HOUSING POLICIES
Recent developments in the Peruvian economy*

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Resumen
Explica la evolución reciente de las políticas habitacionales en el Perú y, sobre esta base, analiza el desarrollo del sector inmobiliario residencial durante los últimos cinco años, considerando los factores financieros e institucionales que lo han propiciado. La primera sección describe el déficit habitacional del país y hace un recuento de las anteriores políticas de vivienda y del contexto en que surge el Fondo MiVivienda. La segunda sección describe la cadena de producción de viviendas y el papel del mencionado fondo. Finalmente, la tercera sección está dedicada al análisis de las políticas de vivienda y, particularmente, a los programas de financiamiento que ha implementado el actual gobierno para convertir a la población más pobre en propietaria de casas-habitación. Finalmente, el documento cierra con recomendaciones sobre lo que debe hacerse para mantener los logros alcanzados.

This document describes, in general, the basic aspects as part of the housing production process to where Government has focused its efforts to create a positive atmosphere for private sector involvement as well as the government's own role and the support it provides.

* Una versión preliminar de este trabajo fue presentada a la conferencia anual de BALAS (The Business Association of Latin American Studies), realizada en Babson College, Boston, en mayo de 2004.

It is very important to stress that, in the medium term, it is the government's responsibility to participate as a promoting entity, regulator, guarantor and a subsidy administrator wherever the productive chain so requires, but not to engage actively by providing funds, preparing projects, and building or selling houses, as the private sector has demonstrated it can perform those roles with little or no corruption, while reducing costs and operating efficiently.

1. A national issue

1.1. The housing deficit

The housing deficit concept describes the segment of the population who lack access to property or to homes with the basic technical characteristics that render them appropriate for living.

We can distinguish a quantitative and a qualitative deficit. The first one refers to the number of houses required so that all the population may have access to a house. The qualitative deficit refers to houses that do not meet certain minimum standards, and may be located in shantytowns, or are damaged improvised houses, etc.

The Housing Promotion Mortgage Fund –MiVivienda Fund (MVF)– is performing several studies to determine Peru's housing deficit, as well as demand for new homes, including a study called «New home market in six cities of Peru»[1] and others covering Peru's 16 main cities.

The objective of these studies was to determine and locate the demand for housing. The housing deficit measured by MiVivienda Fund reaches 2 699 971 houses, as shown in the following chart.

As shown, Lima makes up 18% of the demand, while demand in all other cities is below 10% of the total deficit.

It is important to highlight that other non-governmental entities estimate the housing deficit at around 1,7 million houses (Peruvian Construction Chamber, Capeco).

Chart 1
Housing deficit in the B, C and D income groups of urban Peru

	Deficit	
Lima	477 647	18%
Piura	217 481	8%
Cajamarca	177 961	7%
Cusco	170 755	6%
Puno	170 632	6%
Áncash	135 379	5%
Junín	135 228	5%
La Libertad	121 041	4%
Huánuco	119 498	4%
Loreto	108 932	4%
San Martín	97 657	4%
Ayacucho	89 092	3%
Lambayeque	83 216	3%
Huancavelica	82 888	3%
Arequipa	74 931	3%
Callao	74 325	3%
Apurímac	70 432	3%
Amazonas	61 558	2%
Ica	55 472	2%
Ucayali	54 458	2%
Pasco	44 303	2%
Tumbes	29 821	1%
Tacna	18 934	1%
Moquegua	14 558	1%
Madre de Dios	13 770	1%
Total	**2 699 971**	**100%**

Source: MiVivienda Fund, 2003.

1.2. Housing policies: previous Peruvian experience

Housing policies are specific development initiatives to reduce the housing deficit of a country. In what follows, we briefly analyze their present status and evolution in Peru, together with the national housing deficit.

1. Marita Chang, and Cecilia Esteves. *El mercado de viviendas nuevas en seis ciudades del Perú*. Lima: Unión Interamericana para la Vivienda (Uniapriavi), 2003. Cuaderno 199-200.

In general, home building in Latin America does not meet the people's demands, either because the formal mechanisms of house construction only reach a small part of the population, ignoring its poorest segments, or because informal mechanisms of house construction fail to meet minimum safety and health technical standards.

These problems started to aggravate in the early 1950s, when migration flows to the cities started growing at an exponential rate bringing with them a dramatic increase in the housing deficit.

In Peru, housing policies were traditionally managed by Government, who created banks to finance housing projects and built houses directly. Government used to play an entrepreneurial role, displacing the private sector and taking in its hands the whole home construction chain.

