sector in Egypt. Comparing Egypt with Algeria, Jordan, Morocco, and Tunisia shows that Egypt has the lowest rate of owner occupied property, the highest ratio of civilians in public housing, and the highest ratio of citizens in the informal housing sector (see Table 1). Egypt and Tunisia have the longest delays in settling foreclosure disputes. All of these measures are either impediments to a well functioning property sector, or indicators of current troubles in that sector.

In the Middle East and North Africa, developing the housing sector is particularly important to support the needs of a quickly growing population. Population growth in the Middle East and North Africa is among the highest in the world. The rise in the working age population is particularly significant, requiring more jobs to prevent the current high unemployment rates from increasing further. In Egypt, the unemployment rate is around 12 percent, while the population aged between 20 and 29 years grew about 30 percent between 1990-2000, and is projected to grow a further 20 percent between 2000 and 2010.[10] New housing construction therefore serves two purposes: providing shelter and construction jobs.

Due to these demographic issues, housing and construction represent almost 50 percent of the Egyptian government's investments.[11] In 1998, for example, the government subsidized housing program financed about half of all low-cost units built in the formal sector (approximately 63,000 units).[12] The public sector owns about 29 percent of all housing units in urban areas, compared to 25 percent in Algeria and only 8 percent in Tunisia.[13]

Despite this emphasis on housing, Egypt currently has a supply-demand mismatch in the sector. There is an excess inventory of medium- and high-end properties, while the demand is for low-income housing. Low- and middle-income households do not have access to financing that would allow them to purchase any of the available housing units. MERIS (Middle East Ratings and Investors Service) estimates that total annual demand for housing units is approximately 750,000 units (480,000 for newlyweds; 220,000 for replacement of marginalized areas; and 50,000 for old buildings that are about to collapse). However, total supply to the formal real estate market was only 260,000 units in 2004 (see Table 2), about 35 percent of demand.

Rent control regulations further exacerbate the situation. While Egypt has cancelled these regulations for new leases, existing stock is still subject to them. The result is that over 1.8 million housing units in Egypt are vacant. Over 1 million of those are in Cairo, resulting in a vacancy rate of 14.5 percent, very high by international standards. These units are vacant for several reasons: parents may be keeping them for their children's future use; owners may not want to rent them because the low rents they can receive due to rent controls do not make it worthwhile; or owners may not be able to find buyers who can afford to buy the unit due to the lack of available financing options.[14]

The Mortgage Law of 2001

The Egyptian Parliament approved a new real estate mortgage law in 2001 (although much of it was not implemented until 2004) to regulate real estate bank financing. The law, which is geared towards encouraging housing of low and middle-income groups, allows banks to offer subsidized and non-subsidized loans for the purchase of houses as well as administrative and commercial units and renovating existing ones. The goal is for borrowers to be able to make a 20% down payment and pay off the remainder in installments over 20-30 years. Buyers will receive title while still subject to mortgage. Further, under the new law, banks supposedly will be able to foreclose on loan defaulters in case they default on payments for between six and nine months.

Egypt modeled its Mortgage Law after US mortgage regulations, but there are some serious differences. Financing from both bank and non-bank mortgage lending groups is permissible according to the 2001

[10] World Bank (2005).

[11] MERIS, Middle East Rating & Investors Service (2004).

[12] Erbas and Nothaft (2002).

[13] World Bank (2005).

[14] World Bank (2005).

law, but the two groups are not regulated identically. If a bank is lending money for housing finance, the contract is between the bank and the buyer, as in the US. However, this type of lending is strictly regulated, including the 5% ceiling on all lending to the housing sector discussed above.

On the other hand, in Egypt the non-bank finance houses, as described under law 148, operate similar to banks but are not limited by strict regulations and lending percentages. A non-bank finance house operates as a third party entity between buyers and sellers. Finance houses purchase properties from sellers, increase the price as appropriate under market conditions, and then resell the property to buyers using the installment method. It is recognized that the lender's lien on the property being financed gives it the rights to benefit from the outstanding percentage of loan to the original purchase price of the real estate. Since it is the buyer who retains the physical rights to possession, the difference in price due to mark-up is the compensation for the outstanding loan-to-value percentage.

To encourage the development of this sector, the government created a program that subsidizes housing payment for three months in the event of unemployment so that the default rate drops and the non-bank institutions are not disadvantaged.[15] Another difference is that leasing companies retain property ownership and can repossess assets without having to follow tedious enforcement guidelines.

Current financing options

Since the Mortgage Law was passed in 2001, there have been only 16 mortgages completed. Instead, financing is done either with a personal loan or through the housing developer. In either case, loans are for less than 8 years. In addition, since borrowers are unable to use the property as collateral for the loan, the loans are at high interest rates, making it especially difficult for low- and middle-income households to buy a home.

When developers finance housing, they use an installment system. The down payment is normally between 25 and 50 percent of the purchase price, with the rest of the payments occurring over the next 3 to 8 years. The title does not formally transfer until the entire amount has been paid. The high down payment is a severe constraint, especially for low-income households.

In April 2005, the Egyptian government approved a joint cooperation program between the Mortgage Financing Authority and the National Bank of Egypt. The program is designed to finance mortgages with interest rates at or below 12 percent and a term of 10 to 20 years. While this program sounds promising, it is not clear when or how it will be implemented.

OPPORTUNITIES FOR FOREIGN INVESTMENT/INVOLVEMENT IN THE EGYPTIAN HOUSING SECTOR

There are opportunities for foreign investment in housing finance, housing construction and associated infrastructure. Possible investment areas include the following:

- **New cities:** In 2000, about 64 percent (42.5 million) of Egypt's population lived in urban areas. By 2025, this number is projected to rise to 83 percent (78.8 million) due to natural population increases and migration.[16] To accommodate this demand, the Egyptian government plans on increasing the number of new urban cities from the current 17 cities to 59 cities by the end of 2017,[17] creating substantial opportunities for investors in financing, housing construction and infrastructure.
- **New housing developments:** The structural reforms discussed above are necessary before a fully functioning mortgage market can exist in Egypt. In the near term, many analysts suggest that the most potential in Egypt may be in projects that support construction of low-income housing, with a lease-purchase option, rather than in straight mortgage finance (similar to OPIC's Jopa Villas project in Kenya[18]). This way, financiers would be able to support the provision of low- and middle-income housing, and perhaps structure the deal such that a local bank provided financing. These projects could serve as demonstration projects and provide a step in creating a more robust mortgage market.
- **Existing housing:** There may also be opportunities for private financing in the middle-income market. There is high demand for housing among the middle class, while at the same time there are many vacant units. The mismatch exists because households cannot obtain financing to purchase these units. Providing financing will help both buyers and sellers. The new owners will have housing, and the sellers will be able to invest capital that had been locked up in the vacant units in other areas.

Current players

Some of the international companies and organizations currently involved in the Egyptian housing market include:

- There are 4 firms offering mortgage financing in Egypt, Al Tameer Co., Egyptian Housing Finance Co., National

[15] It should be noted, however, that Egyptian policy makers (academics, various political parties) are currently discussing changes in the approach to these subsidies. Under the new proposals subsidies would be shifted away from the three month payment and would instead help low income borrowers with down payments.

[16] PlanBleu.

[17] MERIS (2004). These plan would also include the creation of new urban areas around existing cities.

[18] OPIC is providing finance and insurance for construction of affordable housing units in Nairobi, using a unique, long-term lease-for-purchase program.

Societe Generale Bank, and the Arab Investment Bank.[19]
  - Al Tameer has authorized capital of $86.2 million, and is owned by a consortium of Egyptian banks, both public and private.
  - The Egyptian Housing Finance Company (EHFC), a private company dedicated to long-term affordable housing finance, was formed in 2004 with the help of the IFC, who took a $1.6 million equity share (20%). [Egyptian banks own 50%; the German Company for Investment and Development (DEG) owns 20%; and the Indian Mortgage Finance Corp. owns 10%]. EHFC will target middle class buyers, with a 14% rate and a maximum of 10 years tenor.
- Century 21, ERA, and Coldwell Banker realtors have offices (or officers) working within this market.
- Stewart International, a large US based international company that provides services to support the real-estate financing industry, such as title assurance, and escrow services worldwide; is reportedly in the process of establishing a new holding company to provide these services in Egypt. Stewart reportedly will control 55% of the new company, and its three Egyptian partners {Coldwell Banker Middle East/ Mansour and Maghraby, the Olympic Group, and the Osman Group} will each control 15%.[20]
- USAID's current major project is a $35 million Financial Services Project, whose objectives are to provide technical assistance, training and information technology to both public and private sector participants in the real estate and finance industries. This five-year project has four parts:
  - Legal reform and technical assistance and training to lenders to develop an environment conducive to a fully-functioning real estate finance industry
  - Modernization of property registration in urban areas: USAID has a pilot project in two districts in Cairo to create a systematic title registry that they hope to use as a template for the registration process
  - Establishment of a credit information system to assist lenders in assessing risk
  - Development of a broader range of financial instruments for the capital markets to increase financing opportunities.
- Chemonics International Inc. is implementing the USAID project.[21] The project will provide assistance to the Ministry of Justice (for property registration), the Ministry of Investment (Mortgage Finance Authority and Capital Market Authority), and the Central Bank of Egypt (for credit information services).
- The US Department of Commerce's Commercial Law Development Program is working to help implement and refine Egypt's new real estate legal framework.
- The World Bank is currently in discussions with the GOE on a program that would
  - Expand property registration based on lessons learned from the USAID-funded pilot registry program
  - Support development of secondary markets for real estate finance.
- Canada plans to support the establishment of a housing and real estate unit within the Egyptian Ministry of Housing.

CONCLUSION

Home ownership, with well-established property rights, forms the foundation of a healthy financial system. In the U.S., for example, despite the sophistication and scale of the U.S. capital market, mortgages remain its cornerstone. The existence of this large, stable pool of finance – with a well-diversified risk basis (and much of it insured) – has been critical in the development of U.S. capital markets. Moreover, creation of a "homeowner class" is one of the surest methods to help a society achieve long-term political stability. As the preceding review of the Egyptian mortgage market makes clear, the Egyptian government has begun the process of building out the institutional capacity and infrastructure necessary to grow a sector that will bring broad economic and social benefits.

[19] Hafiz (2005).

[20] Nametalla (2005).

[21] Chemonics is working with the US Mortgage Banker's Association and the Egyptian Banking institute, as well as the following Egyptian firms: Bahaa-Eldin Law Office; Hassouna &Abou Ali; Zarrouk, Khaled & Co.; FinBi Consulting; ARABSOFT; and Quality Standards Information Technology.

Table 1: Housing Indicators Comparison, MENA and select countries [22]

	Gdp per capita $US-1992 [A]	House price to income [B]	Housing Credit (%) [C]	Owner occupancy (%) [D]	Public Housing (%) [E]	Informal Housing [F]	Construction Costs ($US/M^2) [G]	Permit Delays (months) [H]	Foreclosure Delays (months) [I]
Algeria	2,060	12		45	25	4	500	2	
Egypt	**600**	**7**	**7**	**32**	**29**	**65**	**67**	**3**	**24**
Morocco	950	7	7	46	15	16	158	3	
Jordan	1,240	3	19	75	12	15	150	7	3
Tunisia	1,440	6	6	67	15	29	359	12	24
USA	21,790	4	44	61	1	5	500	36	5
Turkey	1,630	5	3	60	5	51	110	2	6
Mexico	2,490	4	18	83	54	16	267	3	6

Definitions: [B] Median House market price to median income; [C] ratio of housing loans to total loans in government and financial institutions (in per cent); [D] percentage of dwellings occupied their owners; [E] percentage of dwellings owned managed and controlled by the public sector; [F] percentage of dwelling not incompliance with current regulations and those that occupy land illegally; [G] present replacement cost per square meter of a median priced unit; [H] median time to get approvals, titles and permits for a 50-200 unit residential subdivision at the urban fringe where residential development is permitted; and [I] typical time from start to finish of foreclosure (including eviction) an a seriously delinquent mortgage.

Table 2: Supply of Housing [23]

	2002/2003		2003/2004	
	Number	**%**	**Number**	**%**
URBAN HOUSING				
Economy Level	125,600	50.1%	131,000	50.4%
Medium Level	32,000	12.8%	35,000	13.5%
Above Medium Level	9,000	3.6%	10,000	3.8%
Total URBAN	166,600	66.5%	176,000	67.7%
Economy Housing at Rural and Land Reclamation	84,000	33.5%	84,000	32.3%
Grand TOTAL	250,600	100.0%	260,000	100.0%

[22] Erbas and Nothaft (2004).

[23] MERIS (2004).

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How US-Style Title Insurance is Transforming Risk Management in European Real Estate Markets

By Jean-Bernard Wurm, Managing Director, LandAmerica (Europe)

I. BACKGROUND

In this paper, we will review the reasons why Title Insurance has become a universal instrument for real estate transactions in the US, and examine the increasingly important role that it is playing in Europe.

Once only available in the US, Title Insurance is now a well-established financial instrument for mitigating risks in property acquisition, financing and securitization in Canada, Latin America, the Caribbean, Asia and Australia.

