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**Work programme of the United Nations Human  
Settlements Programme and budget of the United Nations  
Habitat and Human Settlements Foundation  
for the biennium 2012–2013**

**Proposed work programme and budget for 2012–2013**

**Report of the Executive Director**

**Addendum**

**Evaluation of the experimental reimbursable seeding operations  
programme**

**Summary**

1. By its resolution 21/10 of 20 April 2007, the Governing Council of the United Nations Human Settlements Programme (UN-Habitat) requested the Executive Director to establish a trust fund within the United Nations Habitat and Human Settlements Foundation to support the introduction of experimental reimbursable seeding operations and other innovative financial mechanisms, and to field test those operations for financing of housing, infrastructure and upgrading for the urban poor. It also requested the Executive Director to carry out, at the end of the experimental activities, in 2011, an evaluation thereof. The present report is submitted in response to that request. Its purpose is to assist the Governing Council in making a decision on the future of the experimental reimbursable seeding operations programme and related financing activities, including the Slum Upgrading Facility.
2. The report concludes that UN-Habitat has a comparative advantage in undertaking global advocacy, advising national Governments and local authorities, bringing key stakeholders together and working with community groups on an advisory and normative basis. The report also concludes that UN-Habitat is not best positioned to continue activity as a direct lender, as a result of a lack of incremental funding for lending activities from external donors and the administrative costs of establishing a permanent lending programme, as opposed to other UN-Habitat institutional priorities.
3. In the light of these conclusions, the Governing Council is requested to authorize the secretariat to examine opportunities to work with partner development finance institutions, who would take the lead in future pilot or scaled-up lending, guarantee and financial advisory activities, with UN-Habitat focusing on normative and global advocacy work in these areas.

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\* HSP/GC/23/1.

## Introduction

4. Housing and local infrastructure conditions in many countries, regions and neighbourhoods are inadequate, with the worst conditions usually being faced by the urban poor. The lack of adequate shelter and basic services undermines the Millennium Development Goal target of achieving a significant improvement in the lives of at least 100 million slum-dwellers by 2020.

5. With the promulgation by the Secretary-General on 20 July 2006 of the special annex for the United Nations Habitat and Human Settlements Foundation (series 300) to the Financial Regulations and Rules of the United Nations (series 100) (ST/SGB/2006/8), which superseded the Foundation's former financial rules (ST/SGB/UNHHSF Financial Rules/3 (1978)), the Governing Council and the Executive Director were empowered to pursue the General Assembly's call to strengthen the Foundation and to develop it into a mechanism to assist developing countries with investments in housing and basic services infrastructure.

6. The present report describes the implementation of Governing Council resolution 21/10 during a four-year experimental period with regard to experimental reimbursable seeding operations and other innovative operations on financing for housing, basic services, infrastructure and upgrading for the urban poor. The purpose of the report is to assist the Governing Council in making a decision on the future of the experimental reimbursable seeding operations and related financing activities, in line with resolution 21/10. By paragraph 3 of that resolution, the Governing Council decided that the consideration of document HSP/GC/21/5/Add.3, on the policy framework and draft operational procedures and guidelines, would be subject to a thoughtful review of the final evaluation by the Governing Council at its twenty-third session, in 2011, of the experimental activities conducted in accordance with paragraph 7 (g) of the resolution, and an analysis of the required risk assessments, including resource implications of the proposed mechanisms in that document and other activities tested during the experimental period.

7. By paragraph 4 of the same resolution, the Governing Council also decided that further extension of the implementation of other aspects of the financial regulations and rules should be subject to consideration by the Governing Council at its twenty-third session.

8. The report further sets out a vision for the future of UN-Habitat work in the area of urban economy and in assisting developing countries to finance the acceleration of the delivery of housing, basic services and infrastructure, building on the experiences gained through implementation of resolution 21/10 and the Slum Upgrading Facility.

9. With over 700 million people living in informal settlements or slums in cities of the developing world and with the full costs of urban upgrading estimated at over \$4 trillion, government and community efforts to upgrade slums and informal settlements have, on their own, not succeeded. Through resolution 21/10 and follow-up consultations, Governments therefore made a request for field-testing of new methodologies for the financing of low-income housing and infrastructure development. Both the lessons learned from this field-testing experience and recommendations on ways to build on them are set out below. The ultimate goal of the recommendations is to augment the flow of funding to urban upgrading and low-income housing, and to create policy frameworks conducive to accelerated development in the context of inclusive urbanization.

