

HOUSING PROGRAM

(GU-0022)

EXECUTIVE SUMMARY

BORROWER: The Republic of Guatemala

EXECUTING AGENCY: Ministry of Communications, Transportation, Public Works and Housing

AMOUNT AND SOURCE:

IDB: OC (in US\$ from SCF)	US\$ 60.00 million
Local counterpart funding:	US\$ 48.80 million
Total:	US\$ 108.80 million

FINANCIAL TERMS AND CONDITIONS:

Amortization period:	25 years
Disbursement period:	4 years
Interest rate:	variable
Inspection and supervision:	1%
Credit fee:	0.75%

OBJECTIVES: The Government is committed to a housing sector strategy that seeks to improve the housing conditions in Guatemala, particularly among the poor. The goal of the present program is to support this strategy by developing and implementing policies that will (i) improve the equity and efficiency of Guatemala's housing markets; and (ii) increase the level of investment in housing occupied by low income households.

The specific objectives of the Program are:

- a) To improve housing conditions among low income households and induce additional private investment in housing by designing and implementing an efficient and well targeted subsidy program;
- b) To increase the efficiency and demand-responsiveness of production and financing of low-cost commercial housing by expanding the role of private sector developers and commercial banks;
- c) To improve the formulation and implementation of housing policy by expanding the role of NGOs, community based organizations and other representative organizations;
- d) To improve the performance of urban land markets, particularly those accessible to low-income households;
- e) To slow the rate of environmental degradation associated with urban development by strengthening environmental management,

- particularly the management of natural hazard risks in the Metropolitan Area of Guatemala City.
- f) To promote the development of an efficient secondary mortgage market.

DESCRIPTION:

Overview: The Program strategy is grounded in a set of fundamental housing policy decisions taken by the Government of Guatemala over the last 12 months. Firstly, the Government has committed itself to the introduction of demand side subsidies accessible to low income households; secondly, the authorities have given increasingly high priority to resolving the issues of land use regulation; thirdly, the successful experience of the Guatemalan Housing Fund (FOGUAVI) in using private housing developers and commercial banks to execute housing policy has given the Government confidence in a "market driven" approach to implementing housing policy.

The Program will rely on two principal instruments: a demand side subsidy and a package of legal and regulatory reforms to promote the development of a legally recognized market in low cost urban land.

The subsidy program will provide a transparent up front sum to reduce the cost of a housing solution. To get access to the subsidy, eligible households will themselves have to come up with a substantial contribution in cash. For middle income households, the subsidy together with the contribution will buy down the size of the mortgage needed to acquire a completed house. For low income households the same program will generally serve a different function: it will provide the resources to improve quality of the (informally produced) housing these households currently occupy.

The program defines a clear and crucial task for the Government in its role as the source of financing for the subsidies. In contrast, assessing household credit worthiness, issuing loans, designing and constructing the housing solutions, are all tasks that will be undertaken by private sector enterprises. The Government will not provide resources, directly or indirectly, for credit.

To ensure that the subsidy is really accessible to low income households, the Program will rely on the intermediation of NGOs and community groups. The Program will provide resources so that these groups can help communities identify, design and execute community upgrading projects. Specialized NGO's will

also help administer the subsidies and appraise the projects.

The Program's second principal instrument is the reform of land markets. For low income households, the dysfunctional land market is currently a major constraint on their willingness to invest in housing. The Program will support a large scale land title regularization policy to resolve the problem of illegality in existing informal neighborhoods. In addition the program will support a radical reform of municipal land-use regulation. This will allow private landowners to put low cost plots of land on the legal market. These "progressive subdivisions" will begin with very low service standards but households will have access to the subsidy program to begin the improvement process more quickly. These reforms will allow a legitimate private market accommodate future urban expansion and so reduce the incentive to invade public lands.

Finally the Program will attempt to put in place a set of simple but effective measures to reduce the environmental damage that can result from urban growth, and to reduce the risk posed to informal neighborhoods by the hazardous topography of Guatemala City's metropolitan area.

The components described below have been designed, not as pieces of a stand alone IDB operation, but as a source of broad support to the Government's over all housing strategy. The IDB's resources will ease the period of transition as the new policies are implemented; however, the critical test of the Program's success will lie in it's ability to improve the equity and efficiency with which local resources are used in the future. The financial and institutional arrangements for the present operation are therefore intended to ensure that the programs initiated over the next four years can be sustained after the period of project execution.

Components

1. The Direct Subsidy Component (\$91.9 million) will provide eligible households with a subsidy to improve their housing conditions. For middle income households the subsidy, together with their own contribution, will help them qualify for a mortgage to buy a house produced by the formal private sector. For low income households the same program will generally serve to provide

the resources to upgrade the informally produced housing they currently occupy.

2. The Land Market Reform Component (\$5.85 million) will implement a package of legal and regulatory reforms through three lines of action: *Land Regularization* will operate in existing informal neighborhoods located on public lands. It will provide eligible households with the services needed to obtain individual registered title to the plot they currently occupy. To avoid giving incentives to further land invasions, no neighborhood formed within the past two years will be eligible. *Progressive Subdivision* will create the legal framework and incentives so that private landowners are able to subdivide land and sell plots with a minimum level of services. Eligible purchasers will apply to the Direct Subsidy Program to help begin the process of upgrading their housing. *Reducing Commercial Development Costs* will help develop a single, unified set of regulations to reduce the time and cost required to comply with municipal procedures for obtaining commercial construction permits.
3. The Environmental Management Component (\$500,000) will set up a strategy of defining environmental priority areas in urban areas throughout the country. These zones will be delineated on easy to manage maps; households will have strong incentives to comply since within these "exclusion zones," no proposal to improve or develop a neighborhood will be eligible for subsidies or other program benefits. In the Metropolitan Area of Guatemala City the program will provide technical assistance to distinguish areas where the natural hazards can be economically reduced by constructing small works (which can be financed with subsidies) from the high risk areas where such works would not constitute prudent investments. Households in the high risk areas will receive informational material explaining how relocation to a more suitable area would enable them to qualify for a subsidy. Municipal and national authorities will receive technical assistance to improve their capacity to manage emergencies.
4. The Institutional Development Component (\$4.44 million) will set up the operating units (Direct Subsidy unit; Land Market Reform Unit; Environmental Management Unit; and Management Information Unit) needed to execute the program

components. In addition the component will provide technical assistance to participating entities (NGOs and others) to help increase their capacity to serve as Program intermediaries; it will provide technical assistance to set up workshops and studies to help commercial banks develop the mortgage market; it will finance the carrying out of annual evaluation studies of program performance; as well as policy and sector studies to strengthen the capacity of the Ministry of Communications, Transport, Public Works and Housing to develop and implement policies and programs.

**ENVIRONMENTAL
CLASSIFICATION:**

The CESI/TRG, at its meeting of January 14 1997, classified this as a Category III operation, and considered the ESIR at its meeting on 22 August 1997. (See Para. 3.28).

BENEFITS:

The principal benefits of the policies supported by the present program will be: (i) The equity of public investment in housing will be increased. The Guatemalan Housing Fund (FOGUAVI) will develop the capacity to deliver subsidies to 9,000 low income households each year; (ii) the efficiency of public sector housing investment will be increased. Demand side subsidies will replace subsidized interests rates, making subsidies more transparent; the design of the subsidies will encourage additional private investment in housing; (iii) the role of private sector agencies in the housing sector will increase. In the formal market, competitive housing developers and commercial banks will face incentives to produce lower cost units; in the informal market, the capacity of community organizations and NGOs to deliver services to the low income population will be increased; (iv) regularizing land holding in informal neighborhoods will provide 50,000 low income households with security of tenure, stimulating investment in housing improvements; introducing progressive subdivisions will reduce the incentives to invade public lands and will reduce the cost of subsequent infrastructure improvement; and (v) the damage to environmental assets caused by urban expansion will be reduced as Program incentives help direct households toward suitable locations for housing construction. A workable policy will be introduced that will reduce the risk of losses from natural disaster, largely benefiting low income households in Guatemala City.

RISKS:

The principal risks to the realization of these benefits are (i) The "leakage" of program subsidies to ineligible families or non housing goods; and (ii) the diversion of program benefits away from the low income households in favor of (eligible) middle income households. These are serious risks that can only be mitigated but not removed. The Program includes the following measures to limit these risks.

- 1) Subsidy Leakage. The probability that the benefits of the subsidy "leak" out to ineligible families or to non-housing services of misuse of subsidies is largely a function of its absolute size in relation to household preferences. The subsidies in the present Program were estimated taking into account observed expenditures on housing investments by the target population; moreover, the intermediaries that manage the subsidies for FOGUAVI (banks, NGOs, cooperatives) will establish stable (and fee earning) relationships with FOGUAVI. They will therefore be concerned with monitoring Program performance and limit leakage.
- 2) Diversion of Benefits. The risk that program benefits may be "captured" by middle income households has a technical as well as a political dimension. The technical problem is that low income households are less able to articulate their housing needs into effective demand for projects. The Program therefore provides training for intermediate organizations (community groups, NGOs, cooperatives) to improve their capacity to provide low income neighborhoods with these services; the program will also provide funds so that experienced professionals can be directly contracted to develop upgrading projects. The political dimension of this risk is more difficult to handle. FOGUAVI has considerable experience in responding to the program requirements of the housing developers and Banks that produce low cost units for middle income households. This lobbying capacity is not currently matched by that of the NGOs that serve the low income market. However, it is likely that the Program will increase their ability to act as a counterweight in the political process of resource assignment.

**THE BANK'S
COUNTRY AND
SECTOR STRATEGY:**

The Bank's country strategy is to give priority to (i) incorporating the low income, rural and indigenous population into the development process; (ii) increasing the coverage and improving the

quality of social services; (iii) modernization of the state; and (iv) the development of the productive private sector.

**PROCUREMENT BY
INTERNATIONAL
COMPETITIVE
BIDDING:**

The cut off levels over which Program procurement will be by competitive international bidding are: \$350,000 for goods and services; and \$3 million for works. (See Annex III, section III).

**SPECIAL
CONTRACTUAL
CONDITIONS:**

The conditionality of the Direct Subsidy component will include as condition prior to first disbursement, the establishment of its operating unit understood to comprise the official adoption of operating regulations and manuals for both the Commercial and Social Windows and the hiring of the corresponding coordinators. (See Paras. 3.2, 3.9).

To ensure that sustainable policies benefit a target population traditionally underserved the Government will (i) meet targets for actions that benefit low income households (Para. 3.41), and (ii) comply with land market reform goals (Para. 3.19). Furthermore, to avoid inflationary pressures in the housing sector, the Government will comply with ceilings on subsidies provided through the Commercial Window (Para. 3.15). Should the Government fail to meet these targets it will suspend commitments corresponding to the Direct Subsidy -Commercial Window. In addition, the Government will prepare environmental maps within agreed time frames (Para. 3.31).

Similarly the conditionality for the land reform component will include as condition prior to first disbursement the establishment of its operating unit which is understood to comprise the adoption of operating regulations and manuals and the hiring of the Unit Coordinator. (See Para. 3.16).

**REIMBURSEMENT OF
EXPENSES**

Up to US\$500,000 corresponding to the contracting of an auditor for the Direct Subsidy Component may be reimbursed chargeable to Loan resources.

Certain operating conditions for each Program component will be specified in the corresponding operating regulations. (See Paras. 2.19, 3.18, 3.23, and 3.29).

**AMMENDMENT TO LOAN
886/SF-GU
RECOMMENDATIONS:**

It is proposed that Loan Contract 886/SF-GU (Global Credit for Small and Micro Enterprise) be amended to permit the use of that Program's resources to finance housing solutions. (See Para. 2.33).

To help insure the sustainability of the policies and programs introduced under this operation, the Guatemalan Government has requested that supplemental resources for continued execution of the program be available. To this effect, it is proposed that once 50% of the Program resources have been disbursed, and the achievement of all performance targets have been verified, subject to the conditions set forth in Para. 2.40, supplementary financing could be provided. At that time, a memorandum describing the progress of the Program, the amount of resources committed and disbursed, and requesting the authorization for up to US\$20 million in additional financing shall be presented to the Board of Directors for its consideration.

POVERTY

IMPACT:

The proposed project qualifies as a poverty-targeted investment as set forth in the Eight Replenishment document. The official definition of poverty in Guatemala classifies as poor any household whose income is less than 4 minimum salaries, equivalent to about \$400 a month. Under this criteria approximately 88% of urban households qualify as poor and 100% of Program resources will benefit households at or below the poverty line. Beneficiaries will be selected by household income. Currently, the Government devotes almost its entire annual housing sector investment budget to financing about 2,000 house targeted at households with incomes of approximately \$350 a month; low income households (with monthly income of US\$200 or less) have very little effective access to these resources. Under the policies supported by the present operation approximately 60% of program resources will directly benefit some 55,000 low income households.

I. BACKGROUND

A. Socio Economic Context

- 1.1 Guatemala's recent macroeconomic performance has been satisfactory with annual GDP growth of 5% and declining levels of inflation and public sector deficit. Nevertheless, increases in tax effort, and improvements in the coverage and efficiency of social services are needed to alleviate the problems caused by widespread poverty. The Peace Accords signed in December 1996 underlined the Government's commitment to undertake the necessary reforms.

B. The Urban Housing Markets of Guatemala

1. Introduction

- 1.2 Income distribution drives the performance of Guatemala's housing markets. Low income households, those with incomes of \$200 a month or less, make up 60% of the urban population. For these households, the informal market is the only affordable source of housing. At the other end of the income distribution, perhaps 12% of urban households have monthly income of \$400 or more, an income that generally enables the household to qualify for a mortgage and so purchase a house produced by a commercial developer.
- 1.3 In this environment, households with incomes between \$200 and \$400 a month, though modest enough in absolute terms, qualify as "middle income". These households, while constituting less than 30% of the market, do play a disproportionately important role in housing policy. Although currently excluded from the mortgage market, many have stable and well documented sources of income. As in many countries of Latin America, helping this population segment move out of the informal market and into the low end of the formal commercial market, represents an important political commitment for policy makers in Guatemala. ^{1/}
- 1.4 The sections that follow will pick out the main constraints facing these housing markets. These constraints, in turn, are the targets for the interventions proposed in the present Program. In the informal market discussed in Section 2 below, poor housing conditions are linked to low levels of household investment and to the gross distortions found in the urban land market. Section 3 presents the principal characteristics of the formal housing market notably the limited scale of the primary mortgage market and the initiatives to develop the "low end" of commercial production. Section 4 analyzes briefly the interaction between urban expansion, and the environment, emphasizing the problems resulting from the invasion of public lands in Guatemala City's Metropolitan Area. The

^{1/} The scale of the market for additional houses in Guatemala is approximately as follows. The urban population increases by some 30,000 households each year. As a result, each year the housing market must accommodate an additional 18,000 low income, 8,500 middle income and 3,500 upper income households.

discussion then shifts from housing markets to housing policy. Public sector investment in housing has not been of great quantitative significance. Nevertheless, the evolution of Government policy, and of the Bank operations that accompanied it, do provide important lessons for the present operation.