In Europe, especially Central and Eastern Europe (CEE), the demand for Title Insurance has increased along with the growth and sophistication of cross-border real estate transactions. According to a survey by Jones Lang LaSalle, the flow of cross border investments in Europe reached €46 billion in 2004. It grew 27% in the first half of 2005 to reach €24 billion and there is no reason it should slow down in 2006.

II. WHAT IS TITLE INSURANCE?

Title Insurance guarantees that buyers and lenders benefit from a clean ownership title. For a one-time premium, it provides coverage against financial loss arising from title defects and other irregularities relating to real estate, such as compliance with zoning, codes and permits. Title Insurance also frees investors and their lenders from having to understand complex legal opinions in various languages, formats, contexts and degrees of reliability. Two aspects should be highlighted:

- Financial Protection Against Both Known and Unknown Title Defects. The original purpose of Title Insurance was to insure against "unknown" defects, with "known" defects shown as exceptions in the policy. That coverage has evolved, and now title companies often provide insurance for "known" or existing defects or title problems.

- Protection Beyond a Legal Opinion. Lawyers provide an *opinion*. Title Insurance provides a *guarantee*. A legal opinion, especially in a large transaction, is fundamentally a disclosure document, in which counsel carefully defines the state of title and related issues, identifying – but not eliminating – risks. Title Insurance goes *beyond* a legal opinion to underwrite risks due to faulty records, ambiguities, negligence, fraud, or even simple mistakes.

III. A BRIEF HISTORY OF TITLE INSURANCE IN THE UNITED STATES.

Title Insurance was created in the last part of the 19th Century. Until then, buyers could acquire insurance for errors and omissions only from their lawyers.

At that time – as in Europe today – each state in the US operated with different laws for conveyance and property rights. Each had a multitude of counties with different sets of regulations for zoning, permit or deed recording. Certain states operated under a system of deed recording similar to France, others under registration of rights similar to the UK. Title Insurance competed with land registration systems, such as Torrens, which 22 states adopted between 1900 and 1922. After the First World War, the Title Insurance industry began to create a national market and became the preferred mechanism.

It is important to keep in mind that until 1974, US banks could not have offices or branches outside their own state and, some, outside their county. (In Chicago, banks were limited to one branch). Banks that wished to operate nationwide could not rely on their own network to perform due diligence or have local expertise. They required two elements:

1. Assurance that there were no potential legal problems for the assets that backed their financing, and

2. A common standard throughout the maze of laws and regulations that still exists in the US. Insurers were successful in convincing lenders that Title Insurance was critical for financing residential mortgages. As a national market grew, Title Insurance policies helped standardize loan documentation and create a secondary mortgage market.

The intervention of the Federal government in the housing market during the Depression, and the ensuing evolution of loans into long-term amortizing mortgages, broadened the need for Title Insurance. The trend accelerated with the housing boom that followed World War II and the creation of Federal mortgage refinancing agencies such as FNMA and GNMA. By 1969, the industry passed the $1 billion mark in total premiums and in 2005, it represented over $17 billion in annual revenues.

When the securitization market started in the US 20 years ago, Title Insurance was already universally accepted. Every asset behind every mortgage, and every mortgage, whether residential or commercial, already benefited from Title Insurance.

IV. THE EUROPEAN MARKET FOR TITLE INSURANCE

Until recently, Title Insurance was unknown in Europe except for the UK, where a more limited type of insurance, Legal Indemnity, has existed for over a hundred years. Several American Title Insurance companies, and one European, recently entered the European market and provide coverage similar to ALTA (American Land Title Association) policies in the US. These not only cover *known* defects or restrictive use of a property but also issues that are *unknown* at the time of closing.

Unlike Title Insurance, which covers defects *unknown* at the time of closing, legal indemnity addresses *specific* title flaws or restrictive covenants. Land Registry (the Queen's Registry) only appeared in the UK in the second half of the 20th Century, much later than in the rest of Europe. Consequently, the Registry is of no use for properties that have not changed hands since it was established. The abundant tracks of land not yet entered in the Registry have created a growing demand for policies that will cover defective title or restrictive covenants.

Defective titles can include a gap in the chain of recorded ownership, missing documents or invalid signatures. *Restrictive covenants* can affect the use of a property but may no longer be enforceable, such as deeds dating back to the 1850s that limit dwellings on a property to "upstanding Christian families."

These covenants may be so old that it is impossible to determine who has a right to have them enforced, such as church deeds forbidding alcohol to be served on the land. With Title Insurance or Legal Indemnity, a developer can go ahead with a residential project or a shopping center and obtain financing without going through the court system in order to have those problems resolved before starting construction.

Traditionally, the various European land titling systems, through registration or deed recording, appear to have generated fewer errors and claims than in the US. There is, however, no hard data available in most countries to know the exact extent of title litigation taking place every year. This lack of demand to cover domestic direct acquisitions, whether commercial or residential, presents different opportunities for Title Insurance in Europe:

1. Notaries or lawyers are only responsible for errors and omissions. Once they have disclosed a potential issue, Title Insurance can assume the risk, freeing the buyer from assuming the risk himself.

2. Most European countries have created a favorable regulatory framework for real estate companies, whether unlisted or in the form of REITs. There is an increasing number of indirect transactions – through acquisition of shares of real estate companies or units of Limited Partnerships – that are not recorded in land registry or by a notary. With title insurance, buyers of shares or units can obtain coverage assuring that they benefit from a clean title as of the day of the transaction.

A Two-Fold Benefit: Protection and Standardization

Acquisition or lending has traditionally been considered safer in one's own country than abroad. There are several benefits to Title Insurance in cross-border transactions:

- The *traditional* role of insurance, since participants often feel uncomfortable with risks taken abroad that they would readily assume in their own country.

- A form of *standardization*. Title insurance provides lenders and buyers with a standard text in English that applies (with only limited variations) in every single country of the European Union and in most CEE countries. For investors or lenders active in cross-border transactions, it can eliminate the need to refer to lengthy legal documentation translated from a variety of languages.

- In large residential portfolios, Title Insurance can greatly simplify the legal due diligence for developers, buyers and lenders. In countries like Spain, where a very high proportion of secondary home buyers are foreigners, providing title insurance can give developers a strong competitive advantage. It can also pave the way for future securitization of the portfolio.

Furthermore, sellers may be not be in a position – or may be reluctant – to provide legal representations and warranties.

- Public companies have to disclose contingent liabilities and carry explanations in the footnotes of their annual reports.

- Private companies may not want to continue having exposure on a property that they no longer own.

- SPVs (Special Purpose Vehicles) that are commonly used may not be dissolved immediately after a transaction and may have to keep a portion of the sales proceeds to back up those "Reps & Warranties."

V. TITLE INSURANCE: A CRITICAL ROLE TO PLAY IN EUROPEAN CMBS/RMBS SECURITIZATION

By the time securitization appeared in the US in the late 1980's, title insurance had already become the norm for commercial and residential loans. In Europe, however, the securitization market developed before the appearance of Title Insurance.

Title Insurance Makes Securitization More Efficient

Securitization in the United States had a dual purpose, one was to absorb the volume of loans that the RTC (Resolution Trust Corporation) put on the market, following the debacle of the Savings and Loans institutions, the second was to make access to home ownership possible for a much larger percentage of the population by creating a secondary mortgage market that can function on a much larger scale.

Title Insurance enhances the efficiency and liquidity of CMBS/RMBS markets by:

1. Helping mortgage-backed securities achieve satisfactory credit ratings

2. Providing a *private* solution to harmonizing legal due diligence across different laws, regulations and languages, especially critical in multi-country transactions

3. Allowing fund managers to respond to investor demands for safety and common standards for legal due diligence and thus helping fulfill their fiduciary requirements.

CMBS/RMBS – A Financial Product Growing in Importance in Europe

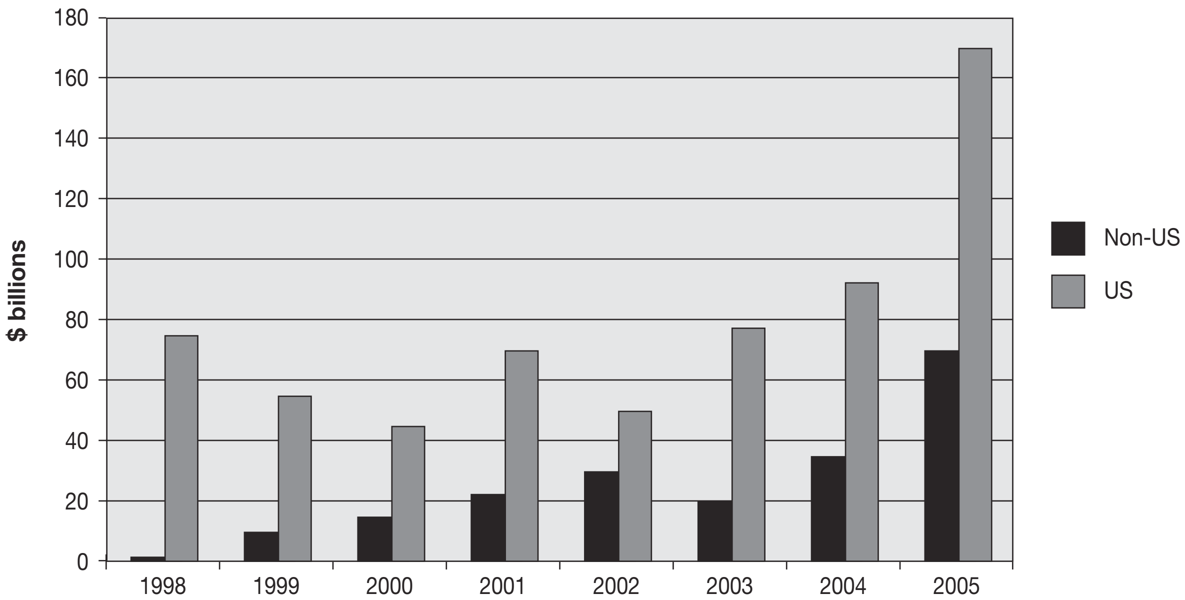
Volumes in Europe lag 10 years behind those in the US. Although European CMBS grew 89% last year (Deutsche Bank, 2005 Review & Outlook for 2006), Europe may *not* witness the sharp increase that the mortgage securitization market experienced in the US after 1995.Source : Commercial Mortgage Alert

There are specific traits of the European securitization market that have, so far, limited its ability to follow the US pattern of growth:

1. The European securitization process has been driven more by issuers than investors. While the ESF (European Securitization Forum) and CMSA (Commercial Mortgage Securitization Association) have set up procedures/standards, and are active in lobbying the European governments and institutions to create favorable legal frameworks for the securitization market, there are still no European standards for loan documentation or legal due diligence. Issuers have attempted to follow certain formats, but there are significant differences remain in the information disclosed to the public for each issue.

2. The focus of European issuers has been to obtain the most favorable financing rather than unload various risks off their balance sheet.

Figure 1: CMBS Volume Trends: US vs Non-US



Source: Commercial Mortgage Alert

AAA tranches in the US represent less than 40%, and AA another 20%, of all MBS issues. By contrast, in Europe, over 90% are AAA and AA, with some issues rated 95% or even 100% AAA.

1. The MBS market continues to be dominated by the UK, which still represented 60% of new issues in 2005. The percentage of Pan-European securitization was only 4% last year, but is expected to grow significantly.

   For Pan-European issues, it is much easier to provide rating agencies and investors with a standard title policy that covers all countries, rather than with translations of legal documentation from different jurisdictions, languages and formats.

2. There will also be new market entrants from countries where the "perceived" legal risks are much greater and the need for title insurance more compelling:

   "Industry analysts predict that Russian mortgage lenders could have $45 billon of MBS outstanding" (Asset-Backed Alert 3/17/06), and Turkish bank, Isbank, is considering $1.4 billion MBS program (Security News, 3/13/06).

3. Single-borrower/single-property issues where title conditions are easier to grasp, represent 28% of transactions to date, but this percentage is expected to diminish.

In the wake of Basel II implementation, Title Insurance can play a key role in broadening the risk profile of European MBS issues.

VI. SUMMARY AND CONCLUSIONS

The formation of a global real estate market in Europe over the last 20 years has created a context similar, in many ways, to the situation in the US at the end of the 19th Century: investors and lenders operating through different jurisdictions, with different laws or rules, as well as very different methods to record and guarantee title.

Title Insurance has evolved into a universal standard in the US real estate market with over $17 billion in annual premiums in 2005. While no one expects the European need for Title Insurance to generate similar volumes, demand for Title Insurance has increased in Europe due to the rising volume of cross-border transactions, the increase in indirect real estate transactions, and the development of a securitization market as a tool for home ownership to a much larger percentage of the European population.

As for securitization, real estate professionals, bankers and rating agencies are becoming increasingly aware of the role Title Insurance can play in simplifying and expediting issuance, covering known and unknown legal risks, thereby enhancing the safety and liquidity of CMBS/RMBS markets.

While there are efforts to harmonize mortgage markets within the European Union, it may take years to move forward. Title Insurance provides a private solution that allows investors, as well financial institutions, to benefit from a vast unified market. In addition, there is a growing demand from American and European investors, rating agencies, and auditors for additional disclosures as well as stronger guarantees.