## I. Mandate for the evaluation of activities implemented under resolution 21/10

10. By resolution 21/10, the Governing Council requested the Executive Director to continue the work of strengthening the Habitat and Human Settlements Foundation so as to accelerate the provision of finance for the mobilization of seed capital, domestic and other financial resources for shelter and related infrastructure with due priority to the needs of low-income households; and to establish a trust fund within the Foundation to support the introduction of experimental reimbursable seeding operations as described in paragraph 7 (d) (iv) of the resolution, as well as other innovative finance mechanisms, building upon the experiences with instruments and partnership networks such as the Water and Sanitation Trust Fund and the Slum Upgrading Facility, for a four-year experimental period from 2007 to 2011.

11. It also requested the Executive Director to report to the Governing Council at its twenty-second session on the implementation of the resolution and specified that an evaluation should be conducted at the end of the experimental activities, in 2011, to guide any decision by the Governing Council at its twenty-third session on potential future applications of the experimental methodologies.

## **II. Implementation of resolution 21/10 and establishment of a trust fund for experimental reimbursable seeding operations**

12. Resolution 21/10 provided guidelines for the establishment and operation of a trust fund. The purpose was defined as:

- (a) To field-test experimental reimbursable seeding operations and other innovative operations for financing for the urban poor for housing, infrastructure and upgrading through community groups, including where there is an expectation of repayments mobilizing capital at the local level;
- (b) To strengthen the capacity of local financial and development actors to carry out those operations and to support the capacity of the United Nations Human Settlements Programme to enhance those operations. In relation to implementation arrangements, the Executive Director was requested:
  - (i) To establish a trust fund for the financing of the experimental reimbursable seeding operations and other innovative operations within the Foundation specifically for the implementation of the experimental activities;
  - (ii) To establish a steering and monitoring committee of 12 to 14 persons appointed in consultation with the Committee of Permanent Representatives. Representatives of Governments, international financial institutions, United Nations bodies, the private sector and major non-governmental organizations may be invited as participants.

13. Key methodological requirements were defined as:

- (a) Partnership arrangements between national Governments, local authorities, community groups and financial intermediaries with which there were agreements for term repayment to the trust fund;
- (b) Experimental activities were different from the current Slum Upgrading Facility and Water and Sanitation Trust Fund arrangements in that some of the activities of the former were reimbursable whereas the latter were only given as grants;
- (c) Experimental reimbursable seeding activities should be extended through intermediaries but should exclude borrowing, direct lending, guarantees or equity investments;
- (d) Having a working operations manual to describe the processes for different reimbursable seeding operations and other innovative finance mechanisms in consultation with the Committee of Permanent Representatives and the steering and monitoring committee;
- (e) Taking into account a balanced regional approach.

14. The following key implementation steps were undertaken by the secretariat, in line with the provisions of resolution 21/10:

- (a) Following the twenty-first session of the Governing Council, UN-Habitat engaged in discussions with the Committee of Permanent Representatives that concluded in April 2008 with the adoption of operational procedures and the endorsement of an operations manual for submission to the steering and monitoring committee established in mid-2008 after an international workshop and based on nominations made by regional representatives of the Committee. The operations manual was approved by the steering and monitoring committee;
- (b) In accordance with paragraph 2 of section I of resolution 21/10 and upon authority of the Financial Regulations and Rules of the United Nations, a designated trust fund was established within the United Nations Habitat and Human Settlements Foundation;
- (c) In developing legal documentation, UN-Habitat worked closely with the Senior Legal Adviser of the United Nations Office at Nairobi and the Office of Legal Affairs at Headquarters;
- (d) Institutionally, the implementation of resolution 21/10 was anchored within the Urban Finance Branch of the Human Settlements Financing Division of UN-Habitat and implemented in the context of focus area 5 of the medium-term strategic and institutional plan, on strengthened human settlements finance systems, complementing the Slum Upgrading Facility Programme.