2. The Informal Housing Market

- 1.5 For the low income population throughout Latin America, the "normal" process for acquiring a house begins when young households establish a shack of impermanent materials in a recently formed neighborhood where access to infrastructure services (water, sanitation, electricity, paving) is poor. Over time, households invest in improvements to both the house and the public infrastructure that serves it. What is distinctive about Guatemala is that this "normal" process has been severely attenuated, resulting in unusually poor housing conditions in the informal neighborhoods. And these informal neighborhoods are continuously expanding to accommodate more than 20,000 additional households each year.

a. Household Investment and Housing Conditions

- 1.6 Low income households in Guatemala invest notably small sums in their housing. A study showed that households with incomes below \$170 a month had invested, on average, less than \$800 on initial expenditures and subsequent upgrading ^{2/}. In contrast, a survey carried out in Panama in 1995 found that households with similar incomes (and facing similar construction costs) had invested a total of more than \$2,000.

Table 1: Family Income and Housing Expenditures (US\$)
Total Expenditure (initial + improvement)

Total Household Income per month	Total Expenditure				Average Expenditure
	<\$330	\$330-\$1,330	>\$1,330	Total	
Low income <\$170	40%	47%	13%	100% (131) ¹	\$770
Middle income \$170-\$330	18%	47%	35%	100% (146) ¹	\$1,120
Upper income >\$330	6%	38%	55%	100% (47) ¹	\$2,240

¹ Number of households surveyed in each income category.

Source: IPC 1997

^{2/} Data on housing investments was collected from more than 300 households in Guatemala City. The full study (IPC, 1997) is held in the project files.

- 1.7 These expenditure data clearly lie behind the persistence of poor housing conditions in Guatemala: out of 700,000 urban houses, more than 300,000 have only one room; 230,000 are constructed of impermanent materials; and 166,000 lack potable water connections. 3/
- 1.8 While investment per household is low so is the number of houses constructed each year. In most Latin American countries, the rate at which urban houses are constructed keeps pace with the rate of formation of urban households. In Guatemala, there is an annual shortfall of about 1,000 units a year. The result is a high level of urban overcrowding with 2.3 number of people per room, compared with a Latin American average of about 1.5.
- 1.9 In part, these fragmentary data are simply the result of Guatemala's poverty. Correspondingly, there is some evidence that as the economy has strengthened over the past three years, so housing conditions may have already begun to improve.

b. Land Markets

- 1.10 Distortions in the urban land market are also a major constraint on household investment. Illegal occupation of land, often but not invariably publically owned, is the dominant mode of urban expansion in Latin America. In Guatemala, this has become highly politicized and integral to civil unrest since successive Government actively sought to repress land invasions. Most low income neighborhoods in Guatemala City continued to form through illegal occupation. However, highly publicized incidents, when squatters were forcibly evicted, had important effects.
- 1.11 A few squatter neighborhoods were dismantled and the incipient housing they contained was destroyed. The indirect effects were more significant. The policy raised the risks and costs of informal construction in general. Insecure tenure reduced the willingness of households to start their own house construction, or to invest in housing improvements. The conventional process of gradual housing improvement in the informal sector was thus blocked. 4/ Since more than 50% of the houses in Guatemala City lack legal title, this insecurity of tenure represents a large scale problem.
- 1.12 The account above evades a fundamental issue: why is illegal settlement so pervasive? If security of tenure is highly valued, at least some low income households would be expected to prefer

3/ Recent census data on housing quality are systematically unusable. Fortunately, detailed quantification of each deficiency is not a critical ingredient for a demand driven housing program. The best attempt to make sense of the data is the study by Clarke (1996), in the project files.

4/ It is a striking feature of Guatemala's informal neighborhoods to see that houses, established more than five years before have not upgraded beyond the original wooden planks. This unwillingness to invest in permanent construction is very likely linked to the pervasive insecurity of tenure.

legal purchase to illegal invasion. ^{5/} In fact, registered title to low cost land is not only rare, it is illegal. Municipal regulations specify minimum set asides, plot size, and service standards for water, sewage, drainage etc. The subdivision and sale of plots that do not meet these standards is illegal and such properties cannot be registered. The distortion in the land market caused by these regulations is not trivial. A study prepared for the present program showed that full compliance with all regulatory standards in Guatemala City requires a sales price for the smallest legally permissible plot to be more than \$3,500 ^{6/}. (See also Section 4 below for a brief discussion of the environmental consequences of this distortion). For the 60% of urban households with total monthly incomes of \$200 or less, the minimum price of a legal lot represents more than 18 months of total income. For these households there has been no alternative to invasion. The de facto prohibition on legal purchase of suitable land by low income households is not restricted to Guatemala. However, the heightened degree of insecurity has made the consequences of prohibition unusually severe.

c. Institutional Actors

- 1.13 There is another explanatory factor in the poor performance of the informal sector in Guatemala. The institutional support needed to install public infrastructure has been very scarce. Public utility companies have been hampered by the usual financial limitations. Moreover, they too are caught in the labyrinth of municipal land regulations. Utilities are legally prohibited from providing infrastructure connections to households without legal title. In many countries, NGOs are able to help fill this institutional gap. However, an assessment of agencies active in urban neighborhoods found very limited capacity to execute upgrading or housing projects.
- 1.14 A few agencies, both private and public, do have the technical and financial skills to support low income households in the informal sector. In Guatemala city for example, a municipal department has developed a model for providing potable water to informal neighborhoods using a single meter to serve several households ("agua en bloque"). A number of savings and loans cooperatives have a substantial portfolio of housing loans. Nevertheless, while a number of groups have provided informal neighborhoods with a political voice, few have developed the skills needed to prepare or execute urban projects.

^{5/} Illegal invasion of public land is rarely cost free to the occupants. The patrons and organizers of an invasion and the illegal subdivisions invariably require payment for their services. Since the transaction is not enforceable at law, it is not uncommon for the same illegal plot of land to be "sold" to more than one household.

^{6/} To explore the possible impact that deregulation might have on land prices, some basic cost analysis was carried out. This suggested that plots costing less than \$800 might come onto the market on the outskirts of Metropolitan Area if a set of truly minimum standards were instituted. (Further details are in Project Files). Outside the Metropolitan Area, price levels would be lower though the impact of deregulation perhaps less dramatic.

3. The Formal Housing Market

- 1.15 The market for houses produced by the formal construction industry is constrained by the reach of the financial sector. In turn, the ceiling on the mortgage market is set by income distribution. Although this means that Guatemala's formal housing market is quite small, private developers have shown considerable initiative in exploring the low end of their market.
- 1.16 Over the first half of the 1990s formal housing production in Guatemala averaged about 5,000 houses a year, rising to perhaps 7,000 more recently. A few large developers, with close links to the banks that provide construction loans and long term financing, dominate this market. Their representative product is a house costing some \$18,000 destined for households with monthly income of more than \$1,000 a month. However, by 1994 commercial developers had begun to make an effort to expand production by producing lower cost units. Aiming at households whose income are between \$400 and \$500 a month, the houses are no more than 24m.² in size, without internal finishing, and now cost around \$7,500. The production of such houses has expanded sharply over the past 18 months as the Government's subsidy program has picked up support. (See Section C below.)
- 1.17 Although these unfinished houses are among the more modest low cost units produced by the unaided private sector in Latin America, housing developers have argued that the cumbersome and inflexible process of obtaining construction licenses drives up their costs unnecessarily. Work has begun to develop standardized requirements for all municipalities in the Department of Guatemala and to set up a "single stop" process for all utility permits and construction licenses.
- 1.18 The numbers from the construction industry are broadly compatible with those from the financial sector. In 1995 the total net increase in mortgage based lending for housing may have been around \$50 million. ^{7/} This corresponds to some 2,900 loans. This limited activity is largely a function of income distribution. Nevertheless, with a modest amount of help, there could be a significant potential market among the approximately 8,000 middle income households that currently cannot afford the debt service required even for the lowest cost unit now offered by commercial developers.
- 1.19 It is also evident that the financial system, although responding to a sustained program of liberalization, is still neither deep nor stable. Interest rates on loans have fluctuated widely over the past two years, a critical factor since all mortgages are issued

^{7/} The structure of the mortgage market appears to be as follows: in 1995, unaided commercial banks issued \$12 million in loans, the state managed agency, the FHA insured an additional \$20 million in commercial loans (See Annex I for its functions), and the state owned bank CHN issued \$18 million.

with variable interest rates. Over the 8 months to July 1997, interest rates on housing mortgages have dropped from 26% to around 22.5%, while inflation has remained constant at around 10%. The positive effects of such a fall are limited by the knowledge that the process could readily be reversed. Reduced government borrowing, which allowed the interest rate to fall, could rise again if the fiscal position deteriorates. Long term lending will not expand significantly unless stable and predictable interest rates become established. A more complete account of the market for formal sector financing is in Annex I.

4. Urban Development and the Environment

- 1.20 Every year, the informal neighborhoods in the cities of Guatemala expand by more than 20,000 additional houses. By definition these neighborhoods do not follow regulatory guidelines. As a result they often encroach on valuable environmental assets, and damage environmentally fragile locations.
- 1.21 These informal areas invariably lack basic sanitation services when they are formed. The very slow process of installing adequate water and sanitation means that they constitute a public health hazard for an extended period of years. From this perspective, the municipal regulations requirements designed to ensure adequate standards for urban development have had a systematically perverse impact. Excluding the poor from the legal market, the regulations prolong the insecurity that inhibits private investment. Public utilities are also hamstrung by the same regulations: without legal title the utility companies are not supposed to install permanent infrastructure, further delaying the upgrading process.
- 1.22 The bulk of urban population growth over the last decades has been located in the Metropolitan Area of Guatemala City, where this informal process of urban development has taken on an especially hazardous character. The topography of the area is characterized by numerous steep canyons that cut through the urban fabric. (See Map Section). Their steep slope and vulnerability to land slides makes these areas unsuitable for construction so that they have been zoned as 'green' areas in the city development plan.
- 1.23 As urban expansion accelerated in the 1970s the first lands to be occupied were publicly owned areas suitable for construction. These have become increasingly scarce, so that low income households have targeted the areas in and around the canyons. Although posing varying degrees of risk to their inhabitants, these hazardous areas have provided low income households with the least bad of a very poor set of options. Currently as many as 200,000 households may be living in such circumstances.

C. The Lessons of Experience: Housing Policy and Bank Operations in Guatemala 1987-1997

- 1.24 For 20 years the Government of Guatemala, with sustained support from the IDB, used a public sector Bank (BANVI) to produce and finance housing for low income households. In response to the chronic financial difficulties created by this model of housing policy, a Housing Fund (FOGUAVI) was set up in 1996 to provide second tier financing via subsidized interest rates to middle income households. Commercial banks managing FOGUAVI resources as trust funds, originate loans to middle income households for the purchase of housing produced by private developers. Annex II discusses how the lessons learned from these policies shaped the strategy adopted in the present Program.
- 1.25 During the second half of 1996 the Government introduced a law to give the housing sector a firmer institutional basis, by creating the Vice Ministry of Housing (VMV) within the Ministry of Economy. More important was its reform of subsidies. Approved in December 1996, the law required FOGUAVI to introduce programs that combined direct subsidies with loans issued at market rates. 8/
- 1.26 The policy dialogue between the Government and the IDB that began in July 1996, took place in an environment in which very substantial advances had already been determined: the institutional framework of supply side public housing programs had been dismantled, and the principal of transparent demand side subsidies had been established. Moreover, the Peace Accords of December 1996 included a commitment by the Government to give priority to resolving the housing problems of the poor. The preparatory studies and policy discussion for the present operation therefore focused on four principal issues: the design of the subsidy program, the management of housing loans, the expansion of FOGUAVI's targeting goals, and a strategy for handling the problems of the urban land market.

8/ As of July 1997, an amendment to the law has been drafted and presented to Congress transferring responsibility for FOGUAVI and the VMV to the Ministry of Communications, Transport, Public Works, and Housing (MCTOPV). The direct subsidy is to be introduced before October 1997.

II. PROGRAM

A. Objectives

- 2.1 The Government is committed to a housing sector strategy that seeks to improve housing conditions in Guatemala, particularly among the poor. The goal of the present program is to support this strategy by developing and implementing policies that will (i) improve the equity and efficiency of Guatemala's housing markets; and (ii) increase the level of investment in housing occupied by low income households.
- 2.2 The specific objectives of the Program are:
- a) To improve housing conditions among low income households and induce additional private investment in housing by designing and implementing an efficient and well targeted subsidy program;
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 - c) To improve the formulation and implementation of housing policy by expanding the role of NGOs, community based organizations and other representative organizations;
 - d) To improve the performance of urban land markets, particularly those accessible to low-income households;
 - e) To slow the rate of environmental degradation associated with urban development by strengthening environmental management, particularly the management of natural hazard risks in the Metropolitan Area of Guatemala City.
 - f) To promote the development of an efficient secondary mortgage market.

B. Program Overview

- 2.3 The Program will rely on two principal instruments: a demand side subsidy and a package of legal and regulatory reforms to promote the development of a legally recognized market in low cost urban land.
- 2.4 The subsidy program will provide a transparent up front sum to reduce the cost of a housing solution. To get access to the subsidy, eligible households will themselves have to come up with a substantial contribution in cash. For middle income households, the subsidy together with the contribution will buy down the size of the mortgage needed to acquire a completed house. For low income households the same program will generally serve a different function: it will provide the resources to improve quality of the (informally produced) housing these households currently occupy.