The Remaking of Housing Policy: The New Zealand Housing Strategy for the 21st Century

By David C. Thorns, Director of the Social Science Research Centre and Professor of Sociology at the University of Canterbury (New Zealand)

Introduction

Analysing shifts in policy requires us to appreciate that they are embedded in the past as well as in the present. Parsons in a recent examination of policy development argues that "it is existing policies which set the agendas for new problems and provide the discourse within which problems will be constructed" (Parsons 1995:231). Understanding the development of New Zealand's housing strategy for the 21st century requires us to understand both the past transformations that occurred through the 1980s and 1990s and the future predictions with respect to the shape of New Zealand's future population, tenure shifts and increasing diversity (NZ Housing Strategy, 2004, 2005).

Housing policy through the 1980s and 1990s was reshaped, as part of the wider restructuring of New Zealand's welfare state, economic strategies and social policies that took place at that time. At the beginning of the 1980s, New Zealand was coming to the end of a quite sustained period of extensive social and economic intervention initiated by the Labour government of the 1930s. This particular pattern was broken in the radical agenda of economic reform followed by the fourth Labour government, which came into power in 1984 (Boston and Holland 1990, Thorns 1992). Some analysts have described this set of changes as a shift from the 'first way' of New Zealand's welfare development to its 'second way', which was constructed around a strong neo liberal agenda. The current post 1999 agenda, then can be interpreted as New Zealand's version of a 'third way' influenced by movements in other social democratic societies and particularly articulated by the Blair Government in the United Kingdom and the Clinton Administration in the USA (Dalziel 2001, Giddens 2001).

In order to explore these changes first an identification of the significant restructurings that took place in the 1980s and early 1990s will be undertaken. This will show how these led to a remodeling of housing policy. Second, the post 1999 moves towards a more interventionist and social development state and a reconfiguration of housing policy will be examined. Finally, the question of whether this marks a return to the pre-1984 set of arrangements or a new form of state practice and policy engagement will be addressed.

Neo Liberal Turn 1984 to 1999

The reforms of the 1984 to 1999 period were radical and extensive and led to the dismantling of many of the central components of the welfare state that had been a part of New Zealand's social and economic development from the late 1930s. Through these policies New Zealand was more firmly integrated into the global economy in a way that was thought would improve its competitive edge and internal efficiency. Improved productivity would then lead to faster rates of economic growth and improved overall financial performance. Thus, like a number of other developed western countries during this period, state assets were privatised, new forms of management for state enterprises were introduced creating state owned enterprises (SOE's), to be run as private companies and return a dividend to the government. In the public sector new management practices were introduced bringing in a more 'corporate' style and new performance based employment contracts. The chief executives of the new SOE's and Ministries were now on an annual performance agreement that set the objectives they were to deliver over the next year. The result was a shift within the public sector to an emphasis on mission statements, goals, strategic plans and performance measures. Such practices have tended to "erode trust between managers and workers and has spawned a new industry of reporting, appraisal and "audit explosion' (Low, 2005:30).

The new regime of state practice that was created was grounded in the idea of the "market" and of the sovereign consumer. The state was "hollowed out" with central functions and activities contracted out to other agencies both private and voluntary/community based. This process led to the blurring of the boundaries of activity and policy delivery between the state, private and voluntary sectors. The state thus adopted new ways of shaping the outcomes of its policies with an emphasis on the "governance" of activities rather than their direct provision (Rhodes 1997). The state thus becomes in some ways more pervasive and controlling rather than less. This is partly achieved through the ways that new public sector management practices operate with the state assessing its performance by its capacity to commodify and displace aspects of what were previously publicly provide goods and services with either market ones or those individually arranged by "responsible citizens" (Brodie 1997, Yeatman, 1994). Under this model citizens became consumers and accountability is measured in terms of efficiency and this is interpreted as achieved through the market.

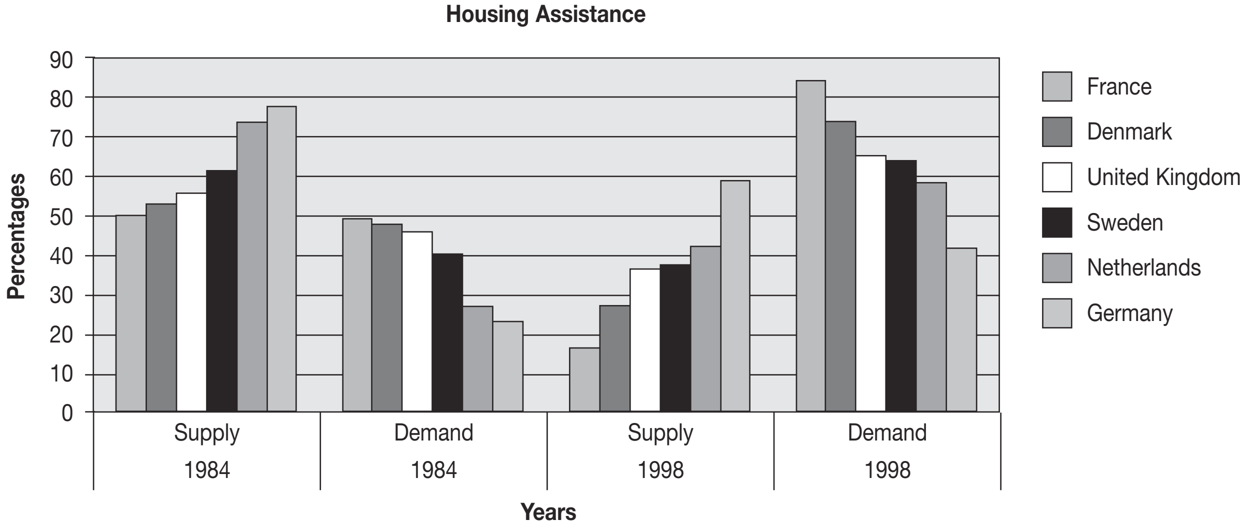
The outcome of the reforms was not as positive as the advocates had suggested Hazeldean 1998, Kelsey 1995). The reforms did not in fact deliver the greater productivity and overall improved economic conditions and increased wellbeing that was given as the reason for the extensive reform strategy. On many indicators New Zealand was in fact worse off in 1999 than it had been in 1984. The initial impact appears to have been had been to depress rather than enhance economic performance with economic growth virtually static for the first 8 years of the reforms only recovering in 1992 which though above the pre reform rate of 2.7% annually was at (3.3%) still below that of our major trading rival Australia (4.2%) (Dalziel 2001). Further, New Zealand had markedly increased the differences between low and high income earners leading to a much more unequal income distribution and unemployment rose significantly in the early part of the reform period to be 10.9% in 1991. Thus by the mid-90s, considerable debate had emerged as to the net benefits of pursuing this essentially neoliberal agenda especially within the Labour Party which was now in opposition.

Housing Policies: The 1980s-1999

Housing during the time of the fourth Labour Government was not extensively reformed and there was a continuation of a mix of policies which included both supply side subsidies in the form of low interest loans to Local Authorities for housing through to housing benefits to assist with rent for low income households. Some new initiatives were added to encourage home ownership – still seen as the ideal housing option- in the form of sweat equity, and home ownership savings schemes (National Housing Commission 1988). Further the Housing Corporation, a multipurpose organization, which both 'funded' and 'provided', escaped extensive restructuring. The resistance to reforming the housing sector, at this stage, appears to have been a reflection of strong institutional resistance from the multi-purpose Housing Corporation and the sensitivity of the Labour Government to the political implications of further radical reform after 1987 (Campbell 1999, Thorns 2000). As housing was not included in the first wave of reforms, the lack of change can also be linked to the splits that occurred in the Labour Government in the late 1980s that weakened the position of the radical economic reformers within the Government.

Pressures and advocacy for change were present during the time of the Labour Government. In both the briefing papers to the incoming government in 1984 and after the 1987 election, strong arguments were made, particularly from Treasury, for a radical change to housing policy along the

Figure 1. Housing Assistance: Selected OECD Countries



lines of the reforms that had swept through the other areas of Government policy (Treasury 1984, 1987). The advocacy, in line with global trends at this time, was for a shift towards a greater reliance upon demand side intervention. Figure 1 shows the shifting pattern of supply and demand side policy interventions in housing across a number of OECD countries and shows, that in all cases, there was a progressive shift towards a greater emphasis on demand side measures over this period.

The election of the National party to government in 1991 continued the pattern of change instituted by the fourth Labour government. However some aspects were intensified. In the first budget of the new government in 1991 welfare benefits were cut in order to encourage the movement of beneficiaries into the workforce (Boston 1999:13).

Housing was also in the sights of the new government for reform. In 1992 *The Housing Restructuring Act* was introduced. This changed both the administration of housing, and the nature of support provided. The Housing Corporation created in the early 1970s, as a multi purpose state organization, was abolished. Responsibility for policy advice was separated from the delivery of housing services. Thus the recently created Ministry of Housing (1988) assumed a more significant role and became the sole source of policy advice. The management of public housing was transferred to a new entity called Housing New Zealand (HNZ), which had the main responsibility of managing the state rental stock. A new form of income assistance was introduced as the principal means of assisting low income people into housing, the Accommodation Supplement (AS)(1993). This was a targeted measure of assistance delivered through the new agency that was created for the management and administration of all state welfare benefits Work and Income New Zealand (WINZ). The administration of the Accommodation Supplement was thus taken away from a specific housing related entity and placed within the general framework of targeted income assistance support. The Accommodation Supplement was based on income and assets tests and could be utilized for assistance in meeting the cost of state or private sector rental or towards home ownership. In order to bring greater efficiency and competition between the rental sectors the rents for state houses were set to rise in three steps to market rents. Those who were unable to pay these rents, as they were in excess of 25% of their income for rental or 30% of their income for house purchase, would qualify for the Accommodation Supplement. The government argued that the cost of the Accommodation Supplement would be equivalent to the current expenditures on income assistance for low-income tenants. However, over the course of the 1990s the cost of the Accommodation Supplement rose steeply, as it was an uncapped allowance, and thus responded to the relative cost of housing and income levels (Campbell and Thorns 2001, Waldergrave 2002). One of the consequences of the cutting of a series of welfare benefits (unemployment etc. in the 1992 budget, was that the number of low income tenants in receipt of Accommodation Benefits and then the Accommodation Supplement grew. The cutting thus did not achieve a net reduction but rather created a transfer of people from one set of benefits to another (Higgins 1999, Murphy 1999).

The Accommodation Supplement was expected to increase choice, as it was available across all sectors and for both rental and ownership. Its advocates thought it would reduce the marginalisation of State beneficiaries, as it gave them greater choice, as they were no longer locked into State housing. The Accommodation Supplement was also intended to increase the supply of rental housing as landlords obtained improved returns and thus would be encouraged to investment more in the sector. Improved quality and competition created as a result of these moves to 'market forces' were expected to create a better supply of housing and a more competitive pricing structure.

The reforms thus addressed the limitation of choice through extending the range of options for low-income households and the problem of creating an adequate supply in areas of high demand. However, the outcomes found were not consistent with expectation. The supplement went largely to those already on other benefits such as the unemployment, sickness, and domestic purposes benefits, or on National Superannuation. Further, the majority went to existing Housing New Zealand tenants as their rents moved upwards towards market rents (Colmar Brunton 1996). Little of the money went into home ownership, so the idea that the AS would be available across a range of tenures did not eventuate. As part of the overall package of change, reflecting a desire to 'privatise' public assets, the government decided to sell down the public housing stock. In 1992 when HNZ was formed it had 69,928 state houses. However, by 1999 the number had been reduced to 58,866 through the sale policy.

The net effect of the changes to housing policy brought in with the 1992 reforms, were to increase rather than decrease housing related poverty through increasing the proportion of household income going on housing costs (Murphy 1999, Thorns, 2000). The level at which the Accommodation Supplement was paid out did not provide a sufficient level to compensate for increased rents, in either the public system, where the levels of rent, moved to market rate, or the private sector. Nor did the expected expansion of the housing stock take place. However, housing is not just about rent levels. People have commitments to both the house as this is their store of memories and meanings that combine to create their sense of "home", and to their local neighbourhoods and communities (Perkins and Thorns 1999, Low 2005). What this shows is that housing markets are slow to adjust, as it takes time to create new forms of stock. This was shown by the difficulties faced by HNZ in its attempts to release housing that was under occupied. Houses, under this new policy, for example occupied by single tenants and couples were now subject to steep rent increases as they moved to 'market rents' rather than being based on tenant income. The lack of smaller units meant that many were unable to move but had their rents rise and thus an increased proportion of their income consumed by housing which contributed to increased levels of poverty. The other problem that arose was the constantly increasing level of expenditure on the accommodation supplement, which started at $340 million and rose to over $800 million by the end of the 90s. This led to demands for even greater targeting to contain the cost of welfare benefits (Campbell and Thorns 2001).