Before the 1990s, the Government had undertaken considered several plans to reduce the housing deficit. These initiatives can be categorized in two groups. First, that financed the purchasing of new houses and others for house construction. As part of its measures to finance house building, Government successively created a Mortgage Central Bank, a private mutual system to finance home building funded through a second-tier bank (Banco de la Vivienda or Housing Bank), and finally, it implemented the National Housing Fund (Fonavi) to provide funding for the Housing Bank. For its own construction efforts, the Peruvian Government created the National Construction and Building Corporation (Enace) to build homes and then sell them at subsidized prices.

All these Government policies to tackle the housing deficit issue were run directly by Government, with minimum private sector involvement. In a context of growing government bureaucracy, lack of incentives for change, an unstable and corrupt political environment, the possibilities of success of the above-mentioned organizations were seriously impaired.

Besides, these measures took place in an adverse macroeconomic context because recession at the end of the eighties (when GDP fell by 10%) and hyperinflation (7 649%), hurt house financing systems eventually leading to their final collapse. Additionally, the purchasing power of Peruvian households' wage earners decreased about 60% while prices of building materials increased incessantly, affecting not only supply by Enace and private building companies, but also demand as revenues fell simultaneously and home prices rose incessantly.

Likewise, the economic crisis affected the quality of the mortgage portfolio managed by the Mortgage Bank and the mutual system, as households' falling incomes led to increasing loan defaults. As a consequence, the risk of this type of credits worsened, therefore reducing supply, since neither the Mortgage Bank nor the Mutual Banks showed any interest in granting house loans.

In the Mutual Banking system, the poor performance of the old mortgage portfolio led to the need to create higher provisions, leading to considerable losses in the Mutual system. Simultaneously, personnel and operational expenses increased.

Finally, financing sources of these systems dried up for two reasons: i) the Government decreased funding for these institutions (including money transfers from Fonavi), ii) the monies received from the customers, through savings deposits, etc. also fell precipitously.

It is worth highlighting that funding from Fonavi was used not only for house financing, but also for building public use infrastructure (water and sewerage networks, highways, etc.).

1.3. MiVivienda Fund

At present, housing policies focus on facilitating ownership by middle and low income families –through so-called social interest housing– of homes built to appropriate technical specifications and provided with access to basic services, so that they meet the required quality standards.

In this scheme, the Government plays a subsidiary role. In its relation with the private sector, it acts as promoter and regulator of the housing market, and as supplier of basic social infrastructure. Contrary to previous experiences, the Government plays does not an entrepreneurial role, but only a subsidiary one.

In this context, the MVF was created with several objectives, including:

– Channeling its resources through the financial system to facilitate home purchasing in projects promoted and executed by the private sector.

– Organizing the MFV target markets, by matching demand for housing, house supply, and the intermediary financial institutions (IFIs).

– Planning, organizing, managing, executing, coordinating, evaluating and supervising activities to raise and use of MVF's economic and financial resources to fulfill its goals.

MVF currently has two programs: the MiVivienda Program (MVP) and the Techo Propio Program (TPP). Even though it is true that both programs share the same objective –i.e. to meet demand for housing from households that normally would not get a mortgage loan, thus reducing the current housing deficit– they do not share the same operational profile, as each targets households in different income groups.

2. House construction chain

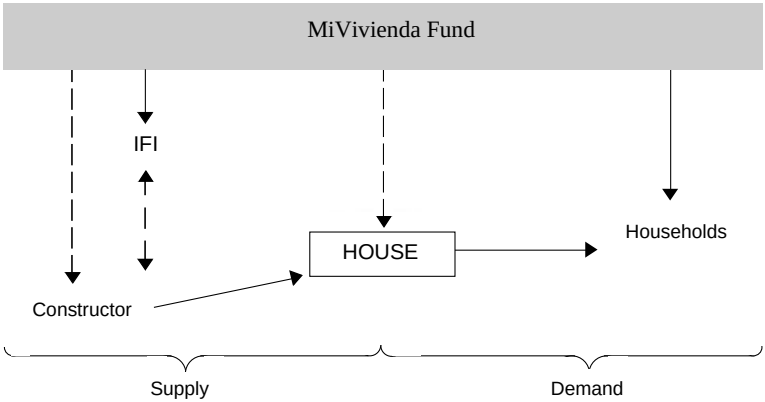
There are three main players in the home building market: building companies, the IFIs and households. An additional player in the Peruvian market is the Government acting through MVF.

MVF's role is to provide the linkages in the Peruvian home building market, as shown in the following graph.

2.1. Supply

There are two groups on the market's supply side: builders and IFIs. With the IFIs, the MVF has a direct relationship because MVF finances MiVivienda credits, when transferring the resources delivered by the IFIs. For transfer the IFI pays MVF a rate for the funds received.