- 2.5 The program defines a clear and crucial task for the Government in its role as the source of financing for the subsidies. In contrast, assessing household credit worthiness, issuing loans, designing and constructing the housing solutions, are all tasks that will be undertaken by private sector enterprises. The Government will not provide resources, directly or indirectly, for credit.
- 2.6 To ensure that the subsidy is really accessible to low income households, the Program will rely on the intermediation of NGOs and community groups. The Program will provide resources so that these groups can help communities identify, design and execute community upgrading projects. Specialized NGO's will also help administer the subsidies and appraise the projects.
- 2.7 The Program's second principal instrument is the reform of land markets. For low income households, the dysfunctional land market is currently a major constraint on their willingness to invest in housing. The Program will support a large scale land title regularization policy to resolve the problem of illegality in existing informal neighborhoods. In addition the program will support a radical reform of municipal land-use regulation. This will allow private landowners to put low cost plots of land on the legal market. These "progressive subdivisions" will begin with very low service standards but households will have access to the subsidy program to begin the improvement process more quickly. These reforms will allow a legitimate private market accommodate future urban expansion and so reduce the incentive to invade public lands.
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C. Components

- 2.9 The Program will consist of 4 components that will support changes in policy, the implementation of new institutional arrangements, and an increase in public investments in housing.
- 1) Direct Subsidy (\$91.9 million)
 - 2) Land Market Reform (\$5.85 million)
 - 3) Environmental Management (\$500,000)
 - 4) Institutional Development (\$4.44 million)

1. Direct Subsidy Program (\$91.9 million)

- 2.10 The component will offer direct subsidies to households whose total income is less than four minimum salaries, approximately \$400 a month. The maximum subsidy will be \$2,000 per household, and within this limit will be directly conditioned on the household's own cash contribution: \$3 subsidy for every \$1 contributed, up to the maximum. To be eligible for the subsidy, the total cost of the housing solution must be no greater than \$10,000.

Direct Subsidy: Summary of Program Parameters			
Parameters	Subsidy Clients		
	< 2 monthly minimum salaries	< 4 monthly minimum salaries	> 4 monthly minimum salaries
Maximum Subsidy	\$2,000		Not eligible
Relationship of Own Contribution to Subsidy	1:3		
Use of the Subsidy	Housing improvement, upgrading, and selfbuild Land regularization with registered title Progressive lots	Purchase of a new house (maximum price of \$10,000) Commercial Urbanized lots	

- 2.11 To allow one set of program parameters to help households in two very different market segments, the subsidy program will have two delivery modalities: a Social Window and a Commercial Window, explained below.

a. Social Window (\$55.4 million)

- 2.12 This modality is designed to help low income households, those with monthly incomes below two minimum salaries, approximately \$200. Applications will be made by groups of households, usually through community association, using procedures similar to those developed for Social Investment Funds. They will use the subsidy, together with their own contribution, to finance projects to improve their housing conditions through a wide variety of actions.
- 2.13 The projects, to be eligible for subsidy financing, must provide each participating household access to piped water, a minimum sanitary facility, basic environmental safety and registered land title. In this way, the subsidy will ensure households will attain at least a minimum standard of health and safety. Households that already meet these standards will be free to use the subsidy to upgrade their housing in whatever way best fits their circumstances. They may choose to reconstruct their house with permanent materials, add on additional rooms, improve bathroom or kitchen facilities, or mitigate environmental hazards. Some may be able to acquire and service a green field site.

- 2.14 To accelerate the start-up phase of the low income projects, this component will provide resources so that the Housing Fund (FOGUAVI) can directly contract experienced agencies to help identify, design and supervise these upgrading projects. By the end of the Program, these agencies will be able to undertake these preinvestment activities on their own, using advances from the subsidy.
- 2.15 FOGUAVI will run workshops for agencies interested in the Program, to familiarize them with the procedures for establishing beneficiary eligibility and for project preparation. Other NGO's will be contracted to evaluate project proposals and to supervise project's execution.

b. Commercial Window(\$36.5 million)

- 2.16 For the middle income households of the target population (monthly incomes between two and four minimum salaries, \$200 to \$400 a month), the subsidy plus the household contribution will provide a down payment large enough to allow these households to buy a new complete, albeit modest, house. The subsidy buys down the size of the credit required, making the mortgage payments accessible to households currently excluded from formal private financing. Facing loan-to-asset ratios of 60% or less, commercial banks will have an incentive to offer mortgage financing to households lower down the income scale than their current clientele. Government resources will not be used for credit directly or indirectly.

c. Scope and Dimensioning

- 2.17 During the execution of the Program, the Direct Subsidy Component will provide subsidies of up to \$2,000 to about 26,000 low income households and 18,000 middle income households. The project's technical files include an analysis of these dimensions.

2. Reform of Land Markets (\$5.85 million)

a. Tenure Regularization in Informal Neighborhoods (\$4.35 Million)

- 2.18 This subcomponent will speed up and expand the process of regularizing tenure in existing neighborhoods located on invaded public lands. The component will finance (i) the preparation and implementation of a package of legal and regulatory reforms to facilitate the transfer of public lands to private use, and (ii) the services households will need to obtain individual, registered title to the lots which they currently occupy. With the security of legal title, households will increase their own investments in housing and thus accelerate the process of housing improvement in low income neighborhoods.
- 2.19 As a matter of course, upgrading projects supported by the Direct Subsidy Component will carry out land regularization if the

neighborhood currently lacks legal title. Adjudication (titling process) will proceed, according to expedited procedures, during the course of the project as the parties to the individual lots are identified and the new subdivision layout is completed. Thus, households are likely to have registered titles even before the physical upgrading project is complete. In addition to the regularization carried out in conjunction with upgrading projects, the component will finance outreach activities to identify and implement land regularization projects in neighborhoods that have not applied for subsidies. To avoid giving further incentives for land invasion, the Operating Regulations will stipulate that lands invaded after 1995 will not be eligible for regularization.

b. Progressive Subdivisions (Opening a Low Cost Land Market)
Subcomponent (\$1.35 million)

- 2.20 The subcomponent will finance the preparation and promotion of changes to existing housing codes enacted at national and local levels. These changes will create the regulatory framework so that private landowners are legally permitted to subdivide and sell land with minimum levels of services. The result will be to open a legal market of land to low income households. FOGUAVI will not purchase land using Program resources. To give landowners additional incentives to enter this low end market segment, the component will also finance the services needed to access the expedited land titling and registration procedures developed under the previous subcomponent. To provide municipalities with an incentive to undertake the needed regulatory changes, FOGUAVI's operating regulations will only approve the granting of subsidies for housing located in municipalities who make the necessary changes to their land use regulations and urbanization standards.
- 2.21 In order to open a land market accessible to the low income population, the progressive subdivisions in Guatemala City will meet, but not exceed, the following agreed standards: maximum lot size of 50 square meters; pedestrian access only (no vehicular access) to lots; public water pipes within 150 meters of every lot (no individual connections); minimum 10% set-aside for public facilities (including walkways); minimum sanitation services (latrines). Comparable norms will be developed for localities in the rest of the country.
- 2.22 To provide a real inducement for landowners to enter this new market it is critical that the process of producing, authorizing, and legalizing a progressive subdivision be made as simple and as rapid as possible. Limiting subdivision preparation to the drilling of a well and laying out the plot sites, for example, should enable a turnaround time of no more than three months.
- 2.23 The low cost, low service condition in which the progressive subdivisions are put on the market will only be the first stage of a process of more rapid improvement. Eligible households may use

the subsidies to purchase the lots and to initiate the process of improvement and installation of urban services.

c. Reducing Costs of Commercial Development Subcomponent (\$150,000)

2.24 This subcomponent will provide technical assistance to support a process initiated in March 1997 to develop a single, unified regulation for construction and urbanization standards and permitting for the entire Department of Guatemala. Technical assistance funds will support FOGUAVI, as Coordinator of the initiative, to develop a model of simplified regulations and procedures. Special attention will be given to developing appropriate construction and urbanization standards for commercially-produced "social interest" (low cost) housing.

2.25 The model regulations, procedures, and construction standards will first be developed and promoted for the Department of Guatemala, and later for the rest of the country. These standards will apply to commercially-produced "social interest housing" and will therefore be considerably more demanding than the requirements for the progressive subdivisions.

d. Scope and Dimensioning

2.26 During the execution of the Program, the regularization subcomponent will provide titles to about 43,000 households and the progressive subdivision sub component will assist the subdivision and titling of about 13,500 low cost plots.

3. Environmental Management component (\$500,000)

a. Exclusion Zones: Mapping Urban Areas (US\$250,000)

2.27 The Project will provide incentives for households to make location choices in areas suitable for housing, while reducing incentives for additional households to occupy hazardous or environmentally protected areas. To do so, the Project introduces a strategy of delineating environmental priority areas throughout the country. Within these "exclusion zones," no proposal to improve or develop a neighborhood will be eligible for subsidies, land regularization, or other program benefits.

2.28 For all urban areas participating in the Housing Program, the component will finance the delineating environmental exclusion zones, using the following methodology: All the different environmental protection criteria that are applicable to a particular urban area will be mapped. Then, in consultation with the environmental authorities and local representatives, a very limited number of the areas (approximately 5) will be chosen as having the very highest priority for protection. These areas will be mapped as designated "exclusion zones." (See Map Section for example). FOGUAVI and local authorities will make these zones -

and their exclusion from Program benefits - known to potential program beneficiaries, authorized entities, developers, and banks. In the review of project proposals for subsidies, FOGUAVI will deny program benefits to all projects which are located, or propose to locate, in areas mapped as exclusion zones.

- 2.29 In the case where existing communities occupy areas at high risk to natural hazards (landslides, for example), they will be provided with information about the risks they face and their options for alternative locations which would be supported by subsidies. Beyond the cost of developing the maps, the component will finance training for officials in the methodology and application of the exclusion zones, as well as the development of informational material for the public. About 40 cities, with a population greater than 50,000, will be mapped under the program.

b. Managing Environmental Risk: Metropolitan Area of Guatemala City (US\$250,000)

- 2.30 In the metropolitan area of Guatemala City, around 200,000 families live on the slopes and edges of steep canyons - areas with varying degrees of risk to landslides. Each year since the 1980s, an additional 8,000 low income households establish homes in these areas. The environmental management component will provide technical assistance to distinguish two kinds of zones:
- a) The areas where the risk can be effectively reduced by simple works (such as containment walls, surface drainage, setbacks and vegetation plantings) will be identified. Households will receive technical assistance and resources through the subsidy program to undertake these mitigation works.
 - b) "High risk zones", where such mitigation works would not constitute prudent investments will be identified. Households in these zones will receive informational material explaining how relocation would enable them to qualify for a subsidy. (See Map Section).
- 2.31 In addition, technical assistance will help the municipal authorities, as well as at-risk neighborhoods directly to improve their capacity to respond to emergency in these communities.

4. Institutional Development (\$4.5 million)

- 2.32 The Institutional Development Component will finance: (i) professional services to manage the subsidy program (\$1.35 million); (ii) professional services to manage the land reform component (\$1.23 million); (iii) setting up a management information system for the program (\$500,000); (iv) providing technical assistance to develop the mortgage market (\$250,000); (v) professional services and logistical support for the promotion of the Program and training of the private agencies participating in its execution (\$192,000); (vi) carrying out sector and policy studies (\$336,000); annual monitoring and evaluation studies

(\$250,000); (vi) the PPF expenditures (\$335,000). An account of how these sub components will operate can be found in Chapter III.

D. Access to Credit

- 2.33 Low and Middle income households currently have very limited access to small scale loans to improve their housing, and face similar difficulties as micro-entrepreneurs when seeking small credits. Taking advantage of the Banks' recent reformulation of the Global Program for Small and Micro Enterprises (886/SF-GU), it is proposed to amend the regulations of that operation so that the purchase and improvement of housing (not to exceed US\$10,000) would be eligible for total value financing. This proposal is consistent with the objective of the Global Credit Program which is to reach a population that has traditionally been excluded from the formal financial system. By allowing low cost housing to be eligible within the Global Credit Program, commercial banks would be encouraged to explore this potential market. At the same time, serving the wider spectrum of low income borrower's demand would encourage the more efficient allocation of Program resources. Finally, it is important to note that for the poor, housing is not only a consumption good but also is frequently a critical capital good for productive activities which take place in the home.

E. Program Components and IDB Policy

- 2.34 In terms of IDB Policy, OP-751 sets out three principal objectives for housing programs improving housing conditions among the low income population, improving the efficiency of public expenditures in the sector, and improving the efficiency of market housing. The present program is designed to actively pursue all three goals: (i) low income households will constitute more than 70% of program beneficiaries; (ii) the adoption of demand side subsidies will greatly improve the efficiency of public expenditures; and (iii) promoting the efficiency of land market is a principal focus of the Program.
- 2.35 IDB practice has been to require that where land purchase has been necessary for an operation, counterpart resources will be used. It is evident the subsidies financed under this operation will be used to purchase housing, which necessarily includes the land on which it stands. Given that the Program is intended to help establish sustainable sector wide policies and that all purchases of land for housing will be carried out by individual households, no distinction between Bank and counterpart resources for the purchase of land is proposed. However, under no circumstances will Bank resources be used to finance the purchase of property owned by the Government.

F. Cost and Financing

1. Program Costs

- 2.36 The total cost of the Program components will be \$102.8 million. Unallocated funds amounting to approximately \$850,000 have been included to allow for unanticipated cost variations in the environmental and institutional components. The Program does not fix a numerical limit on the total number of subsidies provided nor on the number of land titles processed. Consequently it was not considered necessary to estimate cost variations for these items. Inspection, commission and interest costs for the four years of Program execution, have been capitalized into the Program cost table. Total Program cost is therefore estimated to be \$108.3 million.

2. Program Sustainability and Fiscal Constraints

- 2.37 The present Government's expenditure targets for the housing sector were set in the context of the Peace Accords. These committed the Government to devoting up to the equivalent of 1.5% of fiscal revenues to the housing sector. In practice, local fiscal resources budgeted to FOGUAVI for 1997 amount to the equivalent of \$12.2 million (approximately 0.75% of total government fiscal revenues). To avoid a situation in which Bank resources simply displace local resources, the base assumption is that the Government's current assignment of locally mobilized resources will be maintained over the life of the program. This will help ensure the sustainability of the policies described above, after the execution of the Program. At the same time, it is important that the Government's ability to respond to changing macro economic circumstances is not unduly hampered. *Consequently, a contractual condition is proposed so that fiscal resources, transferred in cash to FOGUAVI, in any one year, will be (i) no less than 0.75% of the Government's total fiscal revenues, or (ii) equivalent to US\$12.2 million, whichever is lower.*
- 2.38 Given projected tax effort and economic growth rate, the commitment of 1.5% of revenues to housing, implies that the annual fiscal limit for the sector will rise from its current level of around \$23 million to about \$35.9 million by 20001. These projections set a maximum ceiling for the Program of around \$128 million, well above the expected total cost of \$108.8 million. The difference is due to capacity constraints in the specific markets in which the subsidy program will intervene. (The detailed analysis of program dimensions is in the Project Files). By the fourth year, program expenditure will rise to some \$32 million compared with the fiscal limit of \$36 million.