### III. Lessons learned from implementation

15. The initial concept of the experimental reimbursable seeding operations was to compensate for shortfalls in housing in developing countries by stimulating domestic financial institutions (local banks and microfinance institutions) to lend to the poor. The initial method proposed was to offer financing to the target domestic financial institutions at very low interest rates and in local currency.

16. UN-Habitat learned that offering secondary finance at very low interest rates (as shown in table 1) was less effective in attracting domestic financial institutions into the low-income market than was using UN-Habitat funding to deal with the specific risk concerns of lending for housing in emerging economies. UN-Habitat found that lending as part of experimental reimbursable seeding operations could effectively stimulate investment by:

- (a) Offering local currency loans at social investment rates;
- (b) Offering longer-term financing to match the needs of real property development loans (for loan terms of between 3 and 5 years) or affordable home finance (for terms of between 5 and 20 years);
- (c) Offering UN-Habitat participation as a way of enhancing credit and reducing risk through the reputation of an international development institution, assisting local institutions in obtaining internal and regulatory approval to engage in or expand their low-income lending;
- (d) Offering UN-Habitat assistance to structure and organize the transaction, bringing together government, community group and financial institution parties in a collaborative structure;
- (e) Offering technical assistance and advice to non-governmental organizations in further developing their own capital structures;
- (f) Ensuring that each transaction included livelihood improvement for community members, as needed, and financial education for borrowers.

17. Such lending was successfully used in the last two experimental reimbursable seeding operation loans to reach larger numbers of beneficiaries and stimulate a high volume of additional investment in housing and basic services. End users in these transactions also received very fair lending rates within their local markets.

Table 1

**Experimental reimbursable seeding operation interest rates**

<i>Range of interest rates (percentage)</i>	<i>Average (percentage)</i>	<i>Weighted average (percentage)</i>
<b>1–6.5</b>	3.40	4.18
<i>Range of end-user interest rates (percentage)</i>	<i>Average (percentage)</i>	<i>Weighted average (percentage)</i>
<b>7–14</b>	10.09	9.94
<i>Range of tenor (years)</i>	<i>Average (years)</i>	<i>Weighted average (years)</i>
<b>3–20</b>	10.6	12.8

18. The initial concept of the Slum Upgrading Facility was to explore various ways of increasing slum upgrading, including technical assistance grants and grants for revolving funds. In the implementation phase, the Facility focused on the establishment of grant-funded local finance facilities to offer guarantees to local banks so that they could engage in slum upgrading project finance.

19. When Slum Upgrading Facility and experimental reimbursable seeding operation activities are viewed as a whole, UN-Habitat efforts over the past 18 months have funded 34 projects and lending

programmes, in each case attracting private-sector financing alongside government input and community savings, to fund low-income housing and urban upgrading, and using banking and financial services tools to ensure good project performance, as follows:

(a) Both the experimental reimbursable seeding operations and Slum Upgrading Facility have offered credit enhancement of varying types: cash-collateralized grants (the former) and co-lending and back-to-back lending (the latter) to attract private-sector investment;

(b) UN-Habitat has worked with national and local governments to support these projects and help make them affordable for the target communities. Well-designed government subsidies enhance both private sector finance and community savings investment. Community organization and support is important to project success.

20. In addition, UN-Habitat has learned that:

(a) Progressive home improvement and basic services infrastructure projects that can be supported by the community on a pay-as-you-go basis have had the most success in reaching beneficiaries with incomes in the bottom 30 per cent of the income pyramid;

(b) Project success is improved when livelihood support precedes or accompanies urban upgrading and microlending for housing;

(c) New home construction is financially feasible for lowest-income communities only if significant subsidies are available to cover land and infrastructure costs, and house design is modest and scaled to be affordable to those with low and irregular incomes;

(d) New home construction and affordable mortgage finance are effective ways to upgrade housing for lower-middle income families living in substandard conditions.

21. This experimental phase afforded an opportunity to establish a range of new and important partnerships, to undertake advocacy among Governments and to stimulate the private sector to extend financial services to the urban poor. It also demonstrated that significant resources and expertise were needed for internal and external implementation work and for establishing new administrative processes for lending and guarantee activities.