Additionally, the construction sector receives indirect support for project design, and through marketing, advertising, and others.



Peru's home building market
Graph 1

The construction sector

The Peruvian construction industry is split among a number of small building companies, medium size housing developers and large scale traditional constructors. Given the crisis of the last decade, they face daunting financial constraints preventing them from adequately managing their housing construction flows.

Medium size constructors –used to building small scale projects for the wealthier segments of the population and lacking sufficient creditworthiness– have failed to gain access to fresh project financing to become players in the expanding mass construction market of recent years.

To address the builders' financial constraints, the market has seen a growing number of projects sold off architectural drawings[2] aimed at building client trust in the final product. Additionally, since the constructor gains access to funding from pre-sales and loan takers receive extended grace periods, builders only need to seek financing to cover only a small portion of their projects' financing. At present, off plan sales make up 56% of transactions.

Intermediary financial institutions, IFIs

A fast moving mortgage market in the 1990s did not effectively expand access to housing for the lowest income groups because of their reduced ability to receive loans. Traditionally, shallow bank penetration and a poor credit culture in these income groups strongly prevented them from considering formal housing as an option they could afford.

Falling international interest rates, a faster US economy, lower Peruvian sov-

2. Off plan house sales allow to raise funds for project financing.

ereign risk, and appropriate hedging for MVF-managed products, among other factors, have helped to improve the conditions under which the poorest socioeconomic segments can access home credits.

Also, Peru's Bank and Insurance Superintendent (SBS) has moved decisively to increase transparency in client information, leading to more uniform interest rates and fostering greater competition among financial institutions currently operating in the finance market.

In this context, the MVF and the IFIs are developing two products to meet demand in poor areas: MiVivienda credit and the credit for beneficiaries of the Family Housing Voucher Project. These two will be explained in more detail in the following section.

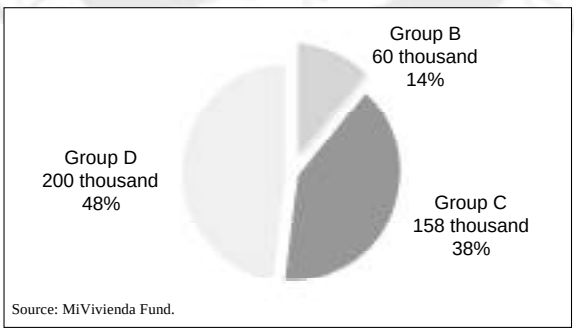
2.2. Demand

MiVivienda Fund studied demand for new houses in Lima. In its first phase, the survey researched a total 1 200 households from the B, C and D income groups evenly distributed among the three income groups.

The main objective in calculating Lima's demand for new houses is to determine the price the B, C, and D income groups are willing to pay for a house. The study assumes that the families who are not home owners make up the potential demand for property.

Thus, potential demand for new houses for Lima's combined B, C and D income groups was estimated at 418 000 houses distributed as follows by target group:

Of the potential demand for new housing, 14,4% comes from the B group (60 000), 37,8% from the C group (158 000) and 47,8% from the D group (200 000). As already mentioned, only non-owners are included as potential buyers, even when the market includes demand for second homes, particularly in for the B group that buys homes for residential as well as speculative investment reasons.

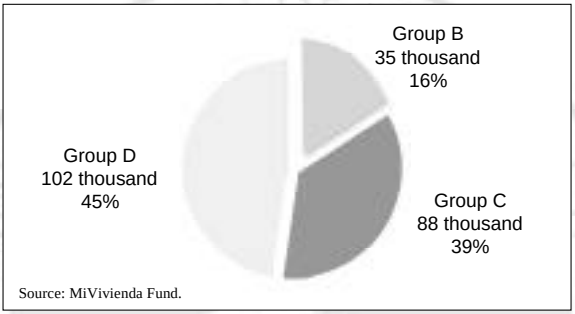


Lima: Potential demand for new houses
Graph 2

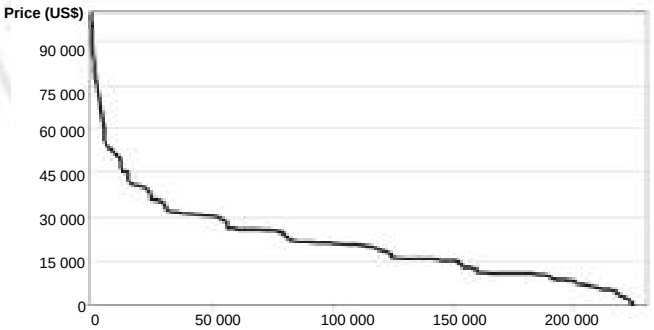
However, it is even more important to examine effective demand, or the population under study who are actually intending to buy a house and planning to do so earlier than in two years[3]. Only once these two factors (disposition to buy and purchase opportunity) are taken into consideration, will it be possible to determine demand for new housing in Lima.