3. Pari Passu and Bank Financing

- 2.39 The present Program has been designed to provide broad spectrum support to the Government's housing strategy. In this sense, all

Government resources assigned to FOGUAVI constitute counterpart financing. The cost table that follows has been prepared under the assumption that the current fiscal and macro-economic conditions will be maintained. This scenario would permit the Government of Guatemala to finance approximately 45% of total program costs. However, to take account of the uncertainty of future macroeconomic and fiscal developments, the Program will establish two parameters for local counterpart resources: (i) the minimum *pari passu*, to be assured on an annual basis for the operation as a whole will be 20%. (ii) Beyond this minimum, counterpart funding will be set in accordance with the contractual condition described in Para. 2.37 above. The Bank's loan of \$60.0 million will be in US dollars from the Single Currency Facility of the Bank's Ordinary Capital.

- 2.40 To help insure the sustainability of the policies and programs introduced under this operation the Guatemalan Government has requested supplemental resources for continued execution of the Program be available. To this effect, it is proposed that supplementary financing, equivalent to US\$20,000,000, could be provided subject to the following conditions: (i) 50% of the Program resources have been executed; and (ii) verification that the objectives of the Program are being reached and Program execution has progressed in accordance with the performance benchmarks. At that time, a memorandum describing the progress of the Program, the amount of resources committed and disbursed, and requesting the authorization for additional financing shall be presented to the Board of Directors for its considerations. These supplementary resources would be available exclusively for financing the registration of property titles under the Land Market Reform Component, and subsidies provided through the Social Window. In all other respects, the supplementary financing would be subject to the same terms and conditions applicable to the present Program, including the commitment of counterpart resources in accordance with the provisions of Paras. 2.37 and 2.39.

COST TABLE

GUATEMALA HOUSING PROGRAM (US\$ MILLIONS)				
Cost Category	Source of Financing			
	Total Cost of Component	Gov. of Guatemala	BID	Percentage of Total Cost
INVESTMENTS IN HOUSING SUBSIDIES	91.90	46.00	45.90	85%
Commercial Window	36.50			
Social Window	55.40			
LAND MARKET REFORMS	5.85		5.85	5%
Regularization	4.35			
Progressive Sub-Divisions	1.35			
Commercial Development	0.15			
MANAGEMENT OF ENVIRONMENTAL HAZARD	0.50		0.50	0.5%
Urban Environmental Mapping: Exclusion Zones	0.25			
Guatemala City: Risk Zones	0.25			
INSTITUTIONAL DEVELOPMENT	4.44	2.00	2.50	4%
Professional Services - Direct Subsidy	1.35			
Professional Services-Land Reform	1.23			
MIS	0.50			
Studies, Monitoring and Evaluation	0.59			
Assistance Mortgage Market	0.25			
Technical Assistance to Participating Entities	0.19			
PPF	0.33			
TOTAL COMPONENTS	102.70	48.00	54.70	95%
UNALLOCATED	0.85		0.85	
PROGRAM COSTS	103.55	48.00	55.55	
FINANCING COSTS	5.20	0.80	4.40	5%
Interests	3.80		3.80	
Credit Commission	0.80	.80		
Inspection	0.60		0.60	
TOTAL COST OF OPERATION	108.80	48.80	60.00	100%
Percent of Total Cost	100%	45%	55%	

III. PROGRAM EXECUTION

A. Program Management and Initiation

- 3.1 The executing agent for the Housing Program is the Guatemalan Housing Fund (FOGUAVI), under the Ministry of Communication, Transport, Public Works and Housing (MCTOPV). FOGUAVI has provided the counterpart team through Program preparation and will be responsible for all aspects of project execution, including the interface with the Bank and disbursement of program resources.

1. Coordination

- 3.2 FOGUAVI, whose director will report to the Minister, will be responsible for the execution of the Program. The Board of Directors of FOGUAVI will formally approve all subsidy and project applications in accordance with the criteria established in the Program's Operations Regulations. Operating units corresponding to the primary investment and technical assistance components will be established, and their coordinators will report directly to the Director of FOGUAVI. *The terms of reference/job profiles for the unit coordinators will be agreed with the Bank.*

2. Program Initiation

- 3.3 FOGUAVI has been preparing for the start-up of the Program through extensive discussions with banks and developers since March. In addition, a PPF with the IDB has been approved. The PPF is intended to help FOGUAVI develop the detailed operational policies and the institutional arrangements required to implement the Government's new housing strategy. Some preparatory tasks have already been completed and the remainder will be carried out between September and December. The PPF is financing work in five main areas: (i) environmental management; (ii) land market regulatory reforms; (iii) management of low income housing projects (Social Window); (iv) design of a management information system; and (v) developing staff manuals for FOGUAVI's operating units.

3. Principal Operating Units

a. The Direct Subsidy Unit

- 3.4 This unit will have two operating teams. The "Commercial Window" team will consist of existing FOGUAVI staff. Their principal immediate task is to adjust and strengthen the existing arrangements for transferring and monitoring the resources managed by the commercial banks. The second team in the unit, the "Social Window" Team will have its own coordinator. The Social Window Team will have the relevant expertise and will be hired with Program resources. They will manage the outreach, project preparation and supervision of the community level upgrading projects.

- 3.5 The unit will be responsible for approving intermediate agencies to handle subsidies and for contracting technical assistance and supervisory services. It will review the preliminary appraisal of beneficiaries carried out by the approved agencies.

b. The Land Market Reform Unit

- 3.6 This unit will be responsible for: (i) the implementation of the tenure regularization subcomponent; (ii) the promotion of the legal and regulatory changes necessary for the Progressive Subdivisions Subcomponent and to speed up enforcement processes for mortgage guarantees; (iii) promotion of model housing codes for commercial development and of streamlined procedures for construction permits; (iv) establishing environmental exclusion zones country wide; and (v) the mitigation of environmental hazards in subsidy-supported projects in the metropolitan area of Guatemala City and the technical cooperation activities that strengthen the capacity to respond in case of an emergency.

c. The Management Information Unit (MIS)

- 3.7 This Unit will create and manage a Management Information System (MIS) to assist the execution of the SIAVI program between its multiple participants, and to provide information about housing sector performance. The information required by the IDB regarding disbursements and other matters will be handled by this unit.
- 3.8 In setting up these institutional arrangements, an important goal is to limit the growth of permanent personnel, and to maximize the subcontracting of specific project services. The total number of incremental permanent staff hired under this program is not expected to exceed 15 for all the units. In the case of the Social Window team and the urban land unit, FOGUAVI may choose to hire the personnel either as individual staff, or to hire a firm to provide a complete range of local and international expertise.

B. Execution of Program Components

1. Direct Subsidy Component

- 3.9 Detailed staff manuals will be prepared under the PPF between September and December 1997; *FOGUAVI's establishment of the Direct Subsidy unit - understood to comprise the official adoption of operating regulations and manuals for both the Social and Commercial Windows, satisfactory to the Bank and the hiring of both the unit chief and the coordinator of the Social Window team - is a condition prior to first disbursement under this component.*
- 3.10 FOGUAVI will use program resources to finance a social marketing campaign involving radio and newspaper announcements and distribution of promotional material.

a. Direct Subsidy Component : Social Window

- 3.11 The low income projects financed under this subcomponent will perform much like a Social Investment Fund. This means that community organizations, with professional services provided by authorized agencies (an NGO, cooperative, municipality, or other agent) will identify and prepare project proposals which will include plans for physical works, land regularization, and financial arrangements. If the project is approved they will also be responsible for executing the project. FOGUAVI's role is limited to approving requests for subsidies and supervising project execution. On approval, each household will receive a "voucher" indicating the amount of subsidy awarded and the contribution required from the beneficiary. The authorized agency will be responsible for holding beneficiary contributions and will be responsible for verifying the use of voucher proceeds and contributions to FOGUAVI.
- 3.12 The management of this kind of project involves operational procedures quite novel for FOGUAVI. To help staff get the necessary experience, and to test the draft operating arrangements, the PPF will finance the preparation of five pilot projects. The projects involve land regularization, and works for housing and infrastructure improvements in informal neighborhoods in Guatemala City. A consulting firm with experience in such projects will work with FOGUAVI staff and NGOs to develop: (i) detailed procedures and a staff manual; (ii) the program of technical assistance for authorized institutions who will assist households design and execute projects; (iii) "good practice" and outreach materials for environmental mitigation measures for at-risk neighborhoods; and (iv) technical assistance to municipalities and national authorities.
- 3.13 To help get this subcomponent off to a quicker start, the "demand driven" characteristics of the voucher style program will be complemented by providing program resources so that FOGUAVI can itself identify communities of potential beneficiaries and directly subcontract firms or individual consultants to prepare projects. By the third year of execution, authorized entities will undertake these preinvestment activities on their own initiative.

b. Direct Subsidy Component: Commercial Window

- 3.14 Under the current FOGUAVI housing program, the bank receives loan applications from households that have been prescreened by the developer, and is charged with assessing the applicant's eligibility for FOGUAVI resources and credit worthiness. Under the arrangements proposed for the present Program, the bank will perform exactly the same tasks but with a crucial operational difference. The FOGUAVI resources will constitute a simple transfer; the loan will be made from the bank's own resources. The bank will verify that the applicant is eligible and can make the

contribution required to qualify for the proposed subsidy. On completing the eligibility and credit assessment, the bank forwards the documents to FOGUAVI for official authorization. The purchase of the house by the applicant can then be completed by the bank. The bank then forwards the information regarding the completed transaction to FOGUAVI, including confirmation of the payment by the purchaser of the required contribution and of the subsidy received. The purchaser will receive a certificate with the same data.

- 3.15 FOGUAVI already has extensive experience in serving this market (it will have authorized more than 3,000 loans during the present year) so that institutional capacity is not the concern that it is in the low income subcomponent. Here, the principal risk is that if FOGUAVI were to expand the distribution of subsidies too rapidly in this limited market segment, an increase in the price of houses eligible for the Program is likely. This is largely a short term problem since, in the medium term, the production of housing is sufficiently competitive to ensure that supply would increase in response to the additional demand. To mitigate this risk, a special contractual condition will limit the total number of subsidies distributed by FOGUAVI through the Commercial Window to no more than 5,000 in the first 12 months of execution and 6,000, 7,000 and 8,000 subsidies in the subsequent 12 month periods, respectively. This schedule can be adjusted in accordance with the mechanism discussed in Annex III, Paras. 1.3-1.5. Failure to comply with this condition shall require the suspension of commitments of Program resources corresponding to the Commercial Window until the condition is complied with to the Bank's satisfaction.

2. Reform of Land Markets

- 3.16 FOGUAVI's establishment of the Land Market Reform Unit - understood to comprise the official adoption of operating manuals and regulations satisfactory to the Bank and the hiring of the unit coordinator - is a condition prior to first disbursement under this component.
- 3.17 Some of the activities contemplated under this component could only be carried out with difficulty under existing legislation. However, their timely implementation is not at risk since they can be initiated for the present Program under the legal authority of the Loan Contract. Loan Contracts with Guatemala are customarily ratified by the Guatemalan Congress prior to their signature. Such ratification has the effect of approving the performance of contractual obligations that are inconsistent with existing legislation.
- 3.18 For purposes of implementing the Program, the Loan Contract will clearly establish the fundamental elements of the streamlined procedures for transfers of public lands to private use and authorizing the progressive lots. The procedures required to implement these temporary reforms will be set out in the Operating

Regulations. In addition, FOGUAVI proposes to require that a letter of no-objection to these legal reforms be obtained from the Municipality in which each housing solution or project is located as a prerequisite to qualify for a subsidy.

- 3.19 These arrangements will only be effective during the life of the Program. To establish their benefits for the long run, it is important that the reforms be incorporated into the complex set of domestic laws and regulations that affect housing and urbanization. *Consequently a special contractual condition is proposed such that the Borrower presents to Congress a package of legal reforms acceptable to the Bank, developed under the Land Reform Component, within 18 months of the first disbursement, or once 50% of the Direct Subsidy component resources have been committed, whichever occurs first. Failure to comply with this condition shall result in the suspension of further disbursements of the Subsidy component.*

a. Land Regularization

- 3.20 The Land Regularization subcomponent will involve two sets of activities, those required to: (i) change the designated land use from public to private use for low cost housing; and (ii) legally subdivide individual parcels with registered title. Both sets of activities will be completed as steps in the Social Window's subsidy project cycle. FOGUAVI will also be responsible for the final legal steps in adjudicating (titling and registering in the Property Registry, FOGUAVI window) the individual lots. The authorized entities will be responsible for the technical steps of preparing the site survey, lot maps, and evaluation of the eligibility of potential beneficiary households.
- 3.21 The staff manual setting out how FOGUAVI officials will manage the process will be developed under the PPF in the context of the five pilot projects mentioned above. This should be completed by December 1997.

b. Progressive SubDivisions (Opening a Low Cost Land Market)

- 3.22 To permit the legal subdivision and sale of "progressive lots," changes to municipal land use regulations and urbanization standards must be made across the country. PPF resources will fund a consultant to work with FOGUAVI to develop a model municipal regulation that specifies absolute minimum standards. Included in the regulatory changes will be a radical simplification of the process for obtaining development permits and for acquiring registered land title for these lots. FOGUAVI's Land Market Reform Unit will provide the model regulations and procedures to municipalities.
- 3.23 To strongly encourage their adoption, FOGUAVI will only approve the granting of subsidies for housing located in municipalities willing to make the corresponding regulation changes. To assure timely initiation of the Program, municipalities will begin by providing

FOGUAVI with a letter of no objection to the proposed changes. The Subsidy operating regulations will require that, within 12 months of first disbursement, municipalities must incorporate the code changes into their land use and other regulations. (These requirements will only be mandatory for municipalities whose largest city has a population of more than 50,000).

- 3.24 PPF funds will support a consultant to propose changes to national and municipal law necessary to permit the legal subdivision and sale of minimally improved lots. Model municipal regulations will be developed in accordance with the standards described in Para. 2.21.
- 3.25 Landowners wishing to subdivide their land for sale in close association with potential beneficiaries of the Subsidy Component - Social Window, may do so by presenting to FOGUAVI a simple subdivision plan and evidence of an established agreement with an authorized entity. The authorized entity will help identify potential beneficiaries and develop their project of self-build or housing improvement. Upon approval of the project, the beneficiaries will purchase the lots from the landowner and proceed to execute their project in the usual fashion.

c. Reducing Costs of Commercial Development

- 3.26 FOGUAVI is currently working with municipalities in the Department of Guatemala, the National Association of Home Builders (FENACOV), the Institute of Mortgage Insurance (FHA) and others, to develop simplified regulations and procedures which municipalities will use for issuing construction licenses for commercial developments of residential housing, with special attention given to "social interest" (low cost) housing.
- 3.27 This component will provide technical assistance to FOGUAVI to develop such a model regulation. The diverse standards and procedures currently in effect will be reviewed and, through a process of broad technical consultation, a uniform and appropriate standard will be developed and promoted throughout all municipalities in the Department of Guatemala, and the rest of the country.