#### **IV. Experimental reimbursable seeding operations**

22. The experimental reimbursable seeding operations trust fund received a total of some \$3.6 million in financial contributions (\$2.85 million from the Government of Spain, \$500,000 from the Government of Bahrain and \$250,000 from the Rockefeller Foundation). As at 31 January 2011, UN-Habitat had disbursed five loans in the context of the experimental reimbursable seeding operations, totalling \$2.75 million, or 76 per cent of donated funds. The balance of funds was used for the steering and monitoring committee meeting and oversight expenses, and for the trust fund reserve required by the Financial Regulations and Rules of the United Nations and in line with United Nations best practices.

23. Projects were selected for loan funding using the following criteria agreed with the steering and monitoring committee experts: innovation, catalytic effect of proposed investment, sustainability, viability and replicability, and intellectually and financially additive. These criteria are reflected in the final approved operations manual. It is possible to draw valid lessons from the experimental reimbursable seeding operations programme, even though the transactions that took place under the programme were disparate in size, structure, geography, partner selection and developmental approach. Below is a summary of the transactions.

##### **A. Nepal**

24. A loan of \$250,000 was provided to the apex non-governmental organization Habitat for Humanity International Nepal (this was the first loan by UN-Habitat to any Habitat for Humanity International affiliate) to leverage grant funding and double the size of its programme for housing improvements by community cooperatives. The loan will be supplemented with the organization's own funds of \$100,000, so as in turn to provide financing to 15 credit cooperatives and village banks, which will then provide loans to what are termed "save and build" groups<sup>1</sup> for housing construction and improvements. Over 900 families will eventually benefit from the loan.

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<sup>1</sup> This scheme begins with a group of low-income families coming together cooperatively to generate cash income, set aside savings and contribute labour and materials. The group saves enough over six months to build the first house. At this stage, Habitat for Humanity International and its collaborative partners provide matching

25. A key impact of this project has been capacity-building for Habitat for Humanity International Nepal. The due diligence process, exposure to new financial and legal analysis, and the focus on improved management of the housing loan portfolio (including loan documentation and portfolio reporting) have provided this apex non-governmental organization with upgraded processes and procedures, faster repayment to promote increased building of homes at a swifter pace, and a preliminary toolkit to approach private-sector lenders for future funding.

26. In addition, the apex non-governmental organization is part of Habitat for Humanity International, a prominent and highly respected international charitable organization with housing lending operations in many underserved emerging markets. The Nepalese branch is the first branch or affiliate of Habitat for Humanity International to gain access to a loan, and this programme has been viewed as a replicable step for financial capacity-building and access to soft finance for many more of the parent organization's housing microfinance programmes worldwide.

## **B. Nicaragua**

27. A \$500,000 working capital loan was provided to a well-established non-governmental organization, the apex microfinance institution Programa de Desarrollo Local (Local Development Programme) (PRODEL), to fund expanded microhousing lending and a new municipal finance loan product for roads, water and sanitation services. Some 40 per cent of the loan will be used to finance the PRODEL lending programme for housing improvement loans, which includes an innovative technical assistance service offering low-income families help in obtaining secure tenure, and the services of an architect and engineer to design phased home improvement within the family's ability to pay. The remainder of the loan will be used to fund the PRODEL innovative neighbourhood improvement finance initiative, in which community group savings and in kind contributions, together with municipal borrowings, are combined to support infrastructure improvement, bringing improved road, sanitation and water services to low-income and peri-urban communities. It is estimated that over 4,000 families will benefit from these funded activities.

28. The working capital line of credit is a key part of the PRODEL initiative to expand its sources of funding and to prepare for eventual fund-raising through the capital markets, thus ensuring the sustainability of this highly innovative apex non-governmental organization. The working capital line can be replicated by other non-governmental organizations dealing with microfinance funded by the Swedish International Development Cooperation Agency (SIDA) in Central America.

## **C. Occupied Palestinian Territory**

29. In the largest catalytic project, the experimental reimbursable seeding operations supported the development of a \$500 million affordable housing programme in the Occupied Palestinian Territory by investing \$1 million in the creation of a new secondary facility for affordable home lending. This catalytic investment was necessary to unlock senior finance from the Overseas Private Investment Corporation of the United States of America, the International Finance Corporation, the Palestine Investment Fund, and two local banks in the Occupied Palestinian Territory (Cairo Amman Bank and Bank of Palestine).