The studies have estimated total effective demand in Lima reaches 225 000 houses.

Based on actual demand figures we can derive the number of houses the people want to purchase in individual price ranges, and thus estimate total market demand (as represented by a demand curve).



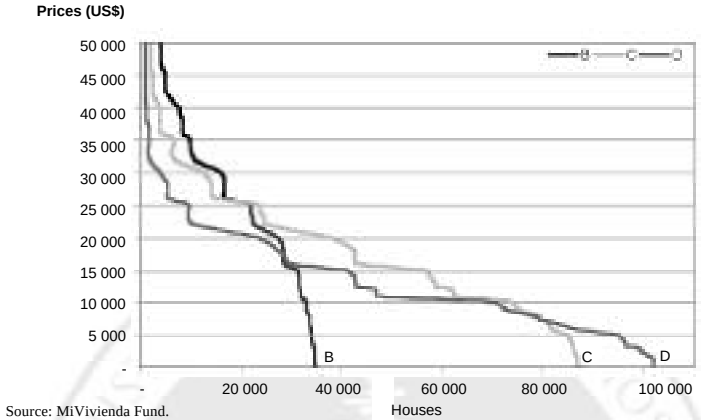
Lima: Effective demand for new houses by income group
Graph 3



Source: MiVivienda Fund.

Lima: Cumulative housing demand from the B, C and D income groups (225 000 houses)
Graph 4

3. This paper assumes 24 months as the longest purchase period.



Source: MiVivienda Fund.

Lima: Demand for new houses from groups B, C and D (225 000 houses)
Graph 5

Housing demand in the non-owning segment can also be examined by income group. Graph 5 reveals the proportional size of the population that demands a new house as much bigger in group D; however, the prices they are willing to pay are lower than in the other socio-economic groups. On the other hand, we can see that demand curves for the poorest socio-economic groups reacts more briskly at lower prices, while at those prices demand from group B is almost stagnant.

3. Solution suggestions

3.1. Current housing policies

3.1.1. Land ownership

Many land plots are government-owned and are registered as such by the Superintendent for State Property (Superintendencia de Bienes Nacionales, SBN).

The government competitively selects construction companies/developers interested in building «social interest» housings projects on land grants where they are asked to build the largest possible number of houses while meeting both technical and financial standards, including number of houses, cost, quality, and others.

More rarely, local and regional governments identify unused (abandoned) private land that is then handed over to developers for home building.

3.1.2. Support to builders

Project design

Supply for the B income group concentrates on homes above US$ 40000. For the C group, supply concentrates in the over US$ 25 000 and underUS$ 40 000 USD bracket. Weak demand and cuts in infrastructure building have hurt formal deve-

lopers financially, leading to increased «informal» (self-start) house construction, as mentioned earlier.

An initial approach to reverse this trend was to encourage developers to build cheaper houses. They were proposed to increase their earnings through mass building at slimmer margins, in other words, giving up their high unit margins in compensation for a strong increase in demand, supported by a steady communication campaign. An important step in this direction was a study to determine cumulative demand in six cities (Lima, Arequipa, Chiclayo, Chimbote, Ica and Tacna).

On the other hand, they were encouraged to introduce new construction techniques to reduce costs per m^2, though perhaps even more important were efforts to foster creative designs to build houses on smaller footage without detriment to either functionality or quality.

These goals were achieved while preserving MVF as a promotional agency and encouraging greater competition in the house building market. A good example of these results can be seen in tenders' results. Having to bid for construction property spurred competition and drastically reduced costs per m^2, compared to prior commercial costs in similar areas.

Constructor financing

Meanwhile, off-plan sales promotions were designed to address the constructors' financial straits, as described above. Builders had to finance only a small portion of the project, allowing them to make a profit. Off-plan sales now account for 56% of all houses sold.

Project risk

Falling public investment in infrastructure projects was crucial for builders as it allowed them to preserve their profit margins, in particular at the beginning of the 1990s. Reduced investment in infrastructure building hurt some builders seriously and eventually led to their collapse. Against this background, MVF's initiatives have not only brought the crisis under control, but have also made it possible for these companies to become profitable again and even thicken their margins significantly.