During the 1990s research into the housing system was substantially reduced within the public system. The National Housing Commission was abolished in 1988 and with its demise the research programme that it had supported ended. Within Government the new Ministry of Housing was interested only in research which examined aspects of the operation of the Accommodation Supplement. Wider questions were not addressed so significant housing research capacity was lost. Research continued within the Universities but this was not closely linked into the policy process and, for the most part, was critical of the reliance on the Accommodation Supplement and drew attention to the way that housing costs were contributing to the growth of household poverty. Also action groups were active in trying to shift policy and organize resistance to the rise in rents to "market rates" and the levels at which the Accommodation Supplement was being paid. These various forms of critique and action found new support when the election of 1999 brought a centre left coalition government into power. The return of state house tenants to an income related rents regime emerged as one of the "pledges" given during the 1999 election campaign by the Labour party. Honoring this pledge provided Labour's housing policy with its initial direction.

Changing Political Agendas 1999-2005

The 1999 election brought into office a centre-left coalition government of Labour and the Alliance (a slightly to the left of Labour grouping[1]). The new government marked out a rather different approach to economic and social policy. In respect to economic policy, they created a Ministry of Economic Development, which indicated a return to a more pro-active stance with respect to government policy. However, they still maintained a strong commitment to the need for fiscal balance and to the global free trade agenda that necessitated the creation of competitive international markets[2]. They actively sought to encourage innovation, and the growth of the knowledge economy. The prime objective of economic policy was still to create economic growth and a competitive internal environment. Markets were not ignored, but still held a central place in this economic strategy. The move to evidence based policy is seen as one of the corner stones of the new government social agenda and here they are drawing upon a 'third way agenda'

In New Zealand, unlike in the UK under the Blair Government, although there was no specific definition of what counts as evidence, there was a similar incorporation of a broad spectrum of ideas into the understanding of the evidence base for social policy. It includes rigorous new research carried out by experts through to community and stakeholder consultations around specific areas of policy development. It mixes those who are inside and outside of Government and looks to create a pool of social scientists that have policy analysis as well as applied research and evaluation skills. One result of the loss of expertise and capacity arising from the policies of the 1980s and 1990s was that there was a "capability" problem and a lack of experienced researchers to respond to the changed environment. This has led to increased attention on how to rebuild capability.

The shift towards the 'evidence-based-policy' formulation has had a number of significant impacts upon the social science sector within New Zealand increasing demand for social researchers and creating a strong growth in the demand for and use of 'evaluation" research within Government. In respect to housing policy this shift has also been significant and has led to the creation of new research, evaluation and policy development capacity.

Impacts on Housing Policy

In the election campaign of 1999, one of the pledges that Labour made, if elected, was that they would return rents for State house tenants to an income related basis. Therefore, in 2000 the Housing Restructuring (Income Related Rents) Amendment Act was passed. This particular piece of legislation reintroduced income related rents for State house tenants, and prevented the further sale of any more public rental stock. The allocation of state rental was to be based on need, thus criteria had to be developed and allocation procedures put in place. A further change was in the organization and administration of housing with a new entity to be created. In 2001 the Housing New Zealand Corporation (HNZC) was formed to replace the Housing New Zealand (HNZ) and the remains of the old Housing Corporation. The new organization had a broader mandate than simply managing the state rental stock. It was once again to include a policy and research capacity. This was to enable the identification of future needs and ensure that the housing sector in general was well placed to provide affordable, decent housing to New Zealand families now and in the future. However, the policy role is divided between HNC and the Ministry of Housing which, was re named the Department of Building and Housing in 2004, and given a focus around regulative aspect of building and a continuing responsibility for the management of the residential tenancies legislation.[3]

[1] Alliance was made up of New Labour, the Greens, Liberals (former Social Credit and Mana Motuhake.

[2] Labour for example is currently neogiating a Free Trade Agreement with China – among the first of the OECD countries to do so.

[3] The Department was established on 1 November 2004 when the Ministry of Housing was renamed the Department of Building and Housing, and building policy functions were added to its role. On 30 November (2004) the functions of the Building Industry Authority were added. A range of other functions will also be added over a 14 month period.

Table 1 Home Ownership Trends

	1991	1996	2001	2006	2011	2016
% Home Ownership	73.80	70.70	68.00	65.80	63.70	61.80

Sources DTZ 2005.

Table 2 Projected Numbers of Owned and Rented Households

	2001	2006	2011	2016
Owned	978,860	1,021,120	1,050,010	1,080,090
Rented	461,440	531,880	597,980	667,930

Source DTZ 2005.

The new organization was to be a socially responsible agency and no longer had to make a profit. In the future government would compensate the Housing Corporation of New Zealand for loss of income created through the new income-related rents policy. Further, the stock of public housing was once again to rise with the government putting in place a scheme to purchase, lease and build further public housing. The new regime of income related rents, initially aided about 40,000 state tenants (Murphy 2003 a and b). The measure was a targeted one and took into account both the income of partners and any income from savings. Once they were over the income and assets thresholds set, rents were then adjusted to market value and assistance was similar to that provide under the Accommodation Supplement to non state tenants. This policy brings in a degree of fairness in the assessment of state and non state tenants and thus reflects the desire within the policy for horizontal equity.

The second major initiative of the new government was the development of a National Housing Strategy. The development was guided by a steering group in which Housing New Zealand Corporation was the lead agency, but also included representatives from Treasury, Department of Prime Minister and Cabinet, Ministries of Social Development, Housing, Health, Pacific Island Affairs, and Te Puni Kokiri[4]. A series of stakeholder groups were established to consider a range of topics including the development of home ownership, research capacity, needs of youth, Maori etc. A draft strategy was presented to Cabinet in December 2003 with the period of public consultation from March through April 2004 before the final strategy was released in May 2005.

One of the key features of the new housing strategy is an explicit recognition that housing is an instrument of social and economic policy, and thus must have a wider range of components than simply demand side income supplementation. The document recognizes changes in home ownerships rates, affordability, and demographic changes, particularly the pattern of household formation and the growing number of younger Maori and Pacific peoples. The fall in home ownership rates was particularly amongst younger age groups and low in come households. For these groups normal loans from trading banks were not bridging the deposit and income gap thus Government intervention and support was seen as necessary to provide a way for low income families to achieve the New Zealand ideal of owner occupation.

The home ownership rate over the ten years from 1991 to 2001 has fallen from 74% to 68% (see table 1) and is predicted to fall further through to 2016. This is particularly apparent in the 25-44 year old group with a 44% decrease in homebuyers amongst this group (Housing Strategy 2004:37) and within this group low income households have experienced the greatest reduction. A range of implications for housing policy and wider social policy arise from this decline, given that home ownership is still seen as the desired housing outcome by the majority of the population and is still strongly endorsed by government. Perhaps the most significant is the increased demand that will be created for rental accommodation with an expected increase of over 200,000 units needed by 2016. The rental market in New Zealand is largely made up of small operators, many of whom have seen real estate as an investment and capital asset rather than as a long term rental activity and thus tend to spend little on maintenance and improvement.

Table 3 provides data on the affordability index (see Table 4) for the twenty years from 1981-2001. The index shows how shifts are related to changes in incomes and house prices. House prices rose more strongly than incomes from 1981 to 1986 leading to a greater proportion of household income going into housing. From 1986 through to

[4] Te Puni Kokiri is the name for the Maori Development Ministry. Since 1980s New Zealand had been developing a “bicultural” partnership with the indigenous Maori population based on the Treaty of Waitangi signed in 1840 between the Crown and Maori chiefs.

Table 3 Social Rented Housing

Social Housing Tenure					
Year	**1981**	**1986**	**1991**	**1996**	**2001**
Housing New Zealand	56,979	56,091	63,552	52,671	52,500
Local Government	16,158	16,653	15,420	14,781	14,115

Sources DTZ 2004.

Table 4 House Price Affordability*

Region	1981	1986	1991	1996	2001
Auckland	34.3%	50.1%	38.9%	45.0%	37.3%
Wellington	24.9%	45.2%	35.8%	30.6%	30.0%
Nelson/Tasman/Marlborough	33.9%	53.4%	41.1%	38.7%	33.3%
Canterbury	24.4%	44.3%	37.5%	35.9%	29.8%

Source DTZ 2004.

**Affordability Index assumes a 25% deposit and represents the proportion of the median household income required to service a 25 year loan on the balance of the median sale price. The higher the index the less affordable the property as it requires a higher percentage of gross household income to service the debt. (DTZ New Zealand 2004:149).*

2001 the index shows that for all but Auckland there was a steady improvement in affordability. However from 2001 there has been a strong housing boom with prices rising much more rapidly then incomes leading to a decline in affordability and a rising proportion of income being required to meet housing costs. This has raised the current concern for affordable housing especially for those entering the market for the first time and those on below average incomes. The highest annual increase was in 2003 with a 23% rise, falling to 14% in the year June 2004-2005. These increases were well ahead of both the inflation rate and the level of wages increases obtained over this period. Both of these were under 3%.

In the post 2001 pattern there are a number of regional 'hot spots' where prices have risen even faster than the overall average. One example is the Nelson region at the top of the South Island sustaining house prices rise increases of 59% from 2003 to 2005. Here growth in prices has been stimulated by overseas buyers attracted to the region by its location and where access to cliff tops and water is still available at globally relatively modest price levels. Auckland as New Zealand's largest city, with strong growth from migration, also continues to be a housing market where affordable housing is difficult to find and provide. Around 70% of the new construction required for both rental and home ownership through to 2016 is expected to be in the Auckland region.

The net effect of these recent changes in affordability has been a decline in housing options especially for single income and beneficiary families and an increased pressure upon the Government to become more interventionist to assist these disadvantaged groups. For example a Salvation Army sponsored report in 2005, advocated a range of additional strategies for low and modest income families to obtain home ownership. These included shared equity, a 'right to buy policy' for the sale of state houses to sitting tenants, a new government supported savings scheme and a scheme for government leasing, at a discounted price, of government owned land in high housing cost areas for key workers (Smith and Robinson: 2005).

National Housing Strategy

The new National Housing Strategy is underpinned by a vision "that all New Zealanders will have access to affordable, sustainable, good quality housing appropriate to their needs" (NZ Housing Strategy 2004:19). The document, then identifies nine principles that will guide and influence future housing policy. These principles range from the recognition of the pivotal role of housing to provide shelter, which is seen as a basic human need, through to the fact that decent housing must be affordable and of good quality and an acknowledgement of the increasing diversity across the population. Further the policy identifies two direct roles for the government. The first is to regulate the housing market and housing quality and the second is to provide assistance to low-income households having difficulty accessing affordable and suitable housing. Both of these shifts in thinking arise from the perceived failures of the single demand side subsidy offered via the Accommodation Supplement to address the needs of lower income households to find adequate housing. The policies are intended to meet this objective have been the assistance delivered either through state rental, which as we noted earlier, has been once again increasing over the past five years, and income supplementation through the Accommodation Supplement. In addition to this, the government has also piloted a home ownership insurance scheme through the newly created Kiwi bank and has provided some funding to stimulate activity by local government and other community based social housing providers especially Maori iwi[5].

The government's housing policy identifies as one of its tasks to "actively explore the potential of a variety of interventions to deliver good housing to meet the specific needs of targeted groups and markets". This clearly marks a significant shift from the hands-off approach of the previous period of housing development during a more market-oriented neo liberal phase of government and a retreat from income supplementation as the sole form of housing support.

The final principle identified in the vision statement is the need for housing policy and interventions to be informed by "solutions focused evidence based research". In order to achieve this, the Centre for Housing Research Aotearoa New Zealand (CHRANZ) was established in August 2003. The mission of the centre is to "invest in rigorous, independent and relevant housing research to support policies and practices that meet New Zealand's changing and diverse housing needs" (NZ Housing Strategy 2003:58).

CHRANZ has since its inception funded a range of research projects into the New Zealand housing system and the links between housing and social, economic and environmental outcomes. In the 2004-5 year CHRANZ has funded research into Tenure Aspirations, Affordable Housing, Maori Housing experiences and a project investigating the future shape of housing.[6] This work is seeking to build an improved research base and understanding of the dynamics of change within the New Zealand housing environment. In the 1980s and 1990s, under the more market-based analysis and policy-making that took place, at this time, systematic research into the housing system was largely neglected and the internal capacity of the government housing sector to carry out research was run down. Thus one of the challenges for the new Centre has been to regenerate capability within the housing research sector.

New Forms of State Practice

In reviewing the housing sector during the last five years it is clear that significant changes have taken place in policy-making, the research environment and in the stance of the New Zealand state to intervention in housing policy. The changes to state practice have been seen by some as a retreat from neo-liberalism, with its sole reliance upon markets and demand side, consumer subsidies, as the solution to providing modest and low income households with access to affordable and decent housing. What is emerging to take the place of these limited solutions is recognition of the need for a broader range of policy tools. However, much of this is still to be achieved in the future. The New Zealand Housing Strategy identifies a range of areas that are under review and the 2005 budget introduced a new "kiwi" savings scheme. The scheme is a voluntary work-based savings scheme due to start in 2007 to help New Zealanders save. Savers are able to select their own funds and can change providers giving opportunities for banks and other financial institutions to play a role in the scheme. Savings are primarily for retirement and lock in until the age of eligibility for New Zealand Superannuation is reached, currently 65. The Government will offer an upfront contribution of $1,000 per person to be 'locked in' until the recipient reaches the age of eligibility for NZ Superannuation or for five years. After three years of savings the Government will offer to the savers a first home deposit of $1,000 per year of membership of the scheme up to a maximum of $5,000 for five years. This means that eligibility for the home owner loans would not be until 2010. The government during 2006 will develop a list of approved providers and the scheme will be regulated by a trust deed similar to registered superannuation schemes. Further details of the scheme will be developed with the approved providers, once these have been determined, prior to the schemes start date of April 2007. Critics of the scheme have suggested that the likely contribution to addressing the current housing affordability problems are slight and that the future contribution is dependant on the behaviour of the market over the next 5 years.