3. Environmental Management Component

- 3.28 Proposals for managing the environmental aspects of the Program were approved by the CESI at its meeting on January 14 1997. The corresponding environmental report was considered by the CESI/TRG at its meeting on August 22 1997 and the arrangements described below incorporate the committee's observations.

a. Exclusion Zones: Urban Areas Country-wide

- 3.29 FOGUAVI will contract the preparation of environmental exclusion zone maps in some 40 key cities (those with population over 50,000)

during program execution, in addition to the six maps completed during Program preparation (Guatemala City, Esquintla, and Totonicapán, Siquinalá, San Lucas, and Chiquimula). Once a map is prepared for a particular locality, program regulations will require compliance with its exclusion zones to establish the eligibility of any specific subsidy application.

- 3.30 The procedure for preparing the maps will require that consultants first identify and map the different environmental protection criteria applicable to a particular urban area. Then, in consultation with the environmental authorities and local representatives, a limited number of the areas will be selected as having the highest priority for protection, and will be mapped as designated "exclusion zones."
- 3.31 *To ensure that FOGUAVI gives high priority to the preparation of the environmental maps a special contractual condition is proposed: within 12 months of first disbursement FOGUAVI will present, to the Banks' satisfaction, 15 maps of key cities as a condition for the continued commitment of Program resources; within 24 months continued commitment will require the presentation of an additional 20 maps.*

b. Managing Environmental Risk: Metropolitan Area of Guatemala City

- 3.32 The most important element of the delineation of exclusion zones in the Metropolitan Area are the numerous steep canyons whose 16%-plus slopes put them at risk to landslides and qualify them as unsuitable for construction under local urbanization codes. However, a study was conducted to refine exclusion zones to distinguish between those areas at "high risk" to landslides -based on past landslides, as well as geological and topographical risk factors - and those areas where the risks can be effectively mitigated by simple, low cost mitigation works ("mitigable risk"). The first approximation finds that approximately 180,000 households will be able to apply for the introduction of mitigation measures, subsidies, and other program benefits. (More details on methodology and findings are held in project files).

4. Institutional Development

a. Program Management

- 3.33 The use of Program funds to set up and staff FOGUAVI's operating units are described in the preceding sections.

b. Technical Assistance for Mortgage Market Development

- 3.34 The subcomponent will finance a consultant based in the Ministry to work with the private sector and the relevant public sector agencies to develop and organize a series of technical studies and workshops aimed at guiding the development of a plan of action for

the development of the mortgage market in Guatemala. A summary of the scope of the studies is in Annex I.

- 3.35 The consultant will organize a series of workshops and meetings where the national parties will discuss the results of these studies with experts and professionals linked to these markets in other countries. These workshops will produce: (i) An understanding of the opportunities and challenges for the development of the mortgage market in Guatemala; (ii) the evaluation of the technical, regulatory and institutional aspects needed for the development of the mortgage market; and (iii) a work agenda that specifies the actions that the public sector and private financial actors can take to promote the development of the mortgage market.

C. Monitoring Program Performance: Reporting, Benchmarks, Disbursement and Procurement

- 3.36 The arrangements for monitoring and reporting Program performance, and the expected disbursement and procurement schedules are described in Annex III.

D. Women and Indigenous Households in Housing Markets

- 3.37 There are no formal legal impediments to women owning real estate, and Guatemalan law has registration procedures for recognizing the rights of common law spouses. Nevertheless, the draft housing regulations specify that the housing solutions subsidized by the Program will be in the name of both spouses, or in the woman's name alone should she be a single head of household. Since the Program's resources are not limited to any specific form of housing solution, all group's preferences will be readily accommodated.
- 3.38 The major sources of inequity for women, and for indigenous households, are likely to reside in poorly designed operational practice. Outreach activities will be designed to reach both husband and wife (not just household head), and to encourage couples to register common law partners. In one of the pilot projects financed by the PPF the consultants will work with an NGO specialized in reaching indigenous households; their report will specify how the proposed procedures and materials include both women and indigenous households.
- 3.39 The plans for developing FOGUAVI outreach and publicity activities specify that informational materials will be made available in Quiché, Mam, Cakchiquel and Kekchi as well as Spanish, and that information centers will be opened across the country.

E. Poverty Impact

- 3.40 The official definition of poverty in Guatemala classifies as poor any household whose income is less than 4 minimum salaries, equivalent to about \$400 a month. Under this criteria approximately

88% of urban households qualify as poor and 100% of Program resources will benefit households at or below this poverty line. Beneficiaries will be selected by examining total household income to ensure compliance with program regulations. Currently, the Government devotes almost its entire annual housing sector investment budget to financing about 2,000 houses targeted at households with incomes of approximately \$350 a month; low income households (those with incomes of \$200 a month or less) have very little effective access to these resources. Under the policies supported by the present operation approximately 60% of program resources for subsidies will benefit low income households. The land market interventions may be of even greater impact for low income households although they do not involve large public expenditures (a 1988 study in the Philippines suggested that security of tenure increased housing prices by about 25%). More than 50,000 low income households should benefit from secure land title as a result of Program actions.

- 3.41 Housing authorities in Guatemala are most accustomed to responding to the political constituency of commercial housing developers and the middle income households they serve. It will not be easy for FOGUAVI to give the necessary attention to promoting projects to benefit low income households. *To help the authorities ensure that the low income beneficiaries are given the necessary priority, a contractual condition is proposed such that the percentage of Program actions (subsidies plus land titles) issued through either the "Social Window" or the Land Reform Component will not fall below the following schedule:*

YEAR 1	YEAR 2	YEAR 3	YEAR 4
40%	50%	60%	70%

Failure to comply with this condition will require the suspensions commitments of Program resources corresponding to the Commercial Window until the condition is complied with to the Bank's satisfaction.

IV. BENEFITS AND RISKS

- 4.1 Poor housing conditions are the result of low levels of investment. This operation will increase investment in the housing sector through two principal pathways. The first is directed to the "end use" market where houses are produced and sold to consumers. Here the program will use demand side subsidies to increase the level of public investment and to leverage additional private investments. The second pathway involves the urban land market. Here the program will remove the principal legal and regulatory distortions that have denied secure tenure to the majority of urban households. These two interventions carry risks as well as benefits. This chapter will summarize the equity and efficiency gains that can be expected from the implementation of the Program, and will identify the principal technical and political risks that accompany such a large scale reorganization of the incentive structure of the housing sector.

A. The Subsidy Program

- 4.2 The proposed subsidy program has a variety of advantages when compared with the scheme now in operation. FOGUAVI currently finances loans at subsidized interest rates using banks as trustees. Under the present operation, the transfers required to finance the "up front" subsidies will be explicitly budgeted ex ante, without the uncertainties inherent in public sector lending arrangements.
- 4.3 For the market segment serving middle income households, the subsidy arrangements will promote efficiencies in the supply of housing. The subsidy is linked to the beneficiary's contribution not to the price of the housing solution. Commercial developers thus have an incentive to find ways of offering lower cost units. Better production technology and more attention to demand outside the expensive metropolitan area can be expected.
- 4.4 The operation will also generate greater efficiency in the financing of houses. To begin with, credit evaluation and repayment will improve since commercial banks, facing the correct incentives, will in the future bear all the credit risks. Middle income households will have the option of borrowing from capital markets rather than having to save for the full cost of their house over an extended period. More broadly, the expenditure on subsidies by the public sector will leverage substantial additional resources from the private sector.
- 4.5 Regarding low income households, the social benefits of the subsidies are more significant. Households that currently cannot afford minimally healthy home environments will receive sufficient resources to ensure that their house has potable water, sanitary facilities, and a constructed floor. Particularly for children and

other vulnerable groups, there will be benefits in terms of improved health outcomes.

- 4.6 The structure of the subsidy program - minimal requirements and no distinctions between eligible income groups - is itself a source of efficiency gains. This pared down approach simplifies administration and reduces rent seeking by applicants. Most importantly, it allows households to choose for themselves how best to use the subsidy and thus maximizes the households' welfare gain from each dollar of public expenditure.
- 4.7 The principal risk facing any earmarked subsidy program is "leakage" ^{9/}. Leakage can take many forms but the underlying principle is always the same: the nominal beneficiary, rather than receive the intended improvement in the targeted service, chooses to use the subsidy to purchase other goods or services. This requires beneficiaries to find a way of getting cash by arbitrage, selling the subsidy in some market. The probability that leakage will occur is largely a function of the gap between the market value of the subsidy and its value to the nominal beneficiary. Well intentioned programs that aim at very substantial improvements in the housing conditions of low income families inevitably generate a very large gap. ^{10/} Reducing this risk requires careful attention to the observed housing preferences of the target population and to the size of the subsidy. A paper in the project files presents the data used to establish the amount of the subsidy in the present Program.
- 4.8 Institutional arrangements can reduce the risk of leakage. The present program will operate through intermediary organizations - banks, specialized NGOs, cooperatives and others -. These organizations will establish lasting relationships with the Program, relationships that will affect their sources of income. It is likely that these agencies will have an interest in restraining arbitrage by beneficiary households.

B. Land Market Interventions

- 4.9 The Program aims to intervene on a large scale to open up a "low end" market in urban subdivisions. The gains from removing the existing market distortions are likely to be substantial. Current regulatory requirements for urban subdivisions were intended to

^{9/} Some of the risks that normally accompany the introduction of demand side subsidies are much reduced in the present case. In Guatemala, banks, housing developers and middle income clientele have successfully collaborated over the 18 months of FOGUAVI's operations. The shift to a fully demand side subsidy will thus be less drastic than for cases where public housing production has persisted. It is nevertheless likely that the change in the management of credit will produce a temporary fall in the number of transactions.

^{10/} In Latin America the classic manifestation of this error has been all too familiar for the past 40 years: the apartment block in a central location financed by the public sector and nominally intended to benefit the very poor, yet occupied in the end by middle income households. These programs also tend to crowd out the housing investments that families would have made in the absence of the subsidy, reducing the net increase in housing investment resulting from the public expenditure on the subsidies.

ensure that minimum service standards were available to the whole population. In spite of these benign goals, the effect of such regulation has been systematically perverse. Without a legal market in low cost land, the growth of the urban population has been accommodated by illegal invasion. This mode of accommodation is highly inefficient since insecurity of land tenure inhibits investment and blocks the normal process of up-grading. Moreover, the disorderly and conflicted process of informal subdivision increases the cost of any subsequent effort to introduce urban infrastructure.

- 4.10 So far as existing informal neighborhoods are concerned, the one time cost of regularizing land tenure is very modest and will initiate a flow of benefits as households with heightened security increase the investment of their own resources in housing improvements. The component that promotes Progressive Subdivisions has a more ambitious goal. It aims at ensuring that future urban growth can be accommodated in a more efficient fashion. Municipalities will be induced to drastically reduce the minimum standards required of subdivisions. The incentive to invade lands and settle in risky areas will be reduced as the legal supply of low cost plots increases. Subsequently, the subsidy will be available to kick start the process of upgrading services. Since these subdivisions will be "planned" rather than invaded, the cost of introducing infrastructure will be little more than that encountered in green field site developments.
- 4.11 The process of changing the legal framework of land regulation, and of regularizing land titles, may be halted for bureaucratic or political reasons. This would limit the scope or the permanence of the reforms. However, the major risk to the successful implementation of the land market interventions is that urban land with legal title would continue to command too high a price, so that invasions by low income households would continue to take place. Such an outcome might result from some further distortion in the land market not addressed by the program. One possibility is that the supply of land may not be competitive in some urban markets. It is difficult to estimate this risk in the present state of uncertainty about the structure of land holding in urban areas, but it is clear that a solution would require action beyond the scope of the present program.

C. Environmental Management

- 4.12 If the land market and subsidy interventions proposed by this program are implemented on the scale expected, there will be a significant change in the way that urban development impacts the environment, and conversely, on the risk posed by environmental hazards to the urban population. The standard instrument to enforce standards for good land use in urban areas is the regulation of building licenses. This is essentially a negative incentive, and one that, de facto, has been ignored by the majority of households. The present program offers the positive incentive of a subsidy to

households that are willing to comply with easily recognized "exclusion zones". Both current and potential future applicant households will face substantial incentives to locate their houses in compliance with the environmental zoning.

- 4.13 The downside risk of these proposals is negligible: if they do not operate as expected the result will simply be that urban development will continue to ignore, as it has always done in the past, broader environmental concerns. What reduces the probability of this outcome is the fact that the subsidy program together with the environmental maps are more readily managed than the conventional process of compiling environmental criteria and applying them to particular project proposals. By reducing the complexity of environmental management, the program expects to increase its efficacy.

D. Location Decisions and Program Incentives

- 4.14 The incentives provided by the subsidy, land market, and environmental policies will interact to change the way that households make location decisions. The effect of this change will be particularly strong among the low income population.
- 4.15 As matters now stand, invading public lands and settling in hazardous zones often represent the best of the constrained location alternatives facing low income households. The combination of subsidies with increased supply of planned subdivisions should shift the balance towards "planned" rather than invaded neighborhoods. Households that choose to set up their home in the Progressive Subdivisions, will be able to devote the full value of their subsidies to improve their housing conditions. Households now settled in areas of manageable risk will still benefit from Program support; however, much of their subsidy will be absorbed by the required mitigation works such as, containment walls and drainage systems. For these households, the improvement in the quality of their housing services will therefore be reduced. Indeed, the more unsuitable the terrain the smaller will be the amount of resources available for the improvements in housing. Households in environmental exclusion zones or highly risky areas, will benefit neither from the improvement subsidy nor from the land titling support.
- 4.16 Taken together these policies are designed to offer a graduated set of benefits and incentives that translate public concerns into private benefits. It is highly probable that the incentives described here will, in fact, need to be corrected. The Program design is best seen as a first step. The changes proposed will undoubtedly shift incentives in the right direction. Putting these policies into action will generate the information needed to begin the process of adjustment.