Larger profits have not been their only benefit. Other benefits include a sharp learning curve as they learned to build cheaper houses using new technologies, greater access to both credit for project development and to markets previously closed to them, and faster and cheaper registration costs, and others.

All of this greatly reduced the perceived risks in urban construction projects, a development that has not gone unnoticed by potential home buyers and financial organizations in the new house real estate market.

Marketing

A major government initiative to increase turn over in private house building included advertising projects in the media, at real estate trade fairs and shops, and the MVF web site[4].

Additional publicity came in the form of morning live television broadcasts showing high ranking government offi-

4. http://www.mivivienda.com.pe

cials during their tours to inspect and commission project building works.

Financing for buyers

Real estate is an important driver of the Peruvian economy. In the last 12 months, the programs managed by the MVF have helped to double the building industry's contribution to the Peruvian economy. Nevertheless, a major segment of the population nationwide does not yet receive financing to allow them to own a house. To narrow this gap, MVF has created the MVP and TPP programs described above.

3.1.3. Subsidies

The following chart shows the present structure of Peru's housing market, including the relations among players, and their respective market segments and positioning. MVF appears as a non-production, investment entity. It plays a key facilitation role in matching supply and demand through its MVP and TPP programs' second-tier loans channeled by IFIs to the B2, C and D income segments.

MiVivienda Loans

The product was designed under the premise that the government should act as a facilitator and promoter. These loan products should be sustainable over time to remove one of their main risk components.

MiVivienda loans provide funding to IFIs at a higher rate than the regular long-term rate from these entities. However, several collateral advantages allow them to make a profit, including lower loan risks (one third subordinate or two thirds proportionally), the matching of terms and currencies, the Good Payer Refunds (PBP) and a free financial margin. An attractive product design has lured already 34 IFIs to affiliate with the MVF to place their loans in almost every department (state) in Peru.

IFIs benefit from free margins they set themselves competitively, and from loan risk hedging, funding, currency matching, term matching, Good Payer Refunds, all of which translates into acceptable profit rates compared to the reduced risk they take. In addition they are able to expand their client portfolio and reach new market segments through additional financial products.

Also, the IFIs benefit through their other products. When customers choose an IFI to get a mortgage loan, they will usually buy other financial products such as credit and debit cards, consumer loans, Severance Payment Accounts (CTS), etc. from the same organization. A relationship may thereafter be built founded on the customers' loyalty for the organizations that trusted them. It is the IFI's decision to provide them with all their products in an atmosphere of cordiality and transparency.

We also have to understand that the main objective of MiVivienda credit is to finance the construction and purchase of new houses or expanding a previous construction. Eligible applicants must fill certain standards[5].

The value of the house[6] to be purchased or built must not exceed 35 Tax

5. (i) Not having benefited from Fonavi or Banmat programs, (ii) becoming eligible for an IFI mortgage loan, (iii) not owning a house.
6. Not including the value of the land and the value added tax.

Chart 2
Structure of Peru´s Housing Market

Role	1st tier organization	2nd tier organization	Type of subsidy	Income group
Type of investment				
Non productive investment (diminished borrower repayment capacity)				
Mortgage	Banks	Cofide** (Coficasa)		A, B1, B2
	IFIs	MiVivienda	PBP	B2, C1, C2
		Techo Propio	BFH	C3, D
	Banmat*		Banmat	D1, D2, E
	Banmat		Banmat	Natural disaster victims
Consumer credit provider	Banks			Payroll and self-employed workers
	Consumer banking			Payroll workers (B2-D1)
Productive investment (increased borrower repayment capacity)				
Commercial credit provider	IFIs	Cofide		Companies Self-employed workers (A-B)
Micro-credit provider	Multilaterals	Cofide (IDB, CAF***)		Self-employed workers (C-D)
	Banmat		Banmat	

* Banco de Materiales.
** Corporación Financiera de Desarrollo (Development Financial Corporation of Peru).
*** Corporación Andina de Fomento (Andean Development Corporation).

Units (UITs)[7] and the down payment should not be less than 10% of the total value of the house[8]. Nevertheless, borrowers can substitute their land plot for the cash down payment.

The maximum repayment term for Fund loans to the IFIs, as well as the latter's loans to direct beneficiaries, is 20 years. End-beneficiary loans with terms 10 years or longer are divided into two stages: the first one is the non-concessionary stage, covering 80% of the loan, and the second concessionary stage covers the remaining 20%.

Repayments for the first portion are made monthly while for the second stage repayments are made half-yearly.

