



Affordable housing & financial inclusion





Financial inclusion

Financial inclusion aims to empower poor individuals, low-income households, and small to medium-sized enterprises (SMEs) via access to and adequate use of a broad range of regulated financial products and services, including credit, deposit, insurance, remittance, and payment. When applied to the housing sector, it means access to financial advice, banking services and affordable credit.

Financial inclusion has improved in the last two decades in Cambodia, accelerating with the introduction of fintech companies providing online banking services. Despite this positive trend, there is still a lack of affordable housing products and services on the market. Microfinance is a critical vehicle for providing housing finance to those whom traditional mortgages cannot reach.

- In 2017, 78% of Cambodians did not have a savings account – a prerequisite to acquire a home loan.
- Accessing housing finance remains a challenge in Cambodia. Commercial banks and Microfinance Institutions (MFIs) both provide options for home loans, but require property titles as collateral, along with 20 to 30 % deposit. These criteria effectively manage risk for the lender; but they exclude many Cambodians from accessing home loans.
- This situation has driven some households towards less reputable lending schemes, placing households at greater risk of losing their property.
- Multiple options need to be developed to avoid low-income households falling into a debt trap and back into poverty.

TAKE AWAY POINTS

Despite the successes of MFIs in the two past decade, borrowers generally use MFI loans for home improvement, or building houses in provincial areas where land is considered more affordable. Expanding the role of MFIs to include home loans in Phnom Penh is an area that needs to be addressed.

Borrowers who cannot access traditional housing finance due to high housing unit prices, have resorted to risky non-traditional and non-banking financial solutions, sometimes offered by developers themselves.

Increased partnership between all levels of the government, community organizations, lenders, donors and developers would foster more innovative policy solutions and improve lending and credit pathways to lower income markets. This approach is more effective if the government facilitates access to land for development and subsidizes loans (e.g., through share equity models) to acquire assets.

Financial institutions have suggested two main options for increasing access to affordable housing finance:

- Develop better understanding of subsidy, credit pathways and risk-management arrangements which can be underpinned by either by the Government or international cooperation actors.
- Reducing upfront finance costs for customers by accessing finance from international financial markets for Cambodian financial institutions.

Sustainable financial products supporting affordable housing access to the most vulnerable groups have been developed by cities and government around the world. These models should be further examined for adaptation to the Cambodian context.



THE CURRENT STATE OF HOUSING FINANCE

Approximately one in every four loans in the Cambodian banking system are allocated to real estate (residential, commercial, industrial). Commercial banks accounted for 96.0% of all real estate loans with MFIs accounting for only 4 %.

One of the top five commercial banks in Cambodia has capped housing loans at 10% of the overall loan portfolio, believing that increasing this ratio would be too risky. For two out of the top five MFIs, housing and home improvement loans represent currently 21 to 26% of their loan portfolios¹.

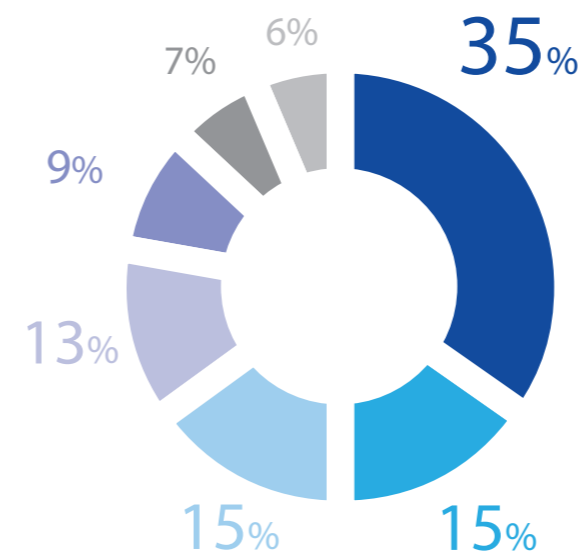
Commercial bank housing loans average 25,000 USD per loan, whilst home improvement and purchase loans from MFIs range from 2,500 USD to 11,000 USD. MFI clients generally borrow for home improvement, or to build new homes in the provinces.

Anecdotal evidence suggests that clients are gradually seeking loans for personal consumption over investment and income-generating activities. Financial institutions interviewed suggested current lending strategies focus on productive loan delivery. Because of the demand for personal loans, an increase in the cap for personal loans is highly likely.

¹Information shared during interviews with TUPS research team which took place between July to September 2020.

MICRO-FINANCE & FINANCIAL INCLUSION IN CAMBODIA

Cambodia has seen rapid growth in financial inclusion through microfinance – both in terms of borrowers and average borrowing size per capita².