30. The programme will offer good-quality housing stock to nurses, schoolteachers and families who have been overcrowded as a result of the low stock of affordable housing stemming from the lack of building in the West Bank. It is expected to employ over 100,000 construction workers and aims to build more than 30,000 affordable homes during the life of the programme.

31. The project further lays the financial basis for the development of the mortgage market in the West Bank, where mortgage lending has previously been negligible, and no local banks have been lending to lower-class or lower-middle-class borrowers. The World Bank will support the improvement of the legal and regulatory environment relating to mortgage lending, and CHF International will design financial education programmes for borrowers to be offered by the local banks, increasing bank capacity to deal with and fairness towards lower-income borrowers.

32. As a result of its participation in the project, the International Finance Corporation has expressed an interest in launching a global microhousing facility as a public-private partnership to support increased funding for microhousing lending in emerging markets.

33. The total investment stimulated by the \$2.75 million of experimental reimbursable seeding operation funding disbursed is over \$500 million from all project partners (including domestic banks,

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funds for the construction of two additional houses. These first three houses go to the neediest families in the group chosen by the group itself. At the end of 24 months all families in the group have had their housing needs met.

government sources, and \$300 million from the international financial institutions the Overseas Private Investment Corporation and the International Finance Corporation).

#### **D. Uganda**

34. A loan was provided to bring a local bank into a neighbourhood upgrading project, stimulating it to offer both construction finance and long-term mortgage loans to community members. The programme is a collaborative effort between UN-Habitat; DFCU Bank (a domestic private-sector bank with previous involvement in mortgage lending to the middle class, but not to the urban poor); a local municipality; a local residents' association; and the Ministry of Lands, Housing and Urban Development. The loan of the equivalent of \$500,000 in Ugandan shillings enabled the bank to commit matching funds to finance neighbourhood upgrading in Tororo, a town in eastern Uganda.

35. The bank and the Ministry both carried out affordability analyses for the target population. Initial concerns about low income levels and informal income notwithstanding, the bank concluded that it was feasible to provide housing loans to community members when accompanied by technical assistance to provide more opportunities for improving income prospects of potential borrowers (planning funded by UN-Habitat) and a livelihood support fund (from the Ministry); participation by community members in savings programmes; and the ability to qualify borrowers for home purchase based on their savings records. The municipality committed itself to contributing to basic services infrastructure, and the Ministry provided architectural designs for the homes to be built. The bank contributed significantly to the steering and monitoring committee and the hiring of the project manager. It has expressed interest in replicating the project in other locations and the Ministry is looking to develop between 40 and 50 similar projects nationwide.

#### **E. United Republic of Tanzania**

36. A loan was provided to encourage a local bank to fund a municipal sites and services project, resettling those living in informal settlements. The loan to Azania Bank of the equivalent of \$500,000 in Tanzanian shillings supported a municipal loan made by the bank to the Mwanza City Council to fund a site survey, planning and infrastructure installation in a peri-urban area occupied by families living informally. The Council had previously undertaken similar projects on a smaller scale. The funding allowed the Council effectively to begin redevelopment to make the site attractive to both middle-class and low-income families and to secure a funding commitment from the Ministry of Lands, Housing and Human Settlements Development to compensate those living on the site for the value of their existing homes, thus achieving social harmony.

37. Proceeds from the sale of 700 larger plots to middle-class families will repay the municipal loan to the bank, which in turn will repay UN-Habitat. This will allow the municipality to service a total of 2,800 plots, with 2,100 plots (with secure tenure) to be offered for sale at a modest cost to low-income families, including a right of first refusal for those previously living informally in the area.

38. The formalization of land use in the area is also expected to increase the City Council's tax base, enabling it to provide better public services to the population. The municipal loan concept is replicable in other municipalities, and the eminent domain payments from the Ministry are an excellent government initiative to balance the needs of urban development with the interests of low-income informal dwellers. The project should be replicable in other Tanzanian municipalities, and the city of Kisumu, Kenya, has also expressed strong interest in a similar projects.