7. US$ 32 130.
8. The total value of the house does include the value of the land and the tax.

Good Payer Refunds (PBPs) are awarded to payers who make their monthly payments punctually during a full half-year. They then become eligible for a concessionary installment for that period. Punctual borrowers therefore pay only 80% of the corresponding total half-yearly bill. The discount is transferred to the IFI that will in turn pay back only 80% of the initial loan granted by the Fund.

Although initially IFIs did not find the product attractive, through the Banks' Association (Asbanc) the MVF explained that despite more expensive MVF funds than the banks' own long term financing, this greater cost was compensated by the lower risk the offered by the Fund, and the PBP's lateral benefits to their clients.

Banks could therefore be free to channel larger funds to other more lucrative segments, would not run into major risk, and by eventually expanding their client base, could use their idle installed capacity. So the overall advantages exceeded the disadvantages.

Interbank is an interesting case in point. Initially they did not show much interest in promoting the product and were little involved. At a special meeting, the MVF explained the potential advantages of selling the product and the benefits obtained by its competitors when developing this market segment.

Starting from there, the change was radical. This year they became leaders for the number of loans awarded, and rank second for amounts of loans granted. Also, they bet on Techo Propio, the other Fund product targeting the poorest people of Peru.

Effects of the MiVivienda credit

A calculation of housing demand for this program –included in the demand survey mentioned earlier– determined that effective demand by the target segment of MiVivienda loans reaches about 145 185 houses, of which 44% would be located in Lima and 66% in the provinces. If the PBP component is included, effective demand rises to some 189 150 new houses, 43% in Lima and 67% in other cities.

The following chart shows PBP increases demand by 30% overall, with a greater impact in the US$ 8 000-US$ 20 000 and US$ 30 000 - US$ 35 000 brackets.

The Techo Propio Program (TPP)

MVF also manages the TPP targeting the poorest segments and in particular households with net monthly incomes around 1 000 Nuevos Soles[9].

The program's loans include a component from the beneficiary's savings, a direct subsidy (the Home Family Voucher, or BFH), and a loan component managed by the IFIs, except in the «Zero Debt» system, where only the first two are included.

For first-home purchases the direct subsidies are structured as follows:

- For new houses from US$ 4 000 to US$ 8 000, a subsidy of US$ 3 600.
- For new houses from US$ 8 001 to US$ 12 000, a subsidy of US$ 1 800.

9. US$ 287 at an exchange rate of 3,48 Nuevos Soles to the US dollar.

Chart 3
PBP impact on effective demand

	Lima	Other Urban Areas	Urban Peru
Without PBP			
Between 8 000 and 15 000	9 686	15 679	25 365
Between 15 001 and 20 000	9 327	11 429	20 756
Between 20 001 and 25 000	11 121	16 766	27 887
Between 25 001 and 30 000	10 403	13 188	23 592
Between 30 001 and 35 000	8 251	8 722	16 973
Above 35 000	15 067	15 546	30 613
Total	63 855	81 331	145 185
With PBP			
Between 8 000 and 15 000	14 708	22 229	36 937
Between 15 001 and 20 000	13 273	18 701	31 975
Between 20 001 and 25 000	13 991	18 025	32 016
Between 25 001 and 30 000	11 121	16 303	27 424
Between 30 001 and 35 000	11 121	13 212	24 333
Above 35 000	17 219	19 247	36 466
Total	81 432	107 717	189 150
Effect of PBP%			
Between 8 000 and 15 000	51,9%	41,8%	45,6%
Between 15 001 and 20 000	42,3%	63,6%	54,1%
Between 20 001 and 25 000	25,8%	7,5%	14,8%
Between 25 001 and 30 000	6,9%	23,6%	16,2%
Between 30 001 and 35 000	34,8%	51,5%	43,4%
Above 35 000	14,3%	23,8%	19,1%
Total	27,5%	32,4%	30,3%
Effect of PBP			
Between 8 000 and 15 000	5 022	6 550	11 572
Between 15 001 and 20 000	3 946	7 273	11 219
Between 20 001 and 25 000	2 870	1 259	4 129
Between 25 001 and 30 000	717	3 114	3 832
Between 30 001 and 35 000	2 870	4 490	7 360
Above 35 000	2 152	3 701	5 853
Total	17 578	26 386	43 964

Source: MiVivienda Fund, 2003.

Within the ranges indicated, the supply has concentrated on houses cheaper than US$ 8 000, in order to get the largest possible subsidy.

The target population for this program is in the C2 and D income groups who show the largest housing deficit. BFH supplements the borrowers' incomes to make applicants more easily eligible for loans.

Additionally, there are alternative ways for granting the subsidy to poor families who are already eligible for a loan, or who own a house or a land plot and wish to build on them. The following chart summarizes these options.