REASONS FOR NOT HAVING A BANK ACCOUNT IN CAMBODIA

World Bank. (2017). Global Findex database 2017

- Insufficient funds
- Lack of necessary documentation
- Financial institutions are too far away
- Financial services are too expensive
- Lack of trust in financial institutions
- Religious reason
- A family member already has an account

²Gonzalez, Adrian. (2010). "Is Microfinance Growing Too Fast." in MIX Data Brief No. 5: Microfinance Information Exchange

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- Cambodia is one of the five largest microfinance markets in the world in terms of borrowers and average debt per capita³.
- The average microloan debt per borrower in Cambodia is around USD 3,370, the highest average amount in the world. That number is close to the entire median disposable income for rural Cambodian households in 2017 (about USD 3,900) and is more than double the 2017 GDP per capita (USD 1,427). Credit is growing by 40% per year⁴.
- The Global Findex⁵ - a global database on how adults save, borrow, make payments, and manage risk – states that Cambodians aged 15 and over with a bank account rose from 4% in 2011 to 22% in 2017. In 2017, 27% of adults had borrowed money from a financial institution, and only 16% of them had an outstanding mortgage.
- Of the 78% without an account in 2017, there are financial exclusion challenges. Unmarried household heads, those without complete primary education, and households belonging to an ethnic minority are significantly more likely to borrow from informal sources, which highlights further financial inclusion challenges.

⁴<https://www.economist.com/asia/2020/08/15/cambodians-are-bingeing-on-microfinance-loans>

⁵World Bank. (2017). Global Findex database 2017. Retrieved from <https://globalfindex.worldbank.org/#GF-ReportChapters>.

The microfinance boom has received some criticism for increasing indebtedness among Cambodians. But it has also played an important role in 'banking' the 'unbanked' and has provided an alternative to the use of informal lending. Between 2004 and 2017 the proportion of households resorting to informal moneylenders dropped from 32% to less than 6%⁶. In 2017, the National Bank of Cambodia capped interest rates charged by formal lenders to 18%, which forced many to adapt their business models – some had charged up to 30% interest rates. However, most MFIs compensated the losses due to the NBC measure by creating additional fees. Despite the interest rate decreasing over the past decade, some lending practices have been denounced as still abusive and harmful⁷.

BARRIERS TO ACCESSING CURRENT HOUSING FINANCIAL PRODUCTS

Banks and MFIs both provide options for home loans, but the perceived and actual risks often prevent lending to low-income groups. These barriers on the borrowers' side are caused by, although not limited to, high transaction costs (fees), interest rates, deposit requirements (up to 30%), insurance costs (more common with commercial banks) and collateral requirements (soft or hard land title). Low-income customers require a different approach to make responsible and sustainable financial decisions, with a stronger emphasis on households' credit assessment and support throughout the loan repayment, lower interest loans over a longer term, affordable and simple insurance and financial counselling.

⁶Microfinance and social welfare, Cambodia Policy Note. World Bank Group. 2019.

⁷Collateral Damage, Land loss and abuses in Cambodia's Microfinance sector. Cambodian League for the Promotion and Defense of Human Rights, Sahmakum Teang Tnaut, August 2019.

OWNERSHIP TITLES & COLLATERAL

Currently, nearly all commercial banks and MFIs require property titles as collateral. Some will accept soft titles (official recognition of legal occupation delivered by the Commune authority), some only hard titles (official recognition of legal ownership delivered by the Department of Land Management). Some require the title for the property currently being purchased, while others require the title of an already fully-owned property. Because hard titles are rarer than soft titles, some financial institutions are considering the acceptance of soft titles as collateral, to reduce the number of households turning to informal money lenders. Others also point to regulations which do not allow moveable assets to be put down as collateral, while lending practices should not be based on the possession of a land title but on the capacity to repay.

IRRESPONSIBLE LENDING

Irresponsible lending, including housing developers offering zero-deposit purchase plans, has emerged in recent years. These loans include much higher interest rates than commercial banks or MFIs and can trap consumers who lack the financial literacy to understand the impact of the higher interest. If these loan obligations cannot be met, the buyer can lose their home.

It is simply impossible for the poorest groups to provide the collateral required by most lending institutions as they often lack the necessary documentation. As a result, the system increases the likelihood of the poorest groups to seek out informal and predatory lending.

There is global recognition that access to finance is essential for low-income groups to secure land and decent housing, but it must be done in a manner that doesn't place either the customer or the lender at risk. Because of this, affordable housing, both ownership and rental options, are increasingly financed, produced and managed in many countries by a combination of state, commercial and community stakeholders, using a variety of hybrid governance and funding arrangements⁸.