The new form of state practice is something thus of a hybrid as it continues a number of the key policies from the neo-liberal reform period particularly the accounting, transparency, contractual and reporting requirements which tend to disaggregate policies and programmes and thus work against the whole of government emphasis which is supposed to be more central now within policy development. It also reflects a shift from direct provision to an emphasis on partnerships and thus to the "governance" of activities through a range of strategies including outsourcing , contracting and forms of quality control that maintain the capacity of the state to "steer" the system.

Further the commitment to a greater level of local partnership models and an increased emphasis on evidence and research to underpin policy and the empowering of local communities is still largely within a framework of government contracting. Thus in many cases, this does not represent a significant shift in power and control but increases the level of surveillance and management that central government has over local activities (Larner and Butler 2003; Saville-Smith and Thorns 2001).

5 In 2003 the Government allocated $63m to a 4 year programme of social housing demonstration projects to be developed in partnership with iwi (Maori tribal groups), third sector housing providers and local government.

6 CHRANZ research completed and currently being carried out can be found on its web site.www.chranz.govt

A desire to encourage greater participation by local government and third sector and the Kiwi (Maori) authorities in housing delivery is present at the policy level. The state no longer wishes to be the sole or only provider of social housing. This is clear in the housing strategy document, where they talk about and look for ways in which others can be incorporated into the mix.

The present emphasis on evidence based policy formation and the idea of focusing on what works has become a significant part of the new pattern of state practice. The government convened major policy and evaluation conferences, have been key show cases for this new policy thrust and have centered on bringing together the research, policy-making and community sectors to discuss ways in which they could work better together, sharing their knowledge and expertise. However, limited debate has emerged around what counts as evidence, which is a critical component of such arguments.

The major changes in housing policy that have been identified are part of a broader set of initiatives that are currently reshaping state practice around new forms of partnerships and an emphasis on evidence based policy formulation. The debates surrounding the move to the Accommodation Supplement in 1992 were mostly around the extension of the neo-liberal agenda to housing and the shifts in international practice. It is an interesting comment on local knowledge that the consultants appointed to design the Accommodation Supplement in 1991-2 were drawn from the USA (Thorns 2000, Campbell 1999, Murphy 1999, 2003a). By 1999 there was an evidence base for the argument that the Accommodation Supplement, far from solving the problems of the former housing policy regime, would create a greater amount of housing related poverty and not substantially increase housing choices. However, it was a political decision – the campaign pledge by Labour to restore income related rents for state house tenants - that created the first post 1999 change. Subsequently housing has been incorporated into the wider 'social development" agenda of the Government and has been linked into a social development strategy with its underpinnings of an "evidence based" approach.

Housing policy in New Zealand is increasingly being framed around questions of future housing and embracing more than the state sector with the idea of creating new forms of public/private partnerships. Further future growth in the not for profit sector is seen as necessary to expand the options for lower income households which are not seen as a key target market for the major trading banks. Social housing, in terms of publicly built and rented housing is only one small component of such a strategy. Macro economic policy and a wider set of interventions into both the demand and supply of housing are now on the table. Government though is not returning to the pre 1984 position of being itself the major provider. The new preference is to be a facilitator of others through partnering and providing guarantees and looking for more flexible forms of assistance that recognize the increasing diversity within New Zealand in both life courses and in its population and household structures. The success of these new directions will need to be assessed over the next 5 years as the Government seeks to implement its new housing strategy

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Home Loans – Recent Trends in Sri Lanka

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There is a rising demand for home loans in Sri Lanka. The market has grown at a compound rate with the escalation of per capita income and changing patterns of consumption and saving habits in the recent past.

Sri Lanka is an island situated in the Indian Ocean with a population of 19 million. Its GDP has been growing by an average of 6% for the last 3 years. GDP per capita stood at US$1,200 in 2005. The Colombo Consumer Price index - the official price index to measure inflation – showed growth of 11.1% in the year to January 2006 compared to 8.8% one year ago. The overall rise in consumer products and the rise in international commodity prices contributed to domestic inflation during 2005. The unemployment rate, which is around 8%, has remained unchanged for the last 3 years. In the banking and financial sector, the Average Weighted Price lending Rate (AWPR) of commercial banks stood at 12.1% in January 2006. However, during the same period, the Average Weighted Deposit Rate (AWDR) remained as low as 6.34%. The rate of interest charged on housing loans currently varies from 11% to 15%. These spreads suggest that the banks in Sri Lanka keep very high margins even for secured lending.

The key factors triggering the progressive growth of home loans on the demand side are:

a) Declining interest rates over the past year have encouraged investment in properties rather than in low income yielding government securities and term deposits.[1]

b) Rapid rises in income in the private sector, which makes housing more affordable. Increasing income levels have shifted consumption to areas such as housing.

c) Tax benefits extended to borrowers, which have further reduced the effective cost of borrowings.

d) The demand arising from migrant workers and Sri Lankans residing abroad. Many Sri Lankans residing abroad prefer to invest in housing in Sri Lanka, as an alternate means of investment. Migrant employees who work and reside abroad, desire to have a house of their own in Sri Lanka once they return to the country. Therefore they invest their hard-earned money on real estate for two specific reasons: first, the return on investments is comparatively high due to the appreciation of prices; second, they cannot expect a real positive return on their bank deposits due to negative interest rates prevailing in the country.

Certain factors on the supply side have also supported growth in housing finance. They are:

a) Emerging competition in the housing finance sector between lenders; this has resulted in lenders charging lower rates of interest and offering more and better facilities.

b) An increasing number of new entrants to the housing finance market such as foreign and local commercial banks.

c) The introduction of several new products by lending institutions to meet the needs of a wide variety of customers . Floating rate mortgages, branded housing loan products and expansion of loan portfolios by lending institutions by way of securitization, are new to Sri Lanka.

d) Increasing collaboration between lending institutions and housing developers. Such collaboration minimizes legal issues relating to mortgages, thus making it easier to purchase a property. In Sri Lanka, housing loans are mostly obtained for individual house building. The development of land by developers and condominiums are rather new in Sri Lanka. In the case of developers who develop land for sale, banks are now in collaboration with them to ensure clearance of title for the entire land so that the bank need not clear title for each block. This has minimized legal issues for individual house builders.

e) Introduction of home loans at floating rates which have become popular among borrowers, since the cost of borrowing at short term rates is comparatively less than long term fixed rates. This is mainly due to the perception among borrowers that they could enjoy lower short-term rates as the variable rate product is new to Sri Lanka.

[1] In Sri Lanka the real return on savings is currently negative: i.e. – the rate of inflation is higher than the interest rate on deposits. Therefore, people prefer to invest in properties.

Demand for Housing

The annual demand for housing in Sri Lanka is estimated at a rate of 80,000 to 100,000 units. This number is expected to substantially increase in the future. In addition, there is a growing demand for condominium units in the Western provinces of Sri Lanka from expatriates and Sri Lankans residing abroad.

The construction of high-rise apartments has become a lucrative business and the number of such buildings in the city area is increasing rapidly. The Apartment Ownership Law No 11 of 1973 has been amended by Act No 45 of 1982 and further amended by Act No 39 of 2003 giving more and more authority and flexibility to apartment owners and lenders.

There are a large number of houses all over the country which require upgrading. The latest figures published by the Department of Census and Statistics have put the number of fully and partially damaged units after the Tsunami at 77,561.

Major Players

State owned institutions play a major role in the housing finance market in Sri Lanka. Traditionally, the housing finance market has concentrated on State funded sources since housing development strategies in Sri Lanka have been mainly initiated through State owned institutions. The Government concentrates mainly on affordable housing for low and middle-income earning groups. This policy includes subsidized housing loans, participatory housing schemes for low-income groups and apartment complexes in urban areas for middle-income groups. In urban areas, shanties are cleared and the land is released for development of apartments for shanty dwellers. The income derived from the acquired and released land would be sufficient to construct apartments for shanty dwellers who abstain from the right of living on the land acquired.

State owned lending institutions include State Mortgage & Investment Bank (SMIB), Housing Development Finance Corporation (HDFC), National Housing Development Authority (NHDA) and the National Savings Bank (NSB). These institutions have a combined market share of 65 % of the housing finance market.

However, Government sponsored housing finance strategies have become more and more non-viable due to the non-availability of government funds for these institutions. The government now realizes the need to develop a self-sustaining housing finance market with the participation of private institutions.

Currently, state owned commercial banks and local and foreign private commercial banks which have aggressively entered the housing finance market, play a major role in these activities. For example, NDB Housing Bank Ltd. (NDBH) commenced its operations in 2001 as a bank specializing in housing finance and is the only specialized private sector housing finance institution at present. NDBH is an extremely small entity with an asset base of US$ 14.5Mn and a market share of around 2%. Therefore it is yet too early to evaluate its performance.

In addition, certain micro-finance institutions introduced housing loans to their members as a part of an attempt to develop the living conditions of the poor. This scheme is becoming more and more popular among the members of such communities, as the processing of loans is less cumbersome when compared with that of traditional housing finance. Micro-finance institutions release loans to their members for housing purposes only on a group guarantee. The cumbersome documentation procedure of title reports, extracts, approved building plans, etc is not followed and no mortgages are involved.

Source of Finance

Housing development lacks Government funding due to budgetary constraints. Consequently, activities of institutions such as the National Housing Development Authority are confined to recoveries only. Other State owned institutions such as SMIB and HDFC depend on deposit mobilization and funds borrowed from the debt market for their mortgage market activities. In contrast, the NSB funds its housing finance operations by deploying 100% of its own mobilized funds. NSB's current strategy for enlarging its retail portfolio has helped its housing finance operations immensely, as it is one of the viable and productive areas of finance that the NSB is permitted to operate, within statutory limits. Most commercial banks deploy their own mobilized funds for housing finance operations. Although the AWDR in Sri Lanka is around 6%, the current lending rates vary from 11% to 15%, demonstrating a wide gap between deposit terms and loan terms. However, the banking community claims that high margins are due to taxes on banking operations such as corporate tax at 35%, VAT on certain banking operations at 20% and stamp duty etc. The other main contributory factor is the high non-performing loan (NPL) ratio currently prevailing in Sri Lanka.

Since the debt market is not yet adequately developed, access to long-term funds for housing finance still poses difficulties. Most banks use short-term funds from savings and current accounts and deploy these funds to disburse long term housing loans, thereby creating an asset-liability mismatch. In Sri Lanka, the Central Bank does not specifically require lending institutions to prepare a duration gap analysis periodically, in order to verify their asset-liability mismatch. Although there are no specific regulatory provisions, the Central Bank of Sri Lanka nevertheless continuously monitors the asset liability mismatch of banks in order to ensure their liquidity.

The Employees' Provident Fund (EPF) provides housing loans to its members through State banks, retaining the fund balance of members as collateral. There has been a steady demand for loans under this scheme since loans are granted purely on the recommendations of the EPF. The main drawback of this scheme is that borrowers use the EPF loan scheme to make early withdrawals from their Provident Fund balance, which would otherwise become available to them only on reaching the age of 55 years.

In order to overcome the lack of funds for long term housing loans, housing finance institutions could develop credit instruments backed by their mortgage portfolio, thus enabling lending institutions to issue mortgage backed securities to raise long term funds. HDFC has already issued Mortgage Backed Notes to raise funds from the debt market. However, the absence of a proper legal framework, the lack of uniformity in arranging such notes, and the lack of understanding by the players are some of the hindrances in developing a secondary mortgage market in Sri Lanka.

Loan Products

Most loan products offered are fairly standardized because the demand for loan products is mostly uniform.

The common features of currently available housing loan product are shown in the table below.

The attempt made by certain lending institutions to add value to loan products has not been a success due to lack of demand for such value additions. For example, some lending institutions offered a loan package that includes building materials at a discounted price, but the response to such schemes has not been encouraging.

Cross selling of products and services to the prospective borrowers is also not very popular in Sri Lanka. In the Indian market, on the contrary, cross selling is very popular. For example, a person looking for a housing loan is also offered a life insurance, home protection insurance, personal loans and other banking products.

Going beyond standardized housing products, the National Savings Bank offered to its customers loans for the improvement of their living conditions. They could get finance from the NSB to beautify their houses through new furniture, landscaping, curtaining, air-conditioning etc. As a result, a bare building could be converted into a home by furnishing, landscaping, curtaining and providing many more extra facilities such as hot water, air conditioning, internet connection etc. NSB also offers loans to existing home loan customers, for personal consumption purposes such as education, health, purchase of consumables and motor vehicles.