E. Political Benefits and Risks

- 4.17 There is of course a political dimension to the introduction of any major change in social policy. Housing policy is no exception. In many countries, the decision to abandon 'supply side' policies has aroused intense political debate, and the involvement of a multilateral agency can intensify the controversy. This kind of political risk is not applicable to the present program. The underlying policy changes emerged over a series of years as part of the broader reforms being implemented in Guatemala's public sector. The major legislative framework was approved by Congress in December 1996.
- 4.18 Nevertheless, the political economy of the present operation does carry both benefits and risks. The subsidy program will serve both middle income and low income beneficiaries. FOGUAVI's current arrangements have made it responsive to commercial housing developers, and to the middle income households they serve. The present operation may help reinforce the development of a new political constituency for housing policies, among the variety of intermediate agencies working in low income neighborhoods to prepare and execute housing projects. By creating a market for the services needed to improve housing conditions among the low income population, the program will generate a new set of actors to which FOGUAVI will learn to respond.
- 4.19 These arrangements also carry risks. The nature of the 'integrated' program, in conjunction with FOGUAVI'S experience with meeting the demands of middle income households, makes it easier for the latter to 'capture' program benefits and absorb a disproportionate share of resources. Providing subsidies to middle class households with the banking system as the disbursement agents, will always be easier than the effort required to reach low income households. This risk is inherent in the program design and will require careful monitoring. However, the program does incorporate measures to reduce the risk. The most obvious are the contractual conditions that link Bank disbursements to the attainment of minimum targets for actions to benefit low income households. The program also includes pro-active measures to multiply the number and capacity of agencies that can help prepare housing projects to benefit low income households.
- 4.20 During the execution of the Program more than 40,000 low income households will obtain secure title to the land they occupy; more than 26,000 will receive a subsidy to help them improve their housing conditions. However, the longer term impact of the Program will lie elsewhere. The Program will start the process of setting up sustainable financial and institutional arrangements for the housing sector. The principal challenge to housing policy stems from the 18,000 low income households that must be accommodated each year in Guatemala's cities. The Program aims to equip FOGUAVI with the capacity to serve these households by expediting some 20,000 land titles and issuing some 9,000 housing subsidies each

year. The Government of Guatemala has committed itself to spending the equivalent 1.5% of its fiscal resources on the housing sector. The policies and programs that will be introduced during this operation will help channel these resources to make the future expansion of Guatemala's cities more efficient, more equitable and more responsive to environmental values, than has been possible in the past.

I. MORTGAGE MARKET

A. Present situation

- 1.1 Widespread poverty and a high concentration of income place mortgages as a financial product (even on preferential terms) beyond the reach of a large portion of the population. The cheapest commercial housing on the market (US\$7,500) cannot be purchased with mortgage financing on favorable terms 1/ without a minimum monthly income of approximately US\$400. Only 12% of the country's urban population have an income that satisfies this requirement 2/.
- 1.2 At this level, the coverage of the mortgage market is reasonable. In 1996, with estimated resources of US\$50 million 3/, financing was granted for 2,900 homes, or 11% of new housing construction in the country that year. This is not to say that there is no room for increasing the efficiency and coverage of the mortgage market but simply to point out that the main obstacle to market growth is the absence of effective demand. Here, the SIAVI-Middle Income program comes into play. It will make borrowing more accessible to a large segment of the population which would otherwise be unlikely to obtain unsubsidized commercial mortgage financing.
- 1.3 Mortgage financing is concentrated mainly in four of the country's 30 commercial banks 4/. These institutions provide housing loans that are officially guaranteed by the Instituto de Fomento de Hipotecas Aseguradas (FHA). Mortgages do not account for a large share of bank portfolios 5/ (8%) although an increasing number of banks have identified this area as an opportunity for growth and profit. In fact, one new institution, Vivibanco, works exclusively with financing of this kind.

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- 1/ Interest rate of 18%, at 20 years, with 90% home financing and monthly payments amounting to 25% of family income.
 - 2/ Furthermore, one segment of this group is unable to demonstrate constant income flows that would allow it to have access to formal installment credit (informal sector).
 - 3/ Mortgage obligations are usually for US\$18,000 or 90% of the value of the house, with variable rates of approximately 20%, over 20 years. Monthly payments are equivalent to 25% to 36% of family income of approximately US\$1,200.
 - 4/ Private commercial banks administer 80% of assets in the formal system which, in December 1996, amounted to US\$5 billion, equivalent to 27% of GDP.
 - 5/ Mortgage certificates are not registered as loans but as zero-risk investments in FHA securities.

- 1.4 The State was unsuccessful in its bid to become a player in the mortgage market as a first-tier bank. Consequently, against a background of modernization of the financial system, the activities of the National Housing Bank were suspended and Banco de Crédito Hipotecario Nacional (BCHN) began to be restructured with a view to eventually privatizing it. Although mortgages (US\$18 million) have been reduced as a share of its overall portfolio (24%), BCHN is still the main source of FHA-unsecured mortgages. It also has the worst recovery record. The BCHN's role in the mortgage market is uncertain and will depend largely on the results of the privatization process. The use of FOGUAVI-subsidized financing administered by commercial banks has been replaced with a more transparent mechanism of direct subsidies supported under the present program.
- 1.5 However, support for the development of a commercial mortgage market through the Institute of Mortgage Insurance (FHA) has been extremely positive for this market in which 50% of all transactions (estimated portfolio of US\$25 million in 1996) receive its backing. The FHA is a public financial institution that (in addition to establishing and enforcing building codes) guarantees mortgages by means of Secured Mortgage Certificates that provide tax benefits to investors. These certificates are very attractive investments because they are transferrable, are guaranteed by the State, are tax exempt (30% of net income), and as a bank asset do not need to be backed by capital. Moreover, for financing of housing with an area of less than 60m², the yield is exempt from the value added tax charged on interest-bearing securities (10%).
- 1.6 Secured mortgage certificates are issued by the FHA in the home buyer's name (on the same terms as the mortgage loan) and are "purchased" by banks and other financial intermediaries. The need to enforce the guarantees has traditionally been low, less than 1% ^{6/}. The cost of the guarantee to the buyer is 1% of the debt outstanding per year, which is generously offset by the financial terms and conditions of the unsecured mortgages:

^{6/} In spite of these findings and considering the recent dynamic growth of the FHA, the effective equity base available to the State to support these guarantees is considered prudent for considerations of financial and fiscal health.

	<i>With FHA guarantee</i>	<i>Unsecured</i>
<i>Effective interest rate <u>7</u>/</i>	20%	24%
<i>Term</i>	<i>Up to 20 years</i>	<i>5 to 10 years</i>
<i>Loan/House value</i>	95%	80%

1.7 Ranging in amount from 50,000 to 500,000 quetzals (US\$8,300 to US\$82,300), secured mortgages are intended mainly for families with average monthly incomes of US\$450 to US\$4,500 8/. Based on its technical staff, the FHA is seeking to broaden its client base, and is therefore developing financial products that are better suited to the income profile of households with incomes of less than US\$450 provided that they meet the thresholds established for financial viability.

1.8 To encourage growth in the supply of financial services for basic housing, the government has ruled that when private guarantors issue a loan guarantee of any kind, mortgage bonds or securities granted to the SIAVI target group, these secured credits, bonds, or instruments will enjoy the same fiscal rights and privileges as FHA bonds. The corresponding regulations have not been issued.

B. Main obstacles to development of the mortgage market

1. Interest rates

1.9 Guatemala has been unable to maintain a stable macroeconomic environment that can be sustained for long enough to promote the development of an installment credit market. High and volatile interest rates, in particular, reduce demand for credit by making it unaffordable for a growing number of borrowers.

1.10 Interest rates are at levels that reflect macroeconomic uncertainty, a fragile tax base, uncompetitive market conditions, and low operating efficiency. Commercial interest rates in real and nominal terms and intermediation spreads have traditionally been high, effectively reducing demand for installment financing. In an economy with inflationary expectations of 10%, lending rates are presently around 22.5%. The gross spread between the average lending rate and the average rate paid on deposits is 11.5% and the

7/ This rate consists of the interest rate (18%), the commercial bank administration fee (1%), and the FHS administration fee.

8/ Interest rate of 20%, at 20 years, with 95% home financing, and monthly payments amounting to 30% of family income.

net spread, after discounting the cost of bank holdings, is 8.5%, a reflection of serious inefficiencies and/or incompetence.

2. Absence of adequate financial instruments

- 1.11 In Guatemala, the mortgage market has developed on the basis of simple nominal adjustments in interest rates, which are determined by the rate paid on deposits and/or the inflation rate. In this regime, the inflation rate is fully reflected in the interest rate, effectively shortening the term of the loans and reducing the borrowers' ability to pay.
- 1.12 In this environment, new financial instruments need to be found that take into consideration threshold ability to pay (relative to income) and that permit adjustments, other than by means of interest rates, to offset the impact of inflation. An example of this is the indexing of debt balances and the setting of a constant nominal rate equivalent to the expected real interest rate. To avoid the critical conditions that result from lags in real wages in periods of high inflation, this indexing arrangement may be supplemented by indexing the payments to a general wage index, thereby protecting the borrowers' ability to pay, extending the repayment terms in inflationary periods (although they are shortened in periods of sustained increases in real wages), and guaranteeing the real return for lenders. The possibility of indexing to other currencies has not yet been explored. Although this permits access to markets and resources that are more stable, it would need to go hand in hand with arrangements for exchange risk protection.

3. Financing and liquidity of the mortgage market

- 1.13 A lack of funding and liquidity in the long-term debt market has been a major impediment to the development of the mortgage market. Although a characteristic consistent with macroeconomic instability, it is also exacerbated by capital markets that are not mature.
- 1.14 Funding in the financial system is very short term (typically 30 to 90 days). Consequently, debt is highly volatile posing a serious risk to liquidity and interest rates for intermediary banks with a more long-term perspective. This explains why bank loans are typically granted for extremely short terms. Between 1985 and 1989, loans for under one year accounted for 87% of total lending. In the 1990-1995 period, at around 81%, the percentage was not substantially different.
- 1.15 The securities market has done little to help raise resources for term financing in Guatemala. The securities listed in the securities market are characterized by being extremely short term. Stock issues are limited (there have been only eight issues) and

repos – sales transactions with an agreement to repurchase by banks or brokerage firms – account for most of the volume in fixed-income securities. The terms in the repo market are 7-15 and up to 30 days. Most private debt issues are 10-year programs, with revolving short-term issues.

- 1.16 It is interesting to note that efforts (i) to seek stability and certainty in financial terms and conditions, (ii) to seek confidentiality, and (iii) to escape taxation, have resulted in the proliferation of off-shore financial institutions. The level of intermediation in these markets is not certain although some local observers estimate that lending by these institutions could be as high as 50% of all bank lending in Guatemala, which in December 1996 amounted to US\$2.553 billion. Access by the housing sector to these resources is minimal.

4. Financial technology for small loans

- 1.17 In light of the fact that the mortgage market will gradually expand to reach low-income groups with lower unit credit demands and higher administrative costs, the costs of intermediation may rise considerably. So that these costs will not act as a brake on market expansion suitable credit technologies should be disseminated and adopted to address the needs of small borrowers.

C. Proposed support

- 1.18 The main support that could be provided for the development of the mortgage market in Guatemala would mean: (i) adopting the financial modernization measures being considered in phase II of the financial sector program; (ii) taking actions to promote the capital market development that is being supported by the MIF; and (iii) supporting the results of the government's privatization and reform program.
- 1.19 The housing program will help to bring about increased demand for credit, as a result of the SIAVI-Middle Income program. In addition, a minor component has been included for studies to promote dialogue at the national level on options, challenges, and possibilities for deepening the mortgage market. Specifically, a series of activities have been devised to evaluate, with the private sector, the best options for institutional and financial development of this market.
- 1.20 The general objective of this component is: (i) to provide the authorities who establish housing policy with documented evidence of the potential impact of the mortgage market on the country's housing and capital markets, and (ii) to promote dialogue with and within the private financial sector so that the latter will spearhead the development of the mortgage market. In this way, the Guatemalan government hopes to promote the development of a private

mortgage market and to create a legal, regulatory, and institutional environment conducive to its effective development. The private financial sector has indicated its commitment to participating actively in these initiatives and *its contributions will be recognized as part of the local counterpart for this component.*

- 1.21 The component will consist of a series of studies and workshops directed to the public sector, the private sector, and joint committees from both these sectors. The specialized studies and interaction with experts and professionals connected with these markets in other countries will enable the Central Bank of Guatemala, the Office of Bank Supervision, the FHA, the Vice Ministry of Housing, and private financial agents in the country to familiarize themselves with the institutional, financial, and legal structure required for development of the mortgage market. This technical dialogue at the national level is expected: (i) to provide information on the lessons learned in other countries that could contribute to a better understanding of the opportunities for mortgage market development in Guatemala and the challenges that would be faced; (ii) to identify, evaluate, and disseminate information on the technical, regulatory, and institutional requirements for deepening the mortgage market; (iii) to identify actions that may be taken by the public sector to encourage development of this market; and (iv) to establish a working agenda within the private financial system for development of the mortgage market.

- 1.22 Under the technical-cooperation program, four studies will be conducted on the following topics:

1. *Financial instruments suited to the sustainable development of the mortgage market.* Given their operational complexity, the perception of credit instruments in Guatemala is negative. However, other countries in the region (Chile, Colombia, and Mexico) have been successful with instruments of this kind. More information on these experiences in the operational, financial, legal, and administrative areas will spur the development of these financial products, and make it possible: (i) to improve the effective ability to pay of prospective home buyers; (ii) effectively lengthen repayment terms; and (iii) reduce uncertainty with respect to loan conditions. The study and the informal discussions will have to consider such matters as constant value credit instruments (indexing to the general price index, the wage index, or a basket of currencies), including an analysis of the interest rate and exchange risks for borrowers and lenders. The potential of these instruments as a means of gaining access to international securities markets will need to be evaluated.