Effects of the Techo Propio Program

The MVF's demand surveys examined the impact of the Family Housing Voucher (BFH) on effective housing demand in Peru. Graph 6 describes the two impacts on effective demand:

The first one is a surplus for subsidized homes that may be invested in house improvement or extension. TPP project design is crucial as regards surplus invest-

Chart 4
Products managed by MVF

Product	Subsidy	Amount subsidized		Value of construction	Requisites	Income group
MiVivienda loan	Good Payer Refund (PBP)	20% of loan (Under 3% on the interest rate)		Up to US$ 32 000 (35 UIT)	Non-owners	B2-C1
Product	**Subsidy**	**Subsidy amount**	**Types**	**House value**		**Income group**
Techo Propio Zero Debt	Home Family Voucher (BFH)	US$ 3 600	New home purchase	Up to US$ 4 000	Non-owners (land or house)	D3
Techo Propio		US$ 3 600		From US$ 4 000 to US$ 8 000	Non-owners (land or house)	D1-D2
		US$ 1 800		From US$ 8 001 to US$ 12 000	Non-owners (land or house)	C2-C3
		US$ 2 800	Construction on property	From US$ 4 000 to US$ 8 000	Non-owners (land or house)	D1-D2
		US$ 1 400		From US$ 8 001 to US$ 12 000	Non-owners (land or house)	C2-C3
		US$ 1 200	Home improvement	Up to US$ 8 000	Non-owners (land or house)	D1-D2

ment to prevent these funds from being used in alternative activities, and thereby wasting the loan's social efficiency.

The second effect is the larger demand resulting from granting the BFH, or an additional 30 000 houses.

This demand was determined only considering the population earning under 1 000 Nuevos Soles who are willing and able to purchase a house, as explained before.

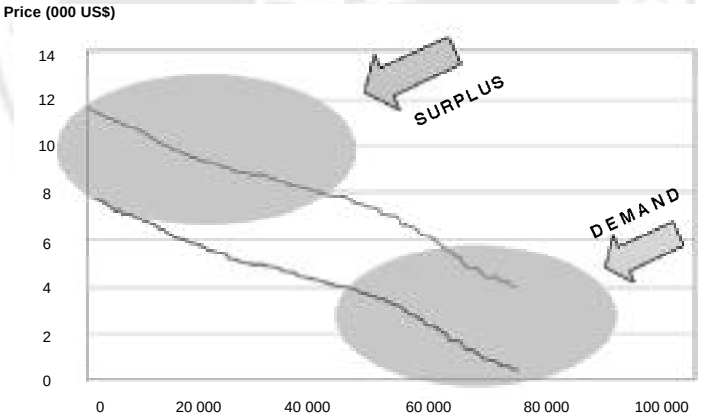
Banco de Materiales (Building Materials Bank)

The Banco de Materiales (Banmat) addresses the problem of the construction, extension and improvement of basic housing by providing loans in kind, i.e. building materials.

Banmat's main funding source is a revolving fund created by contributions to the Fonavi National Housing Fund, and additional contributions from Enace, MiVivienda, and others.

These loans target the poorest income groups through i) the Progressive House Building Program (individual loans), and ii) the Basic Housing Program (loans to groups of people, associations, housing cooperatives, etc.).

Banmat awards direct loans to borrowers with a high delinquency potential. Because they require frequent debt rescheduling and write-offs, these borrowers may have a negative impact on the culture of repayment, mainly in the D income group targeted by TPP loans.



Source: MiVivienda Fund, 2003.

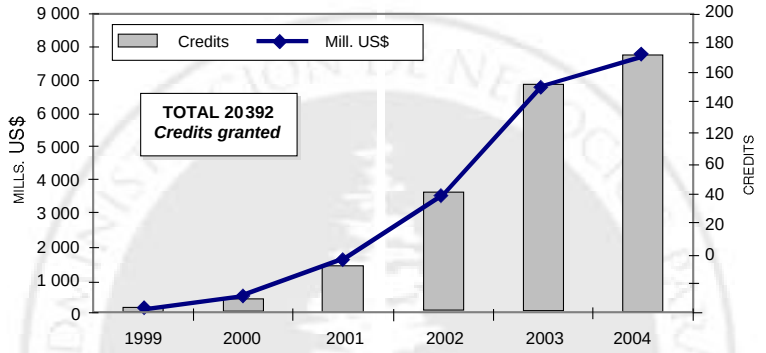
BFH impact on effective housing demand in Lima
Graph 6

3.2. Results

MiVivienda's mortgage portfolio has grown steadily and shows the lowest delinquency rates in the mortgage loans segment, with rates under 1%.