#### **F. Results**

39. To date, the experimental reimbursable seeding operation loan portfolio is on schedule. Repayments have already begun on four of the five loans, with the repayment rate standing at 100 per cent.

40. Project partners have been pleased with the results and have suggested specific follow-on projects. The experimental reimbursable seeding operations, however, have not succeeded in raising additional lending funds, and thus cannot, in their current form, meet the potential for follow-on projects with partners (see table 2).

Table 2

**Experimental reimbursable seeding operation loans and potential follow-on projects**

<i>Project</i>	<i>Loan amount (equivalent in United States dollars)</i>	<i>Potential follow-on projects with partners</i>	<i>Potential follow-on projects (amount in United States dollars)</i>
Nepal	250 000	Five additional lending efforts with Habitat for Humanity International	1 250 000
Nicaragua	500 000	Credit enhancement for PRODEL: \$10 million bond issuance	1 000 000
		Extending working capital to eight other SIDA-affiliated microfinance institutions in Central America	4 000 000
Occupied Palestinian Territory	1 000 000	First-loss credit enhancement to support public-private partnership guarantee global micro housing programme with the International Finance Corporation	10 000 000
Uganda	500 000	Jinja project with Shack/Slum Dwellers International, Cities Alliance, DFCU Bank, ministry, local government	500 000
		40–50 projects in new municipalities similar to Tororo municipality pilot	25 000 000
<b>Total</b>	<b>2 750 000</b>		<b>44 250 000</b>

**V. Specific achievements of the Slum Upgrading Facility programme**

41. Since 2005, UN-Habitat, in the context of the Slum Upgrading Facility, has tested grant-based mechanisms to expand access to housing finance for the poor. UN-Habitat has moved through a process of learning in this respect, particularly with regard to the required financial expertise and process, and has been working steadily towards building internal and partner capacity and understanding where and why early projects did not go as planned.

42. The recent successful experience of UN-Habitat with local finance facilities in Ghana, Indonesia, Sri Lanka and the United Republic of Tanzania suggests that optimal policy and practice for slum upgrading projects and programmes should take into account the following:

- (a) Slum upgrading projects should be designed to be financially viable and to match what the low-income beneficiaries can afford;
- (b) Government housing policy and housing and infrastructure subsidies that encourage leveraging of government input with private-sector finance should be promoted;
- (c) Operating partnerships should be created between community groups, Governments and the private sector, with projects selected that make the most effective use of available funding;
- (d) Financial advisory technical support should be provided by people trained and experienced in finance and project management;
- (e) Successful slum upgrading approaches and support mechanisms should be institutionalized in each target country and community.

43. Local finance facilities are proving to be an important tool in mobilizing domestic investment and funds for low-income housing. The capacity in these institutions will be used further to support national priorities and projects that leverage domestic finance. UN-Habitat technical and financial advisory capacity continues to support the local finance facilities and provide advice to other UN-Habitat divisions. An independent evaluation report on the Slum Upgrading Facility will be available shortly.

**VI. Other specific achievements under focus area 5**

44. Focus area 5 also includes normative activities such as publications on housing finance systems and global advocacy.

45. A detailed research paper on the economics of slum upgrading was produced for the Bill and Melinda Gates Foundation, drawing conclusions and lessons from experimental reimbursable seeding



operation and Slum Upgrading Facility project experiences. This analysis of UN-Habitat finance activities in 11 emerging and frontier economies is making a significant contribution to the global discussion on provision of finance for the urban poor.<sup>2</sup>

## **VII. Key findings of the independent evaluation of the experimental reimbursable seeding operations programme**

46. Pursuant to the establishment of the experimental reimbursable seeding operations trust fund, resolution 21/10 stated that external evaluations would be undertaken of the activities of the sector, including to evaluate progress on the implementation of operations and other innovative mechanisms and to assess alternatives for more effective implementation.

47. An independent evaluator was recruited by UN-Habitat in October 2010, through a competitive process, to conduct an external evaluation of the operations. The evaluation process was conducted in line with the norms and standards of the United Nations Evaluation Group.