2. *Potential for development of a second-tier private or joint public and private bank for channeling national and international funds to the mortgage sector.* In Central America, although initiatives to develop a second-tier bank have been considered in the past, the discussion was limited to a small group of private investors. Bringing the public sector into the debate is crucial, particularly with respect to the regulatory, fiscal, and exchange factors that can determine whether or not the proposal is viable. One section of this study (business plan) will have to evaluate specifically the advantages and disadvantages of the proposal from the standpoint of the private sector and as far as the solvency of the national financial markets is concerned. The study should also identify the effective market, determine the extent to which market expansion is dependent on tax benefits, identify regulatory changes to enhance its operation, capital structure and funding mechanisms (associated risks), and evaluate the structure, volume, liquidity, and volatility of debt markets.
 3. *Identification of markets and access mechanisms that increase the liquidity of mortgage loans.* National and international securities markets offer untapped potential for liquidity for the mortgage market (nonregional capital markets, off-shore resources, pensions funds). The development of financial instruments to gain access to these markets includes such instruments as the securitization of mortgage debt, negotiable mortgage certificates, and mortgage bonds.
 4. *Identification of legal and institutional impediments to the enforceability of mortgage guarantees.* The efficiency of the guarantee system and its associated costs is critical to the development of the mortgage market. Evidence as to its efficiency is not consistent. Accordingly, a field study will be conducted to identify the source of the highest costs and inefficiencies and a specific plan of action to eliminate them will be presented.
- 1.23 In each case, the study and working agenda will be established jointly with the private financial sector and if considered necessary with the Builders Association. *The Bank will approve the terms of reference and working agenda of the workshops.* All of these studies will need to consider experiences in other countries, to identify the pertinent legal and regulatory aspects, and to invite professionals actively involved in the mortgage markets outside the region to participate in the discussions. Once the findings of each study have been presented, workshops will be organized to discuss these findings. To achieve a fair degree of technical deepening, groups from the private sector, the public sector, and joint committees will meet to discuss each study. A consultant will be hired to organize these activities.

- 1.24 A budget of US\$250,000 (under review) has been allocated for these activities, to cover preparation of an agenda, studies, discussions, development of a strategy/action plan for adoption of recommendations, evaluation of what has been accomplished with the component and financing of a local consultant to coordinate the component 9/. *The first disbursement of the financing for this component is conditional on a consultant being selected to administer it in accordance with the terms of reference agreed on with the Bank.*

MORTGAGE MARKETS STUDIES

Item	Total cost
Coordinating consultant	US\$20,000
Consultants (studies)	US\$150,000
International experts (speakers)	US\$50,000
Leasing expenses (premises)	US\$6,400
Communications	US\$16,600
Printing supplies	US\$4,000
Evaluation	US\$2,000
Contingencies	US\$1,000
TOTAL	US\$250,000

- 1.25 The mid-term report and ex post evaluation of the program will include an evaluation of the effectiveness of the component in attaining its objectives and will include copies of the studies conducted, the findings of the workshops, and the action plans if necessary.

9/ Organizing the activities including studies and workshops calls for considerable work in: (a) preparing the terms of reference in conjunction with the private sector; (b) selecting experts to conduct the studies; (c) following up on the work done by the experts; (d) organizing meetings with the public and private sectors to discuss the structure of workshops and to select participants and speakers for the workshops; (e) inviting participants and speakers in consultation with the Bank and the Guatemalan government; (f) organizing the logistics for the workshops; (g) establishing and implementing a mechanism; and (h) framing and supervising the workshop evaluation process.

**LESSONS OF EXPERIENCE: HOUSING POLICY AND BANK OPERATIONS IN GUATEMALA,
1987-1996**

A. Phase 1: 1987-1992: Instruments of Supply in the Public Sector

- 1.1 The principal agent for setting and implementing Housing Policy in Guatemala during the 1970s and 1980s was the National Housing Bank (BANVI). Following the dominant style of intervention to improve housing conditions among the poor, it's principal policy vehicle was the "sites and services" project. BANVI would purchase sites or use its own land holdings, and directly contract their subdivision and development with a full set of urban services. Beneficiaries were then provided with low interest loans to acquire the lots, and to buy the materials with which to construct their house. BANVI, in common with similar agencies throughout Latin America, was not able to manage effectively the financial aspects of these programs.
- 1.2 In January 1987 the IDB approved an operation with BANVI (804/SF-GU) as executing agent, to finance some 12,500 serviced sites; the works were begun in September 1989 and by the date of final disbursement (March 1996) some 8,300 lots had been produced. Faced with considerable financial weakness in BANVI, the Government of Guatemala decided, during the Program's execution, first to halt operations and then to dismantle the agency. As a result, the operation with the BID, originally estimated at \$56.1 million was cut back so that the actual cost was \$32.04 million; of the original loan of \$43.8 million, \$24.9 million was disbursed and \$18.89 million was canceled.
- 1.3 Three main lessons can be drawn from this period of housing policy:
 - 1) Problems of Scale and Single Source Supply
The operation's original goals, although too demanding for the executing agency's capacity, fell far short of what the target population could absorb. The production of housing solutions by a single publicly managed agency is unlikely to be an effective way of meeting the needs of low income households on a national scale.
 - 2) Failure of market know how
The average direct cost of the serviced sites alone was about \$3,300. This is very close to the commercial price currently charged to middle income households by commercial developers. The housing "product" (a fully equipped plot) and the targeted population were poorly matched. Private developers are likely to do a better job of market analysis than the officials of a government owned bank.

3) Absence of Financial Prudence

The loans offered to BANVI beneficiaries were far larger than a prudent micro credit agency would lend to first time borrowers at similar income levels. This suggests that much of BANVI's financial weakness stemmed from poor financial design as much as poor administration. Private banks are likely to handle credit better than public agencies. 1/

B. Phase 2; 1992-1996; Transition to a Market Oriented Policy

- 1.4 Although these judgements seem harsh, it is worth emphasizing that BANVI's performance was no different from that of a dozen similar agencies throughout Latin America. What was distinctive was the Government's response. Rather than continue to inject more public money into BANVI, by 1992 the Government began to look for alternative policy instruments. The authorities organized a seminar to learn of the experience of other countries in the region, looking particularly to Chile, Costa Rica and El Salvador. In 1994, a technical assistance operation financed by the IDB (ATN/SF-4260-GU and ATN/SF-4261-GU) gave further support to the search for an alternative model of housing policy.
- 1.5 It was in this context the Guatemalan Housing Fund (FOGUAVI) was conceived - a second tier alternative to BANVI's failures as a primary source of housing finance and production. FOGUAVI was expressly prohibited from directly financing or developing housing. It established links with private housing developers and with commercial banks that served as policy executors.
- 1.6 The public sector was very largely out of the business of housing construction, but it was still very much involved in housing finance. FOGUAVI aimed at reaching a population segment that did not have access to commercial housing finance and chose a subsidized interest rate as its policy instrument. FOGUAVI's resources were managed as trust funds and the banks issued and serviced the loans.
- 1.7 FOGUAVI began operations in early 1996. Initially, both the banks and developers were wary of the new approach. However by April 1997 nearly 2000 purchases had been financed, for an average loan size of about \$6,000. Most of these loans were used to purchase the kind of small house that constituted the low end of the market served by commercial developers. FOGUAVI's policy of offering subsidized interest rates of around 15% so that access to mortgages, previously limited to households with monthly incomes of \$500 or more was accessible to households with incomes of around \$300.

1/ The IDB loan proposal for (804/SF-GU) showed that 62% of BANVI's 50,000 loan accounts were in default. The IDB analysis concluded however that a BANVI plan for arrears recovery was "satisfactory and includes an analysis of the causes of the arrears".

1.8 This transition phase achieved critically important results. FOGUAVI demonstrated the viability of "market driven" policy instruments as opposed to the "administered" instruments adopted by BANVI. Politicians and officials have seen that public policy can be achieved through private agents. Banks and housing developers have had direct contact with a new and potentially profitable market segment.

1.9 Notwithstanding these achievements, the arrangements created by this transition phase were far from optimal. Three problems remained:

1) The management of risk

Participating banks performed a purely administrative role. They bore no credit risk but receive fees for originating and servicing loans. The positive economic conditions of the last two years have ensured that serious problems have not yet arisen in the loan portfolio. However, over time, and in less favorable economic circumstances, they have no effective incentive to continue to exercise diligence in assessing potential purchasers or managing overdue accounts. 2/

2) The subsidy instrument

Subsidies implicit in the interest rate are not (and cannot be) fully transparent. They are the result of the difference between the relevant market rates and the preferential rate established by FOGUAVI. Without the ability to predict market interest rates, the subsidies cannot be quantified ex ante, and their cost is not budgeted. 3/ Equally important, the subsidized interest rate inevitably provides a larger subsidy to the higher income beneficiaries who are able to qualify for a larger loan.

3) Equity and targeting

FOGUAVI's program benefitted middle income households but did little for the low income population. Not that the program excludes low income households, but the arrangements do not lend themselves to providing them with the help needed to improve their housing conditions within the informal market. FOGUAVI's annual budget of around \$12 million was largely inaccessible to the 60% of the urban population with incomes of \$200 a month or less.

2/ After some 15 months of operation (Feb 1996 - April 1997) the three largest participating banks have kept overdue loans to about 2.3% of the FOGUAVI portfolio; however, the one bank that has been most aggressive in reaching the low end of FOGUAVI's target population already has an overdue rate of 13.5%.

3/ At the beginning of 1997, with market rates at approximately 26% and FOGUAVI's at 15%, the subsidy on the average loan with a 20 year term would be estimated at about US\$2,400. This of course leaves aside the contingent subsidy that could arise from loan delinquency.

BENCHMARK INDICATORS, DISBURSEMENT AND PROCUREMENT

I. MONITORING AND BENCHMARKS

- 1.1 The arrangements for monitoring and reporting are intended to provide a clear account of what is expected from each component of the program, independent information on actual performance, and the means for the executors of the Program, in consultation with the Bank, to make the necessary adjustments. The activities and results (benchmarks) expected from each component are set out in the execution matrices below. The information to monitor these benchmarks will come from two principal sources: the management information system used by FOGUAVI to supervise the Program, and annual performance studies carried out by independent consultants on samples of projects. To carry out the performance studies, the consultants will visit housing solutions produced under each of the sub components in the Subsidy and Land reform programs. They will also report on compliance with environmental criteria in the projects visited. The information from both sources will be combined in annual reports made by FOGUAVI to the Bank. The reports will be explicitly organized around the Program's benchmark indicators and where significant shortfall is observed, the report will include FOGUAVI's proposals for correcting the situation. Program executors and the Bank will hold annual meetings within a month of submission to discuss the reports and to agree on changes to the operating regulations or other Program guidelines. The *Normas Generales* provide for 60 days following the end of each semester report.
- 1.2 Regarding the subsidy component, the indicators will provide information both on the levels of output and on the quality of the results. For many of the key indicators, the data collected by the MIS will be checked in the sample of performance studies, helping to pinpoint possible areas of mismanagement or poor record keeping. Regarding the land reform component, the indicators cover both the sequence of institutional, legal and regulatory changes required, and the output of regularized titles and progressive sub-divisions. The environmental management component will track both the production of exclusion zone maps with indicators of their success in directing urban expansion.
- 1.3 Because of the concern regarding inflation, under the Direct Subsidy-Commercial Window, maximum targets are established for the total number of subsidies which can be issued during four consecutive periods of 12 months each, beginning with the activation of the Loan Contract. These targets will not be applied in subsequent periods.

PERIOD 1	PERIOD 2	PERIOD 3	PERIOD 4
5,000	6,000	7,000	8,000

1.4 These targets may be adjusted under the following conditions and in the following manner: When the number of issued 1/ subsidies is 60% or greater of the corresponding period, FOGUAVI may request that the target number of subsidies be increased. This request must be substantiated with the following information:

- 1) The average increment of the official Consumer Price Index of the two semesters immediately preceding the request ("Price Inflation").
- 2) The percentage of annual inflation of the construction costs per square meter financed with resources from the Commercial Window ("FOGUAVI Housing Inflation") calculated based on the following data: (a) the average price of the completed house financed with the resources from the Commercial Window for each of the two semesters immediately preceding the request, and (b) the average number of square meters of said housing for each of the two semesters immediately preceding the request.

1.5 If (i) the Price Inflation is equal to or greater than the FOGUAVI Housing Inflation, and (ii) the Bank does not expressly object to the request presented by FOGUAVI within 15 working days ("date of approval"), then the target corresponding to the next 12-month period shall apply and the next 12 month period shall begin, starting on the date of approval. In any other case, a written agreement from the Bank will be necessary to increase the target applicable to each period.

II. DISBURSEMENTS

2.1 To help monitor compliance with conditionality regarding resource commitment the annual report will also include an estimate of the total FOGUAVI expenditure expected that year with a breakdown of the expected financing sources; starting with the second year after the loan is declared eligible, the Government will also provide the Bank with the total resources expended by FOGUAVI during the preceding year, and the sources of that expenditure. If the local resources committed to FOGUAVI fall below the limit established in the corresponding contractual condition, Bank disbursements will be discontinued until the Borrower has presented to the Bank's satisfaction a formal commitment to increase the funding allocation for the current year by the amount of the shortfall.

The tentative disbursement schedule for the Program is as follows:

1/ "Issued" signifies that the purchase-sale agreement for the individual house has been completed and the title of the house is in the name of the beneficiary.

Millions US\$	Yr 1	Yr 2	Yr 3	Yr 4	Total
Local Resources	12.4	12.3	12.1	12.0	48.8
IDB Loan	6.7	13.5	17.9	21.4	
Total	19.1	25.8	30.1	33.4	108.3
Percent	18%	24%	28%	31%	100%

III. PROCUREMENT

- 3.1 The Program does not envisage contracting of works by the executing agency. The procurement of goods will be limited to the purchase of basic computer equipment that will not exceed US\$100,000 and will be conducted under national public bidding, in accordance with local legislation. The principal procurement will be the contracting of consulting and management services. International competitive bidding is expected for a total of approximately US\$3.14 million in management services.

- 3.2 The management of the Direct Subsidy - Social Window Unit and of the Land Market Reform Unit will require technical and managerial skills that may be difficult to obtain locally. Following the Bank's procurement procedures for consulting services, two two-year management services contracts will be tendered under international public bidding (IPB) to support the execution of each of these components. Each management contract has been estimated to cost approximately US\$600,000. If upon termination of the Subsidy Unit and Land Market Reform Unit contracts the executing agency considers that the contracts have been satisfactorily performed, the executing agency may extend the original contracts for an additional two years. Simultaneously the executing agency will also contract under international public bidding (IPB) the services of a firm to handle the management information system (MIS Unit). A two-year management services contract will be tendered for approximately US\$200,000. If upon termination of the MIS contract the executing agency considers that the contract has been satisfactorily performed, the executing agency may extend the contract for an additional two years.

- 3.3 The executing agency will also contract consulting services for project preparation, project evaluation, sector studies and supervision activities. These services, which have been estimated to have costs ranging from US\$15,000 to US\$50,000, will be procured under national public bidding (NPB) in accordance with local legislation. The estimated procurement schedule is detailed in the following table.