⁸Van Bortel, G. et al., 2018. Affordable Housing Governance and Finance: Innovations, Partnerships and Comparative Perspectives.,

DEVELOPING NEW INCLUSIVE FINANCIAL TOOLS

MAKING LOANS AFFORDABLE TO VERY-LOW & LOW-INCOME GROUPS

NGO-BACKED HOUSING MICRO-LOANS A SOLUTION TO HOUSING FINANCE FOR THE MOST VULNERABLE?

The Habitat Improvement for Poor Communities in Phnom Penh, implemented by NGO Planete Enfants et Développement, supports vulnerable families in five Urban Poor Settlements in Phnom Penh to upgrade their house, or rebuild a new safer one.

1. The first option is a renovation kit: up to \$350 USD

2. The second option, currently under development, will be to support the construction of a new house priced between \$3,500 and \$5,000 USD.

To ensure financial participation is both accessible to the target group and allows borrowers to make an informed decision about financial risk, a tailor-made financial product was co-developed with MFI Chamroeun.

Households can borrow between 100,000 and 800,000 riels (approximately \$100 to \$200 USD) at a monthly interest rate of 1.5% (with an opening 2% processing fee). Tenor ranges from 3 to 12 months, and the repayment process is supported and monitored by the village leader and an MFI loan officer. Loans can be allocated to groups or individuals, in which case a

guarantor is needed. This system allows to waive the need for any collateral. Defaulting loans are covered through a provision in the agreement: the NGO will cover up to 50% of the amount of defaulting loans, and the MFI agrees to cover the potential loss of the remaining amount.

Previous community-led programs have sought to address barriers mentioned in the previous section, but have largely failed to address sustainability and financial aspects of housing programs for low-income groups in Cambodia.

The Urban Poor Community Development Fund (CDF) took the concept of pooling resources beyond individual community savings groups to city scale, allowing for more ambitious housing projects for low-income groups to be initiated.

The CDF model relied heavily on the government providing free land for relocated communities and political support of individuals within government⁹. Unfortunately, there was an absence of risk management and formal legal framework which would make the program more sustainable.

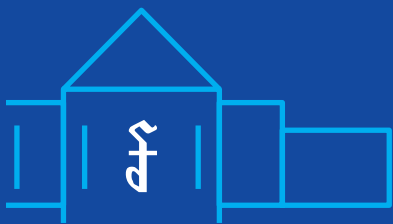
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In Cambodia, the need to bridge the financial gap between public and private resources could be addressed with the support of international cooperation and opportunities offered by blended finance mechanisms. These options need to be further explored: other cities and countries have led the way and offer interesting examples for possible adaptation to Cambodia.

⁹Brugman (2019) and Dasgupta & Beard (2007)



DEVELOPING TAILOR-MADE MORTGAGES BACKED BY PUBLICLY-OWNED FINANCE INSTITUTION

In Pakistan, the social enterprise Ansaar Management Company (AMC), with the support of UK-based social enterprise Reall, developed mixed-tenure housing sold on the open market. AMC developed a mortgage product for low-income buyers in partnership with a semi state-owned finance institution, Housing Building Finance Company Limited (HBFCL), which created a mortgage product tailored for AMC customers with a minimum monthly income (USD 161). Mortgages are loaned at a fixed interest rate of 12 % (compared to 35 % offered by microcredit providers in Pakistan, and 18 % offered by microcredit providers in Cambodia) over 20-year terms, and a deposit requirement of 25 %. AMC reduces risk to the lender by ensuring borrowers have land certificates and homes are built to quality standards. AMC also offers instalment plans for those who are ineligible for a bank loan – this allows for the sales process to start before converting to a mortgage. This model could be piloted in Cambodia with the commitment of a national bank and a housing developer.



DEVELOPING A DEPOSIT-FREE MORTGAGE VIA A REINSURANCE PRODUCT

In Beira, Mozambique, the social enterprise Casa Real, with the support of UK-based social enterprise Reall, as well as the Dutch government operating through the impact advisory firm Fount, lobbied several mainstream banks and the Central Bank of Mozambique, for Absa Mozambique (formerly Barclays) to launch a new housing mortgage product in 2019. These mortgages are targeted to customers with monthly incomes lower than USD 237 per month. Absa provides financing for up to 95% of the sales price (compared to 70% from Cambodian banks), made possible by negotiating a reinsurance product for the bank to provide mortgages without a down payment. Absa charges interest on the loans at the national prime rate (18 %), plus a relatively small margin of 0.25 per cent (this compares favorably in Cambodia as interest rates range from 8-12 % in commercial banks). This model could be potentially replicated in Cambodia to address both the deposit and lending amounts through provision of a guarantee in Cambodia, and could be carried out by a local organisation or institution with community and commercial credibility.