48. On the basis of the evaluator's expert review and analysis of relevant documents and technical lending processes, interviews, a written questionnaire and field visits, the evaluator produced a report, whose main findings are as follows:

(a) There is a strong consensus that the experimental reimbursable seeding operations are relevant. Most interviewees (who included staff members and consultants of UN-Habitat and the United Nations Office at Nairobi, members of the Committee of Permanent Representatives, expert members of the steering and monitoring committee, donor representatives and programme borrowers) were in favour of the concept of the programme and would like to see in the future some version of catalytic developmental lending for housing and basic services in some way linked to the UN-Habitat work programme;

(b) Failure to carry out a documented feasibility study before beginning programme implementation contributed towards an underestimation by UN-Habitat of the human and financial resources that were required to implement a lending operation programme;

(c) Administrative burdens posed a significant challenge to programme implementation. The programme's operation was not as efficient as it could have been as a result of the limited support resources made available internally and the continuing administrative burdens in implementation;

(d) The programme today stands close to best practice with regard to the delivery of finance for low-income housing and basic services infrastructure;

(e) Issues related to governance need attention.

49. The evaluator concluded that all the programme targets had been attained, except that for fund-raising, with only \$3 million of a target \$15 million raised.

50. The evaluator observed that the programme had had an innovative financial impact. Low-income households in Nepal, Nicaragua and the Occupied Palestinian Territory had already benefited from projects. All projects were implemented in countries defined as low-income or lower-middle-income economies. The intended target groups within each respective programme country had been reached or were in range of being reached.

51. With regard to the goal of encouraging financial institutions in the countries to engage with the target groups, the evaluator observed that that goal had been met by various types of collaboration with financial institutions, depending on the local situation. In the Occupied Palestinian Territory, Uganda and the United Republic of Tanzania, local banks were among the partners of the programme, while in Nepal and Nicaragua the financial partner institutions were village banks, savings cooperatives and microfinance institutions.

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2 Hewson, B.C. (2011), "Urban economics: building assets for the urban poor: analysis of urban upgrading and funding projects and programs in eleven emerging and frontier economies, 2009–2010", paper prepared for the Bill and Melinda Gates Foundation.

52. Comparing other lending programmes within the United Nations system, the evaluator found that the United Nations Capital Development Fund and the International Fund for Agricultural Development had a similar strategy and structure, and both had an institutional mandate for lending. The former was undertaking operations in the field supporting microlending, which might include a percentage of microlending for affordable housing, with a strategy comparable to that of the programme. It was launching an initiative on municipal finance and infrastructure finance and was seeking to link to housing microfinance opportunities.

## VIII. Recommendations for future decisions

53. The evaluator offered a number of suggestions to bear in mind when considering the future of the experimental activities:

- (a) Appropriate technical expertise should be tapped into, with financial experts involved at the design stage;
- (b) Implementation should take place on the basis of a feasibility study and through sustainable organizational infrastructure. If lending was continued at UN-Habitat, this should include:
  - (i) UN-Habitat making a substantial contribution of capital of at least \$4 million;
  - (ii) A workforce of between 7 and 10 Professionals and a yearly budget of between \$2 million and \$2.5 million;
  - (iii) Investment in a true administrative lending and support system;
  - (iv) Setting up a small (10-member) active board structure to oversee the programme;
- (c) Flexible funding mechanisms should be provided and diverse funding options (grants, loans, credit enhancements or guarantees, or a mix of all three) offered;
- (d) Support should be provided to financial institutions to enable the development of a variety of products to increase the programme's effectiveness through a more diverse loan portfolio;
- (e) Research, innovation and dissemination of experiences should be undertaken, distilling lessons learned from UN-Habitat global research and from various pilot affordable housing programmes;
- (f) Explicit target beneficiary populations for future lending should be defined.