PROCUREMENT SCHEDULE

PRINCIPAL PROGRAM PROCUREMENT	Financing (%)		Method	Prequalification (Yes-No)	Estimated publication date of the SPN
	BID	Local			Semester/Year
A. PROCUREMENT OF GOODS:					
1. Computer Equipment US\$100,000	100%		NPB	NO	I/98
B. CONSULTING SERVICES:					
1. Consulting Firms:					
Management Services Contracts: Subsidy Social Window Total: \$1.3 million Each contract: \$650,000 (ave.) No. Contracts: 2	50%	50%	IPB	YES	I/98 I/2001
Management Services Contracts: MIS Unit Total: \$400,000 Each Contract: \$200,000 (ave.) No. Contracts: 2	50%	50%	IPB	YES	I/98 I/2001
Management Services Contracts: Land Reform Unit Total: \$1.2 million Each contract: \$600,000 (ave.) No. Contracts: 2	50%	50%	IPB	YES	I/98 I/2001
Subsidy Social Window Projects Preparation ("Incentive Funds") Total: \$2.9 million Each contract: \$20,000 (ave.) No. Contracts: 145	50%	50%	NPB	NO	
10 contracts					I/98
15 contracts					II/98
20 contracts					I/99
20 contracts					II/99
20 contracts					I/2000
20 contracts					II/2000
20 contracts					I/2001
20 contracts					II/2001
Social Marketing Total: \$100,000 Each contract: \$50,000 (ave.) No. Contracts: 2	50%	50%	NPB	NO	I/98 I/99

PRINCIPAL PROGRAM PROCUREMENT	Financing (%)		Method	Prequalification (Yes-No)	Estimated publication date of the SPN
	BID	Local			Semester/Year
Annual Monitoring Studies	50%	50%	NPB	NO	I/98 I/99
Design and Setup					
Total: \$50,000					
Each contract: \$25,000					
No. Contracts: 2					I/99
Annual Report					I/00
Total: \$200,000					I/01
Each contract: \$50,000 (ave.)					I/02
No. contracts: 4					
Land Reform Component					
Subcontracting Title Preparation:	50%	50%	NPB	NO	
Subcomponent: Legalization					
Total: \$4.35 million					
Each contract: \$15,000 (ave.)					
No. Contracts: 290					
15 contracts					I/98
10 contracts					II/98
30 contracts					I/99
35 contracts					II/99
45 contracts					I/2000
45 contracts					II/2000
55 contracts					I/2001
55 contracts					II/2001
Preparation Exclusion Maps	50%	50%	NPB	NO	
Total: \$225,000					
Each contract: \$5,000 (ave.)					
No. Contracts: 45					
10 contracts					I/98
10 contracts					II/98
15 contracts					I/99
10 contracts					II/99
TA Land Use (GIS)	50%	50%	IPB	YES	I/98
Total: \$120,000					
TA Emergency	50%	50%	IPB	YES	I/99
Preparedness/Training					
Total: \$120,000					

2002 EXECUTION MATRIX

Component: SIAVI (1) Institutional Aspects

Overall Goals: (1) Increase Level of public support to low income HH
 (2) Increase efficiency of public investment in housing sector

Specific Purposes: (1) Introduce transparent, efficient demand subsidies
 (2) Expand role of private sector agencies: developers, banks, NGOs
 (3) Leverage additional private investment in housing

		By December 1997	Yr. 1	Yr. 2	Yr. 3	Yr. 4	Information Sources & Observations
Monitoring		Contract Unit Chief Contract Low income Chief	Hire up 4 full time local staff with low income expertise Hire two international staff with low income expertise	Hire 1 additional full time local staff with low income expertise Continue contract for 1 international expert	Hire 1 additional full time local staff with local income expertise Continue contract for 1 international expert		Annual report on project performance will cover activities and indicators listed in matrices; sources will be: MIS and performance studies
Procedures	Operating regulations: Middle Income Projects Staff manual: Middle Income Projects Operating regulations: Low Income Projects Staff manual: Low Income Projects	Submit revised version for IDB approval Prepare with PPF resources Prepare draft with PPF resources	Submit draft to IDB Prepare draft; Submit draft to IDB	Propose operating changes in annual report	Propose operating changes in annual report		
		Hire Consultants with PPF resources to design MIS specifications Advertise RFP for implementing and managing MIS	Select firm for MIS contract and implement design				
Monitoring Program Performance		Hire consultants to design performance studies	(1st. Quarter) Submit report on resource commitments for current year. (4th. Quarter) Carry out performance studies in 5 low income and 5 middle income projects	(1st. Quarter) Submit annual report on previous year's progress; resource commitments for current year. (4th Quarter) Carry out performance studies in 5 low income and 5 middle income projects	(1st. Quarter) Submit annual report on previous year's progress; resource commitments for current year. (4th Quarter) Carry out performance studies in 8 low income and 8 middle income projects	(1st. Quarter) Submit annual report on previous year's progress; resource commitments for current year. (4th Quarter) Carry out performance studies in 12 low income and 12 middle income projects.	Operating cost-staff costs + admin costs
Efficiency Ratios	Operating cost/Total # Actions/Total Expenditure		Include ratios in annual report: \$1,400/# 7%	Include ratios in annual report: \$1,050/# 4%	Include ratios in annual report: \$936/# 3%	Include ratios in annual report: \$908/# 3%	Total # actions-subsidies + registered individuals/land titles

GU-0022 EXECUTION MATRIX
Component: SIAVI (2) Outputs

Guxmatrix

General Goals: (1) Increase level of public support to low income HH
(2) Increase efficiency of public investment in housing sector

Specific Purposes: (1) Introduce transparent, efficient demand subsidies
(2) Expand role of private sector agencies; developers, banks, PDOs
(3) Leverage additional private investment in housing

		by Dec 1997	Yr. 1	Yr. 2	Yr. 3	Yr. 4	Information Sources and Observations
Level of Output	# Soins		L: 3,750 M: 3,750	L: 6,000 M: 4,500	L: 7,500 M: 5,000	L: 9,000 M: 5,000	Program performance studies will involve work on a sample of projects collect data on all indicators. Will include recommendations for correcting identified problems and taking advantage of observed good practice.
Targeting	Average HH Y Median HH Y		L: \$150 M: \$375	L: \$100 M: \$300	L: \$80 M: \$275	L: \$80 M: \$275	
Solutions Total Costs	Average Median		L: 3,000 M: 7,000	L: \$2,500 M: \$8,000	L: \$2,000 M: \$8,000	L: \$2,000 M: \$8,000	
Construction	New Construction Upgrade Exist. M2 Construction FHA Approved		L: 100% upgrade M: 100% new	L: 85% upgrade M: 95% new	L: 70% upgrade M: 95% new	L: 70% upgrade M: 95% new	All data will be disaggregated by HH income group; L refers to HH Y < \$200/month (equiv 2 minimum salaries); M refers to HH \$200 < Y < \$200/month (equiv 2-4 minimum salaries)
Location	Metro GU City Other Dept Caps Others	60% MGUC	50% MGUC	50% MGUC	50% MGUC	50% MGUC	
Financing Subsidy	Average Median		L: \$1,500 M: \$2,000	L: \$1,200 M: \$2,000	L: \$1,000 M: \$2,000	L: \$1,000 M: \$2,000	
Contribution	Average Median		L: 60% Norm in cash M: 100% Norm in cash	L: 70% Norm in cash M: 100% Norm in cash	L: 80% Norm in cash M: 100% Norm in cash	L: 80% Norm in cash M: 100% Norm in cash	Data in US\$ and as % of total solution cost
Loan	Average Median		L: No loans M: 100% w. loans; \$4,000	L: No loans M: 100% w. loans; \$4,000	L: 10% with loans M: 100% w. loans; \$4,000	L: 10% with loans M: 100% w. loans; \$4,000	

Abbreviations: HH Household; PDO: Private development organization; Y Income (US\$ per month); FHA: Insurance Agency; L: Low Income; M: middle Income

GU-0022 EXECUTION MATRIX Component: SIAVI (3) Promoting Role of Private enterprises, NGOs, Community Organizations, Municipalities.							
General Goals: (1) Increase level of public support to low income HH (2) Increase efficiency of public investment in housing sector.				Specific Purposes: (1) Introduce transparent, efficient demand subsidies (2) Expand role of private sector agencies; developers, banks, PDOs. (3) Leverage additional private investment in housing			
		(By Dec 1997)	Yr. 1	Yr. 2	Yr. 3	Yr. 4	Information Sources and Observations
Role of NGOs, Community Orgs, Municipalities	# Contracted to prepare/supervise/execute low Y projects	5 COs in pilot projects	10 contracted	15 contracted	15 contracted	15 contracted	
	# authorized to handle subsidies		5 authorized subsidies/ 10 authorized for t.a	10 authorized subsidies/15 authorized for t.a.	10 authorized subsidies/15 authorized for t.a.	10 authorized subsidies/15 authorized for t.a.	
	# authorized to provide technical assistance						
	# requesting projects		25	40	50	60	
	# Training Workshops	1 workshop financed by PPF	2 workshops financed by program	2 workshops financed by program	2 workshops financed by program		
Private Enterprises	Commercial banks authorized to handle subsidies	5 authorized under new FOGUAVI procedures	10 authorized under new FOGUAVI procedures	15 authorized under new FOGUAVI procedures	Maintain	Maintain	
	Loans issued by commercial banks	See SIAVI Matrix I					
	Housing Developers (Projects for > 4 new houses)	5 developers with projects pre-approved by FOGUAVI	15 developers with projects approved by FOGUAVI	20 developers with projects approved by FOGUAVI	25 developers with projects approved by FOGUAVI	Maintain	
	Building Contractors (upgrading projects, and < 4 new houses)	5 contractors hired to execute pilot projects	15 contracted to prepare projects	25 contracted to prepare projects	35 contracted to prepare projects	45 contracted to prepare projects	

0022 EXECUTION MATRIX
Component: Land Market Reform

General Goals: (1) Create a more efficient and more equitable land market (2) Increase incentives to invest in housing for low income households				Specific Purposes: (1) Legalize tenure in existing informal neighborhoods (2) Promote market in low cost land			
		By December 1997	Yr. 1	Yr. 2	Yr. 3	Yr. 4	Information Sources and Observations
Regularization	Tracts transferred out of public domain/Certification of Habitability		25 Tracts Transferred % in GU City	65% Tracts Transferred % in GU City	90 Tracts Transferred % in GU City	110 Tracts Transferred % in GU City	
	Parcel Maps		25 Parcel Maps Prepared	65 Parcel Maps Prepared	90 Parcel Maps Prepared	110 Parcel Maps Prepared	
	Registered Title		3,000 titles registered	9,000 titles registered	13,000 titles registered	16,000 titles registered	
Progressive Sub Divisions	Model Code for Progressive Sub Division	Prepared with PPF resources; submitted to IDB	Letters of no objection to code from 20 localities	Letters of no objection to code from 20 additional localities			
	Package of Reforms to national legislation		Coordinated package prepared by consultants	Codes authorized for use in 20 localities	Codes authorized for use in 20 additional localities		
	Accelerated Title/sub division for owners of sub division		# Tracts submitted for sub division: 10	# Tracts submitted for sub division: 20	# Tracts submitted for sub division: 30	# Tracts submitted for sub division: 30	
	Plots titled through FOGUAVI		Plots titled: 1,500	Plots titled: 3,000	Plots titled: 4,500	Plots titled: 4,500	

2002 EXECUTION MATRIX

Component: Environmental Management

General Goals: (1) Reduce the negative impact of urban expansion on the environment
(2) Reduce the natural hazards facing irregular neighborhoods in Guatemala City.

Specific Purposes: (1) Introduce environmental exclusion zones to major cities together with incentives to comply with the law
(2) Finance works to mitigate risk of landslides in Guatemala City

		By December 1997	Yr. 1	Yr. 2	Yr. 3	Yr. 4	Information Sources and Observations
Planning			Hire unit chief; draft procedures and submit to IDB				
Exclusion Zones Nationwide							
Production Environmental Exclusion Maps		Selection of priority cities	Contract mapping in 15 cities with pop. > 50,000	Contract mapping in 15 cities with pop. > 50,000			
Monitoring Compliance			Submit maps to IDB	Submit maps to IDB			
			Print and distribute 50 copies of each map in SMX (see Xmatrix1)	Print and distribute 50 copies of each map in SMC (see Xmatrix 1)			
			Performance studies: inspect sample of housing within exclusion zones; date of installation? subsidy received? Awareness of exclusion?	Performance studies: inspect sample of housing within exclusion zones; date of installation? subsidy received? Awareness of exclusion?	Performance studies: inspect samples of housing within exclusion zones; date of installation? subsidy received? Awareness of exclusion?	Performance studies: inspect sample of housing within exclusion zones; date of installation? subsidy received? Awareness of exclusion?	
Risk Reduction in Guatemala City							
Trading Projects with required mitigations works	Types of Mitigation works: Containment walls. Constructed stairways/walkways. Water/Sewage drains. Vegetation. Other	Complete designation of "high risk zones" and mitigable risk zones.	# Projects including required mitigation works; type of works	# of Projects including required mitigation works; type of works	# of Projects including required mitigation works; type of works	# of Projects including required mitigation works; type of works	
		Design mitigation works in 5 pilot projects	Cost of works per HH; Cost as % of subsidy per HH	Cost of works per HH; Cost as % of subsidy per HH	Cost of works per HH; Cost as % of subsidy per HH.	Cost of works per HH; Cost as % of subsidy per HH	
Production of "Good Practice" material			Contract production of material on Good practice in Risk Mitigation	Contract production of material on Risks and alternatives for households in High risk areas	Distribute material on Risks and Alternatives for households in High Risk Areas to 70 neighborhoods	Distribute material on Risks and Alternatives for households in High Risk Areas to 70 neighborhoods	

0022 EXECUTION MATRIX

Component: Environmental Management

General Goals: (1) Reduce the negative impact of urban expansion on the environment (2) Reduce the natural hazards facing irregular neighborhoods in Guatemala City.				Specific Purposes: (1) Introduce environmental exclusion zones to major cities together with incentives to comply with the law (2) Finance works to mitigate risk of landslides in Guatemala City			
		By December 1997	Yr. 1	Yr. 2	Yr. 3	Yr. 4	Information Sources and Observations
Training for Municipality			Hire consultants to train municipal staff in use of GIS	Hire consultants to train municipal staff in disaster preparedness			

PROPOSED RESOLUTION

GUATEMALA. LOAN ___/OC-GU TO THE REPUBLICA DE GUATEMALA
(Housing Program)

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the República of Guatemala, as Borrower, for the purpose of granting it a financing to cooperate in the execution of a Housing Program. Such financing will be for the amount of up to US\$60,000,000, which are part of the resources of the Single Currency Facility of the Ordinary Capital of the Bank, and will be subject to the "Special Contractual Conditions" and the "Terms and Financial Conditions" of the Executive Summary of the Loan Proposal.