Fixed or Floating Rates of Interest

Most new entrants to the home finance market have introduced variable interest rates on housing loans. The interest rate, the financial cost of the loan, is not fixed during the tenure of the loan. Instead, the interest rate is benchmarked against a certain index. As the benchmark rate moves up or down, the cost of the loan too changes at pre-determined intervals, usually once a month or quarter. The interest rate on floating rate mortgages may be re-set at predetermined intervals, on either monthly or quarterly basis, so that the interest component either goes up or down depending on the movements of the benchmark rate. The borrowers could be at a risk in instances where the rate of interest goes up.

Most government banks still follow the fixed rate system for home loans. Although it is a fixed rate, the lending bank enjoys the right to change the rate at its discretion, even upwards. Practically this does not happen in Sri Lanka.

There are three important factors which one needs to consider before opting for one type of loan over the other. The long-term expectation of interest rates is the first and most important determinant that needs to be considered when opting for a particular type of loan. If one expects rates to rise in the first years, but then decline gradually over the following years, a floating rate product would be preferable. The other option of going in for a fixed rate product and then switching over at the end of the year will entail additional costs such as prepayment fees and may not make financial sense.

The attraction of a floating rate home loan is that it is not subject to pre-payment charges. This would appeal to individuals who expect lump sum money, which could be used to reduce their loan exposure.

When considering a fixed rate home loan over a floating rate loan, the important consideration for the customer is that if the interest rates were to rise, he would be protected from the interest rate risk.

Fixed rate loans are generally priced higher when compared with floating rate products. The difference in interest rates depends on the long term expectation of interest rates. If the borrower thinks that the rate will move up only to the extent of the difference, he will be indifferent to the options available. The deciding factors then, should be when he thinks the rates will increase, and also the long term expectations of interest rates.

In conclusion, there is no exact answer to whether one should go in for a floating or a fixed rate loan. It is a business decision that should be taken by the borrower. However the guidelines given below would help borrowers to arrive at a decision. In a falling interest rate scenario, it is always advisable for the borrower to go for a floating rate

Loan to value ratio	Security	Rate of interest	Duration	Upper age limit	Method of Recovery
75% of Forced Sale Value or purchasing price, whichever is lower.	Primary Mortgage	Fixed Term	15 to 20 years	65 years	Equated monthly instalments calculated on reducing balance.

mortgage and in a rising interest rate scenario, to go for a fixed rate and lock on a long-term contract. If the borrower intends to fully settle the loan prior to the agreed term of the loan or make lump sum payments without a penalty, the floating rate mortgages are more appropriate since there are no pre-payment damages involved. The lenders of floating rate mortgages will lift or lower the interest rate taking into account the movements of the market rates which results in the borrower having to pay more or less than the originally agreed amount. Therefore if the borrower prefers to pay a fixed amount during the tenure of the loan, a fixed rate mortgage would be more advisable. When the rates are relatively low in the market compared to the historical information, it would be advisable to go for a fixed rate in order to enjoy lower interest rates on long-term basis.

Collection Ratios and Provisioning

Collection ratios of housing finance institutions in Sri Lanka are estimated to be in the range of 80 – 95%. In certain cases the non-performing loans (NPL) ratio is around 20%. The following reasons have been attributed to such high default ratios:

1) Political interference in granting loans.
2) Defaulted loans being written-off by successive governments.
3) Lack of credit information and credit ratings.
4) Inefficiency in government-owned banks.
5) Loopholes in regulatory provisions in taking action against defaulting customers.
6) Social and cultural problems, eg auctioning of a residential house could be difficult due to social pressure.

However, NPL ratios of most lending institutions are relatively better, since the majority of NPLs fall in the 3 – 6 month category and the 6 – 12 month category. The NPLs falling within the loss category, ie over 18 months, are relatively low.

Most banks follow the provisioning direction mandated by the Central Bank. Currently Licensed Commercial banks and Licensed Specialized banks are mandated to provide 20% for sub-standard category, 50% for doubtful category and 100% for the loss category after deducting the realizable value of the collateral giving due consideration to the minimum haircut of valuation and the age of the NPL.

Tax Incentives for Housing Finance

Taking into consideration the grave need to construct sufficient houses for the country, the government has introduced incentives to housing lenders, borrowers as well as to property developers. The Budget for 2004 reduced the corporate tax rate applicable to specialized housing finance lending institutions to 20%. Tax concessions are also available for individuals who obtain loans for specific housing purposes. Accordingly, interest paid on housing loans could be deducted from statutory income in the tax declaration. Concessions are also available for individuals on capital payments of housing loans and the rental income received subject to limitations.

Parate Rights

Parate rights, ie the right to execution whereby lending institutions can sell debtors' mortgaged assets without intervention of the court, have been accorded to some selected lending institutions by the Central Bank. Banks that do not fall under this preferential treatment complained about this regulation, pointing out that they would be discouraged from entering into the housing finance business.

Issues in Developing the Housing Finance Sector

The enforcement of Parate Execution rights do not seem to be very effective. Social and political pressure has been brought upon state owned banks to abstain from Parate action. Even after the execution of Parate rights, lending institutions are sometimes hampered in their efforts to obtain possession of such properties. The existing Parate regulations do not entitle the banks to obtain possession of foreclosed property. Therefore the lending institutions need to seek assistance from the courts which is a lengthy and time-consuming procedure.

In order to protect the interest of lenders, it is highly recommended that suitable amendments should be made in order to include the right to obtain possession of mortgaged property without intervention of the courts.

The high rate of stamp duty on the purchase of property has also become a serious problem to borrowers. If stamp duty rates could be reduced, buyers will be motivated to declare the true buying prices to lending institutions.

On the positive side, the government has extended tax concessions to individuals as well as to lending institutions which are dealing with housing loans. The recent amendment to the Rent Act No7 of 1972 which was originally in favour of tenants has drastically removed the problem encountered by house owners with regard to renting of houses.

Conclusion

Recent experiences demonstrate that the formal housing finance sector continues to be elusive to the lower income groups. This needs to be addressed by the government by introducing concessionary housing loan schemes for low-income groups, credit guarantee schemes and re-finance schemes for housing finance lending institutions.

Further efforts of the government are required to strengthen foreclosure laws and land records. It would also be inevitable that expansion of mortgage insurance and credit bureaus should be encouraged.

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Local Authority Housing Policy in Japan: Is It Secure To Function As Safety Net?

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1. Introduction

In the post-war period, Japan experienced rapid economic growth and public bodies spent large amounts of money on large-scale developments of community facilities and motorways. Public bodies for housing, such as local authorities or the Housing and Urban Development Corporation (HUDC) and the Government Housing Loan Corporation (GHLC) provided housing and financial assistance, took significant roles in housing provision at that time.

However, due to changes in the social and economic conditions of the country since the 1990s, these policies are no longer suitable for many people in meeting their housing needs. As a result, Japanese housing policy is now in a phase of major changes.

Consequently, the Panel on Infrastructure Development, which is a consultative body for the Ministry of Land, Infrastructure and Transport (MILT), proposed a *New Concept of Housing Policy* in September 2003 and published the *Interim Report for the Institutional Framework of New Housing Policy* in December 2004. In addition, coalition government parties have begun formulating a new basic act for housing. The Japan Federation of Economic Organizations has also made a concrete policy proposal and recommended the formulation of a basic act for housing and the built environment. In accordance with the interim report and movements in political parties and business circles, the MILT published the *Outline of Housing Policy Reform* and begun considering major issues concerning housing policy and new reform policies.

The fundamental point of the new policies would be a market-driven housing industry that would limit public controls as much as possible. The goal of the new policy is to rely solely on the market and to relinquish government control of the housing market.

The government documents emphasize four strategic fields:

1. development of a new housing financial system based on the free market
2. improvement of the function of the private housing market
3. reform of the public rented housing system towards restructuring a housing safety net[1]
4. regeneration of the built environment for urban areas.

This paper focuses on the third strategy as mentioned above which prominently reflects the direction of Japanese Housing Policy. The first part of the paper will show how past policies have made the public housing system dysfunctional through illustrating the transformation of policy on public rented housing. The second part will illustrate the new policy and discusses the thesis that it will never bring improvement in the public housing system.

2. Transformation of the policy for public rented housing

The Public Housing Act was formulated in July 1951, and has been one of the three pillars of Japanese post war housing policy[2]. The purpose of this Act is to contribute to stability in people's livelihoods and to promote welfare by developing and allocating low-rent housing to people with low incomes in order to ensure healthy and cultured living. The Act defines the system of local authority housing. The central government subsidizes the construction costs of local authority housing that meet the uniform criteria under the Act.

At the time of enactment, there were two types of income criteria and two corresponding subsidies. Tenants with income lower than 10,000yen who were able to live in a small house received government subsidies for two-thirds of all construction costs. Tenants with incomes between 10,000 yen and 20,000 yen who were able to live in a slightly bigger house received subsidies to cover half of their

[1] Housing safety net means function to secure living for people who find it hard to get it in the market.

[2] The three pillars were the Local Authority Housing (Public Housing Act), the Government Housing Loan Corporation and the Housing and Urban Development Corporation (currently renamed to Urban Renaissance Agency).

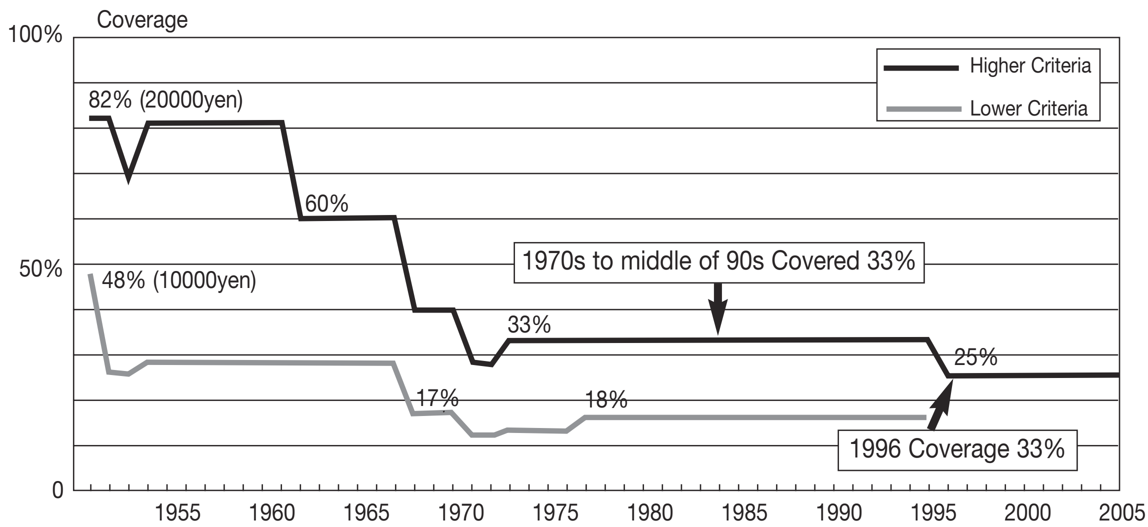
construction costs. At that time, the average income for working class men was approximately 13,000 yen. Under these income criteria, 80% of all households were entitled to local authority housing (see Figure 1).

The central government made a 3-year construction plan, to be implemented between 1951 and 1966. Local authorities were required to implement the plan. During the first fiscal year, 27,436 units were built and after that local authorities built 50,000 to 60,000 units annually. In 1961, the Housing Construction Plan Act was formulated. This Act required the central government and local authorities to make 5-year housing constructions plans and to set the numerical target for housing construction during the designated period[3]. As a result, the provision of local authority housing was promoted but its actual contribution to the plans was insignificant. For example, local authority housing accounted for approximately 7 % of the total number of houses actually provided under the first 5-year plan (1966-1970). The targets set out in the 5-year plans were achieved with the help of the private sector's great efforts. Although it seems that housing policy in the post-war period emphasized the three pillars that provided for public housing and finance, the promotion of middle-income homeowners was actually a more significant issue at this time.

In spite of the 5 year plans, the housing shortage had not been solved. The Public Housing Act 1951 was amended to restrict the entitlement of local authority housing to the lower income group because the amount of public housing provided by local authorities was limited. By 1973, the total number of households had exceeded the total number of houses. Rising land prices and construction costs made it difficult for local authorities to provide houses. As new construction of local authority housing decreased, the system was criticized for promoting inequality between people living in local authority housing and those who are eligible, but not living there. Rents in local authority housing were considerably lower than private rental rates. Tenants living in local authority housing can continue to live there unless their income grows beyond the criteria. People who were not eligible for local authority housing, had to live in low-quality private rented housing with higher rents, until they won a drawing lot to receive local authority housing[4]. In the middle of the 1970s, the income criteria were changed to allow tenants whose income levels were in the lowest 33% to be entitled to local authority housing.

In the 1980s, the entitlement expanded from family households to single households, but was limited to the elderly, physically and mentally disabled individuals, and welfare recipients. In the middle of the 1980s, rising land prices and the onset of the bubble economy made it very difficult for local authorities to provide housing. However, the increase in income levels allowed people to purchase their own housing. The need for local authority housing shrank and new construction of local authority housing decreased.

Figure 1 – Income criteria for local authority housing eligibility 1950-2005



Source: Sumimoto Yasushi (1997), Ministry of Land, Infrastructure and Transport (2005)

[3] The target set out for the first 5-year plan was 6.7million units.