54. The evaluation report sets out four options for the future:

- (a) To establish a permanent, scaled-up lending programme within UN-Habitat. This would involve, in addition to the administrative funding mentioned above, raising sufficient funds to support a larger loan portfolio of 20–50 projects, i.e., \$20 million in loan funds;
- (b) To continue with the current experimental approach, or “laboratory” concept, testing on a pilot-by-pilot basis. This would involve, in addition to the administrative funding mentioned above, raising sufficient funds to support pilot projects, equivalent to the amounts previously raised for the trust fund;
- (c) To liaise with development finance partners outside UN-Habitat but within the United Nations system, including on the transfer of the programme loan portfolio to a negotiated partnership with related strategic objectives to share costs and combine donor support;
- (d) To participate as a sponsor in a multi-donor, scaled-up lending facility further to pilot investment in local infrastructure and housing for the underserved and to offer first loss cover to scaled public-private infrastructure programmes to be developed in conjunction with international financial institutions such as the International Finance Corporation, and including a transfer or agency role in supervision of the experimental reimbursable seeding operations portfolio and Slum Upgrading Facility loan guarantee oversight.

55. Based on his analysis of the programme's implementation during the four-year experimental period, the evaluator identified options (c) or (d) above as the most suitable for UN-Habitat. At its most recent meeting, in October 2010, the steering and monitoring committee recommended the exploration of a similar range of options in moving forward.

## IX. Recommendations to the Governing Council

56. When UN-Habitat launched the Slum Upgrading Facility and experimental reimbursable seeding operation programmes, major international financial institutions, and most private-sector international and domestic banks, were not significant players in the areas of low-income housing finance or urban upgrading. In part as a result of the successful demonstration projects and programmes launched by UN-Habitat, combined with the growth of the microfinance industry, with its demonstration of repayment capability by low-income individuals and communities, this state of affairs is changing.

57. UN-Habitat has learned significant lessons from the programmes, which it believes will be of significant value to developing countries and economies. It would be a significant achievement if UN-Habitat could catalyse programmes at the level of major development finance institutions for low-income housing finance and urban upgrading, similar to efforts previously established by these development finance institutions in scaled up infrastructure lending.

58. UN-Habitat has a comparative advantage in undertaking global advocacy, advising national Governments and local authorities, bringing key stakeholders (Governments and communities) together and working with community groups on an advisory, normative basis. UN-Habitat also has a comparative advantage with its country and regional teams and networks that are already functioning through various divisions and regional offices.

59. UN-Habitat is not best positioned to continue activity as a direct lender, given the lack of incremental funding for lending activities from external donors, and the administrative cost of establishing a permanent lending programme as opposed to other UN-Habitat institutional priorities. Furthermore, it is unclear how UN-Habitat has a future comparative advantage in financial services, especially in ensuring growth to the needed scale and reach. In this light, options (c) and (d) appear to be the most appropriate approaches.

60. The Executive Director proposes, therefore, that the Governing Council should:

(a) Building on the recommendations of the external evaluation and on the institutional lessons learned from the programmes and other housing finance initiatives, support UN-Habitat in further strengthening and focusing its normative work in urban economy, housing and urban infrastructure finance;

(b) Building on recommendations (c) and (d) of the evaluation report, support UN-Habitat to examine opportunities to work with development financial institution partners who would take the lead on future scaled up and pilot lending, guarantee and financial advisory activities in these sectors;

(c) Support UN-Habitat in conducting a study of the feasibility of this new approach, including a full review of the potential future contribution of UN-Habitat in the field of urban economy and finance, and methods for collaboration with development financial institutions on the identification, design and execution of pilot and scaled lending, building on continued discussions with the World Bank, the United Nations Capital Development Fund, the International Finance Corporation, Kreditanstalt für Wiederaufbau (German Bank for Reconstruction) (KfW), Standard Chartered, and other potential partners as identified;

(d) Establish a reserve for the existing loan portfolio equal to 20 per cent of disbursed funds (\$550,000). This level of reserve will cover credit risks inherent in an experimental lending portfolio for low-income housing; operational and legal risks inherent in future management of the portfolio; and exposure from potential adverse currency movements with regard to currency loans not denominated in United State dollars. As a point of reference within the United Nations system, reserves of the United Nations Capital Development Fund loans to microfinance institutions in less developed countries are set at 20 per cent. The approval of the Governing Council for this reserve is requested as per ST/SGB/2006/8 Rule 304.3.2 (e) of the special annex for the United Nations Habitat and Human Settlements Foundation (series 300) to the Financial Rules and Regulations of the United Nations (series 100).