[4] There has been high competition for living in local authority housing. The number of applicants has been ten times, on average, the number of vacant units even now in metropolitan areas.

Table 1 – The number of new constructions

	1985	1990	1995	2000	2001	2002	2003
PF	776,379	1,201,936	837,959	752,205	805,502	876,671	917,384
GHLC	358,335	409,292	531,661	388,706	279,628	188,734	163,392
LA	44,600	40,978	39,436	28,293	26,876	25,646	22,922
UR	20,082	17,657	16,762	14,872	11,460	9,717	7,888
Other	36,676	37,246	44,512	45,767	50,392	50,248	48,497
Total	1,236,072	1,707,109	1,470,330	1,229,843	1,173,858	1,151,016	1,160,083

PF = private finance [0]
GHLC = Government Housing Loan Corporation
LA = Local Authority
UR = Urban Renaissance Agency (Housing and Urban Development Corporation renamed)

Source: Housing construction statistics (1991) (1996) (2002b) (2003b)

In 1996, a major amendment was made to the Public Housing Act. Since then, local authority housing has been provided and managed under the amended Act. There are five significant points in the amended Act. First, the two types of income criteria have been unified and the new income criteria are tighter than in the past. Tenants with income in the lowest 25% are entitled to local authority housing (see Figure 1). There is discretionary supervision for the elderly and disable individuals. The upper limit for them is income in the lowest 40%.

Second, the rent calculation system was also changed. The rent level for each household could be set according to their income and housing conditions such as size, location, and age of the house. In addition, local authorities were required to charge market rents to higher income tenants. It was an incentive for them to get out of local authority housing.

Third, the amended Act allowed the local authorities to purchase or lease houses built by the private sector and other public housing institutions and to utilize private sector resources. Three years before the amendment, the specific high-quality apartment programme was launched. This programme allowed the government and the local authority to provide subsidies for private landlords to build high quality housing which were aimed at providing a portion of the construction costs and rental income. In 2001, another programme was enacted to subsidize well-equipped, high-quality houses, to be built by private builders and landlords for the elderly. The diversification of affordable housing has been desirable. However, the proportion of the housing stock using diversified methods has been insignificant so far. Methods are still not well designed, and local authorities and private landlords are reluctant to implement some of them.

Lastly, although the provision methods were diversified, new housing construction shrank (Table 1). Local authorities no longer provided additional units when they rebuilt existing old housing stock. The minimum ratio of new housing units to existing units changed from 1.2 to 1.0. Local authorities have not necessarily increased the size of the housing stock. Rebuilding without increasing housing numbers has restricted the increase of affordable housing.

While we have looked at several reforms of local authority housing until 1996, it is evident that these past reforms have decreased the provision of local authority housing. As a result, welfare dependent people are concentrated into the local authority housing sector. Although disadvantaged people like low-income elderly and single mother households are concentrated in local authority housing, intensive housing management and welfare services to tenants have been reduced. The past reforms have already made the local authority housing system dysfunctional.

3. New Policy on Local Authority Housing: is it really new?

The government showed in the official documents that local authorities had been playing the role of providing a housing safety net but their role has been no longer effective because demands have become varied due to social, economic and demographic changes. These changes have brought on a need for reform; the principal aim of the reform is to allocate the limited number of local authority housing fairly and effectively. It appears that the government will implement a new reform for local authority housing to work as a housing safety net.

(1) Change the entitlement for local authority housing

To ensure fair distribution, the target range would be narrowed. In order to narrow the target range, the government indicates the necessity of several measures; besides income reviews, assets and savings will be taken into consideration as well. Additionally, income criteria will be regularly reviewed. On the other hand, relaxing the entitlement is also considered. It is for individuals who need urgent and short-term housing such as victims of domestic violence or other crimes and families with children under 6-years-old. The main point of the reform is that the local authority housing should be allocated to the most socially and economically disadvantaged people.

(2) Modify the rent calculation system

As stated before, rents have currently been set with tenants' income and housing conditions. The government indicates a need to reflect on regional differences of income and rent levels and to impose much higher rents for tenants whose income is beyond the criteria in order to promote eviction.

(3) Change the subsidy system

Subsidies restricting usage on the construction of local authority housing will be abandoned. Instead, a local housing subsidy will be enacted. This new system provides subsidies for local housing, which will cover not only public housing, but also part of private housing. However, since the new subsidy will be shared between the public housing and private housing, there will be less money to be allocated to public housing. In fact, national expenditures for housing in 2005 were 20% less than in 2004.

However, this development could have a positive effect. Under the new system, local authorities are required to make a Local Housing Plan. The new plan could allow local authorities to have a stronger grip on the allocation of housing provision and related subsidies. The plan mainly focuses on public housing development, but it is possible that local authorities could have a much more significant role in achieving the comprehensive plan for housing development and management.

(4) Promote the utilization of resources in the private sector

Provisions for affordable housing would not be confined to public direct provision. For example, the Private Finance Initiative (PFI) can be used for providing and managing affordable housing, including local authority housing. In 1999, the Japanese Government passed the Act for PFI which promotes the use of the resources of the private sector (funding ability, management skills and technical capabilities) for the construction and financial and technical management of public facilities. Japanese PFIs are modeled after British PFIs. Concerning public housing, the government has encouraged new development and rebuilding of existing public housing stock by PFI. Local authorities which want to use PFI models for rebuilding the existing housing stock invite private companies to bid for rebuilding projects. However, it is not certain that local authorities can properly control private activities. In Japan, local authorities have relatively weak power when it comes to regulating urban planning and housing development. As stated above, it is a crucial point how the new Local Housing Plan can influence private activities.

(5) Link housing with welfare services

Since there are large numbers of elderly people who live in local authority housing, housing can be combined with welfare service centres to function as day care centres or nursing homes. Part of this idea has already been implemented. However, it cannot be seen that it has solved the problems because services have not always been delivered to people who really need them. There are large numbers of elderly people in local authority housing for whom it would be difficult to deliver detailed services tailored to personal needs. This shows that combining facilities like housing and a welfare service centre is not enough or not suitable for their needs.

In conclusion, it is obvious that the ideas of local authority housing reform fundamentally reinforce the wrong tendencies which were already embedded in the past reforms. It is unlikely that this new reform could improve the housing safety net effectively.

4. Current situations and the priorities of the policy

In the light of the points of the previous section, this section illustrates the problems that have occurred in local authority housing and attempts to examine how the new reform can change the situation.

(1) Concentration of disadvantaged people

The concentration of disadvantaged people is not only a recent problem. It began in the early 1960s with the second amendment of the Public Housing Act. However, it appears that the problem has rapidly progressed. There has been a growth in demand for low-rent housing due to an increase in elderly and single-mother households.

For example, look at the tenants' profile in the case of Osaka Prefectural Housing. There are 138,000 units owned and managed by the Osaka Prefectural Government (OPG) and approximately 128,000 households are occupied. It is the second largest amount of housing stock owned by local authorities in Japan.

According to the statistical documents, 74% of the households are in the lowest income rank (see Table 2). 64% of households in the lowest rank have an income of less than 20,000 yen per month. In addition, the tenants' profile is rapidly aging. Elderly households have increased by 5.5% in the four years from 1998 to 2002. Younger households in the age ranges of 20-30 years and 40-50 years have decreased.

In fact 70? of all households in Osaka Prefectural housing are categorized as in need of special treatment. For example, households including elderly aged over 60-years, disabled individuals, welfare benefit recipients and single mother households are eligible for special categories. This ratio has increased by 10% during the last decade. The same situation has occurring beyond the Osaka Prefectural Housing scheme.

As part of the new reform, it is proposed to expand the entitlement to disadvantaged

Table 2 – Income ranking and ratio of households in 2002, Osaka Prefectural Housing

Income ranking	Income range (yen)		Ratio of household living in houses provided by OPG
	lowest	highest	
I	0	123,000	74%
II	123,001	153,000	6%
III	153,001	178,000	4%
IV	178,001	200,000	3%
V	200,001	238,000	4%
VI	238,001	268,000	2%
VII	268,001	322,000	3%
VIII	322,001	–	4%

OPG=Osaka Prefectural Government

Source: Osaka Prefectural Government Housing Management Report (administrative Internal Information)

households and individuals. By expanding the entitlement, it would help them have access to low-rent housing. However, it is doubtful that the local housing authority will be able to accommodate additional disadvantaged people, because most of the old housing stock is not fitted with accessible features for the elderly and disabled and cannot be linked with welfare service sectors. There are already large numbers of tenants who require welfare services. There is a discrepancy between what tenants need and what local authorities provide. Social isolation and solitary death in apartments have occasionally happened in the public rented housing estates. This happens partly because tenants do not effectively receive services that they need. If disadvantaged populations were concentrated in the public housing sector, more intensive care and services would be needed. It can be said that the link between housing management and welfare services is currently insufficient. Policy-makers have realized these problems, but have not shown concrete measures for achieving solutions. The reform should give highest priority to the issue of establishing a linkage between housing management and welfare services.

(2) Housing Management issues

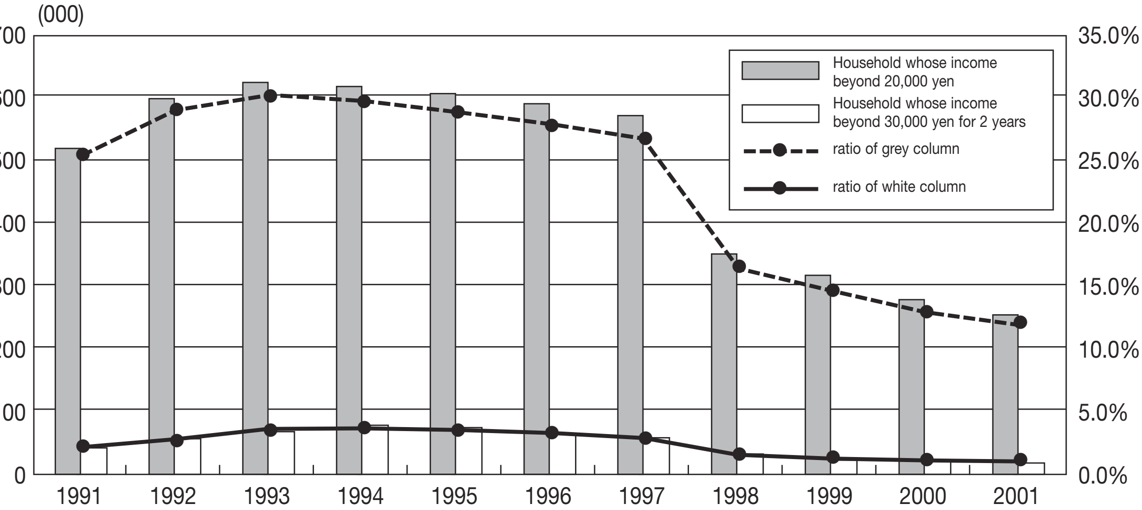
The most significant issue in housing management is that the tenants' associations are no longer viable. In local authority housing, there are still some tenants' associations. They are self-governed and take on daily management tasks such as cleaning communal areas and parking management. However, there is a lack of personnel for administration of the association and daily management because most of the tenants are elderly or disadvantaged. Local authority housing estates usually do not employ managers in the estates, except 'renrakuin', who distribute administrative notices.

Younger and working households can be expected to take a significant role in communities, although their income is often higher than the criteria. Currently, many of these people are being evicted because they no longer meet the income criteria. The public housing sector is losing human resources to look after the community. See Figure 3 to find the decrease in the number of households whose income has gone beyond the criteria since 1997. According to the amendment in 1996, local authorities have strictly carried out the evictions of applicable households. The same trend can be found in Osaka Prefectural housing.

Another issue is rent arrears. Figure 4 illustrates the amount of rent arrears and the ratio of rent collection. Since the middle of the 1990s, following the amendment and the economic downturn, rent arrears have increased. The number of evictions carried out on households in arrears is also increasing (see Figure 5). Most arrears are of one or two months. Arrears tend to be seen as personal problems. However, if a rent collector or housing manager contacted and consulted with these households in time, the number of households that have a large amount of arrears for a long time, who would eventually be evicted, would decrease.

Housing management problems that we have seen so far have been generated by inconsistencies of the past policy. The past policy tended to concentrate welfare-dependent individuals without linkages between housing management services and necessary welfare services for tenants. The new policy will again have the same inconsistency as the past one. If local authority housing is provided for welfare-dependent individuals and households,

Figure 3 – Number and ratio of households whose incomes exceed the minimum criterion to be eligible for public housing



Source: Osaka Prefectural Government Housing Management Report (administrative internal information)

intensive management, including housing, health, and social services should be provided together.

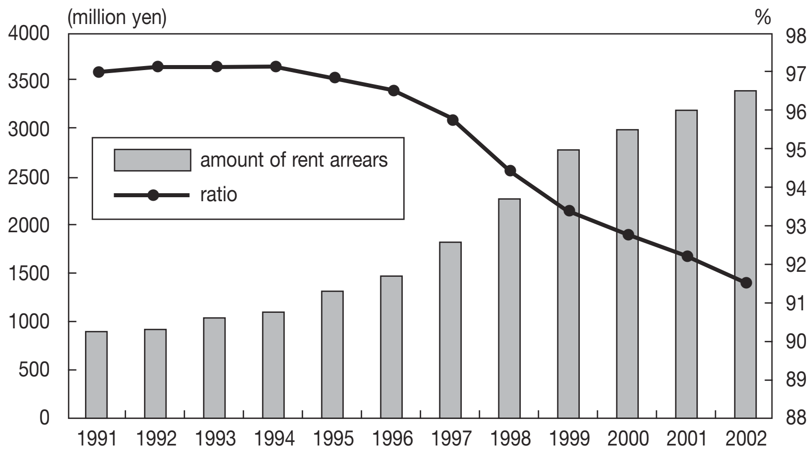
(3) Problems related to housing (re)development

New construction has been restricted by the financial crisis of local authorities and further constrained by the policies that aim to shrink the role of the public sector. In the case of Osaka Prefectural Government, most of the total units provided by the government are rebuilt units (see Figure 6).

Three issues should be pointed out regarding the (re)development of local authority housing. First, a large number of houses built in the 1960s and 1970s will reach the end of their infrastructural duration. Most local authorities have faced financial crisis so they are not able to raise additional money for rebuilding those.

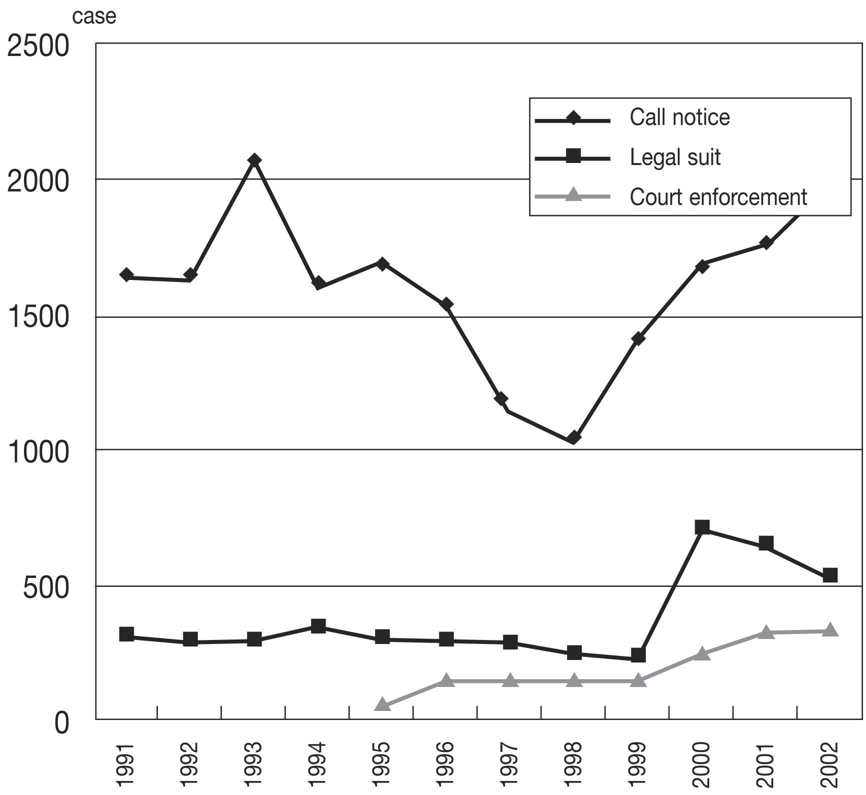
The second issue is a shortage of affordable housing. There are many people paying high rent in low-quality private rented housing, even though some of them are entitled to local authority housing. In the 1980s, the Osaka Prefectural Government estimated this number at approximately 70,000. This is a problem not only for local authority housing, but also for private housing because both sectors cannot provide affordable housing for low-income people. There have been very few effective

Figure 4 – Rent arrears and ratio of rent collection



Source: Osaka Prefectural Government Housing Management Report (administrative internal information)

Figure 5 – Legal suits for rent arrears



Source: Osaka Prefectural Government Housing Management Report (administrative internal information)

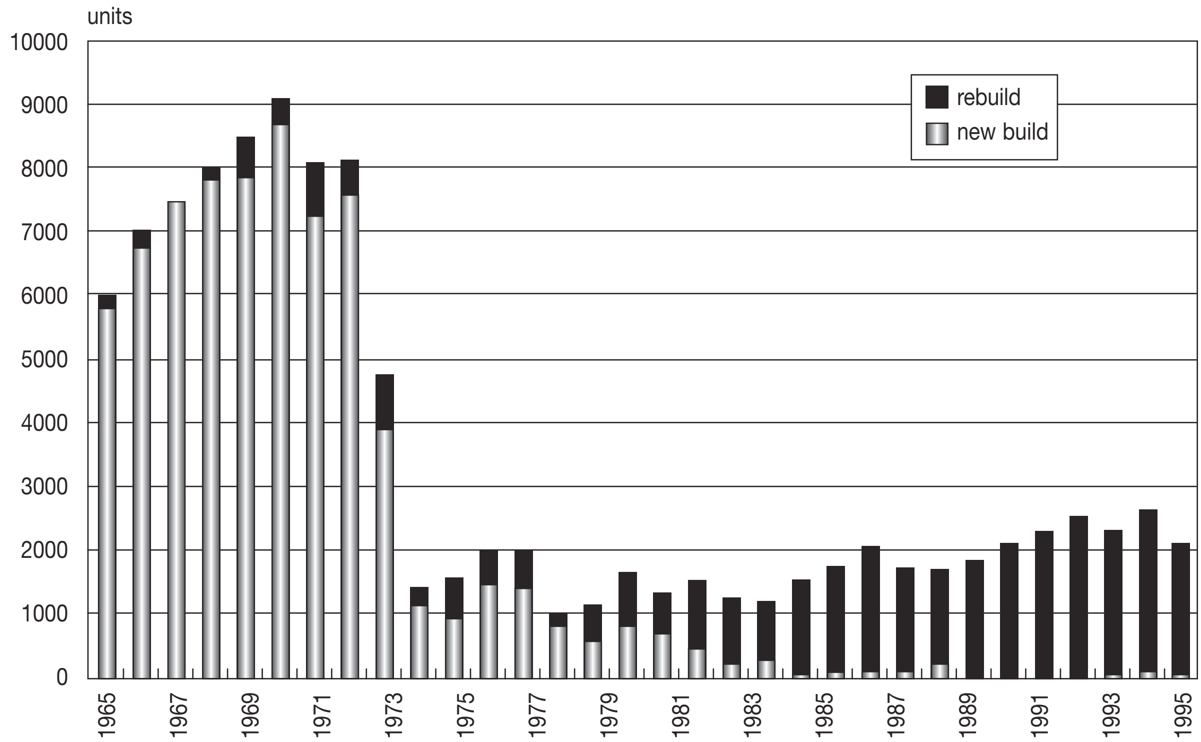
measures in Japan for controlling the provision of affordable housing for low-income people. The provision of affordable housing largely depends on local authority housing. Currently, new construction of local authority housing has been restricted and improvement of existing stock has not been sufficiently implemented. It can be expected that the gap between the demand and supply for low rent housing will expand. It is necessary to increase the numbers of affordable houses in a variety of ways in order to meet various housing needs.

For that purpose, local authorities will be required to investigate local housing needs accurately and to control housing provision in both public and private sector through allocating the limited resources effectively. Under the administrative and financial reform, subsidies for construction costs of local authority housing are abandoned and replaced by a local housing subsidy. It seems that new subsidies could possibly be used for a wider variety of affordable housing. At least the government should not decrease the level of the subsidy. It is necessary both to provide public money to private and non profit organizations adequately and to control them to provide and manage good quality of affordable housing. So far, local authorities have not had enough control of private construction activities and of the comprehensive planning of local housing (not only local authority housing but also other tenures). It is urgent that local authorities consolidate both.

The third issue is high-rise apartments. Many local authorities build high-rise apartments. Due to the financial crisis, they sell a part of the land where the existing stock is located and then use the proceeds from the sale to cover the rebuilding costs. Inevitably, rebuilt housing should be a high-rise structure because the available land becomes smaller and local authorities are required to rebuild at least the same number of units as before (Figure 8). Local authority housing in urban areas tends to be high-rise. However, this does not seem appropriate for a concentration of elderly people.

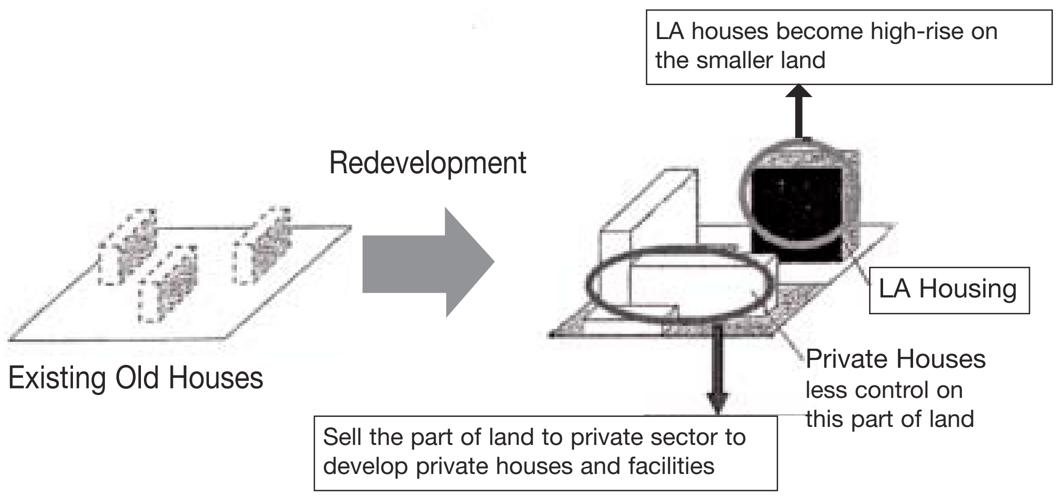
[5] Housing for the victims of the Great hanshin-Awaji earthquake has accommodated more elderly people than other local authority housing. The survey was conducted in 2004 by our research group. It was a questionnaire survey to tenants who live in housing built for victims of the Great Hanshin Awaji earthquake.

Figure 6 – Number of new construction and rebuilding units



Source: Osaka Prefectural Government Housing Management Report (administrative internal information)

Figure 8 – Method of existing local authority housing estates



According to a survey of local authority housing for victims of the Great Hanshin-Awaji earthquake[5], tenants do not prefer to live in high-rise apartments. Young couples with small children feel uneasy about living in high-rises and elderly individuals who live in higher stories are hesitant to go out. Thus, high-rise apartments could be one cause of social isolation and the decline of community.

Despite the decline of community, the concentration of elderly and disadvantaged people, and the lack of housing management and welfare support, rebuilding high-rise apartments is not an appropriate method. The main reason is that, as stated previously, high-rise apartments are not a suitable housing type for the elderly and for young couples with children.

Another problem concerning the rebuilding methods can be found. Local authorities do not always have strict control of land usage after the sale. Redevelopment of the site by the private sector does not necessarily bring about desirable land usage. Weak control should be addressed through the PFI system, which has been implemented to rebuild public houses. In Japan, however, there is less control of urban planning by local authorities and local people compared with Europe and the U.S. Without proper controls, utilizing private resources could worsen the problems stated above. It is necessary for local authorities and local residents to draft a local plan to avoid unsuitable development in their areas. Local authorities should make a more comprehensive plan covering measures for private housing. Although a comprehensive local housing plan has not yet been implemented and local authorities do not yet have sufficient control over private development, it is necessary to make a more comprehensive plan with proper controls. It should help solve many issues within local authority housing and other problems in the housing market as well.

5. Concluding remarks

Local authority housing cannot work well even as a safety net because there is no intensive management provided of services such as welfare provision. Nevertheless, new policies still intend to concentrate disadvantaged people without establishing intensive management provisions.

The problems described in this paper occurred within the local authority housing sector. However, the causes exist not only within the sector but also in housing provision by the private sector. Therefore, it is necessary to look at the entire system of housing provision. In doing so, it is essential to control the private housing market. As stated before, local authorities are facing a financial crisis. Utilizing the market is a reasonable way to provide affordable housing. However, Japanese housing policy has tended to convey controls to private activities. Using various methods for providing affordable housing could relieve the problems within the sector.

Finally, it is expected that the Local Housing Plan could be more influential on wider housing provision. It is not sufficient at present, but it would have the possibility to extend public and residential control throughout the local housing market.

New housing policies on local authority housing are not appropriate for the current problems in this sector. The old policy has not solved the problems, and the new housing policy follows a similar direction as the old one. The new policy would probably not bring any changes but make the problems worse. Japan has pursued welfare state policies in a different way than advanced European countries. Japan has preferred to spend money on urban infrastructure like constructions of motorway, bridges and dams instead of welfare services. In contrast to Europe, housing was of lower importance for Japanese authorities. This attitude could be attributed to the Japanese immature public attitude toward welfare. Contradictions often appear among socially and economically disadvantaged people. They have no say and have not been in a majority so far. As a result, socioeconomic disparities gradually widen. If contradictions spread out to the whole of society, we could expect a real new housing policy to appear.

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