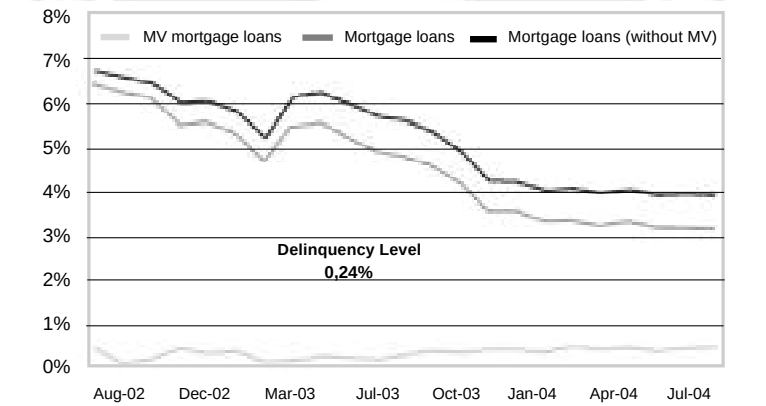
Meanwhile, in its first year the Techo Propio Program assisted over 9 000 poor families mostly for new home purchases.

Candidates apply for the subsidy at monthly calls for applications. After check-



Source: MiVivienda Fund, 2003.

Credits granted
Graph 7



Source: Asbanc, 2004.

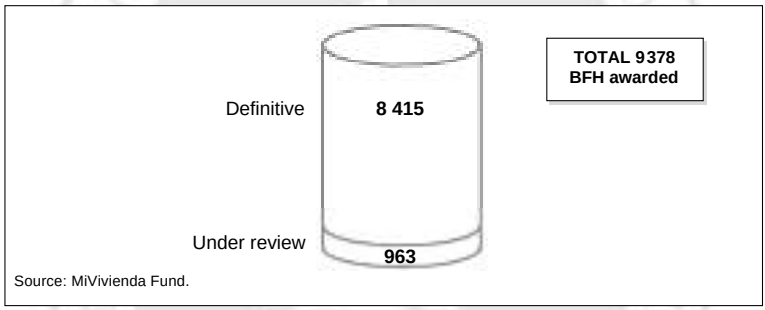
Delinquency rate
Graph 8

ing compliance with loan requirements, eligible families receive their Housing Vouchers. The vouchers are distributed daily and therefore there is no accurate figure for the number of beneficiary families.

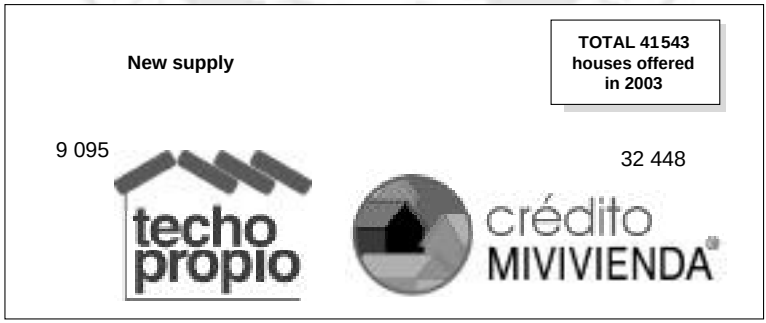
Although these two programs have dramatically increased the supply of homes in Peru, some 90 000 houses must be built every year just to close the existing housing gap.

An MVF study underway aims at determining the returns to Government investment in both the MVP and TPP programs, together with ongoing monitoring and follow-up of TPP beneficiaries to provide the baseline for a subsequent assessment of the program's impact on the assisted populations.

MVF programs create a return flow of government revenues either from MVP beneficiaries to the IFIs and then back to the Fund, and as national (federal) and as local taxes, rates on city services, property registration fees and other contributions to either the central or city governments.



BHF assigned (October 2004)
Graph 9



New supply of homes in Peru
Graph 10

Moreover, these programs have a direct impact on the construction and financial sectors and through them on the economy at large. This impact may be quantified by determining the multipliers for the industries directly involved in house building.

4. Development outlook

The time has come for restructuring Peru's mortgage market. Several Latin American countries have pulled ahead in developing housing plans and classifying their markets, and the MVF can benefit from their experience.

Government should not be involved in first-tier banking to avoid creating a perceived «credit-State» link that creates a poor repayment culture and hampers private capitals from flowing to this industry.

The proposed changes are a task for the housing sector that would thus foster a secondary mortgage market, with the following advantages:

- Better risk management for lenders in the primary market and lower credit risk for participants.
- Easier access to more resources for the housing industry that those available in local banks.
- Access to financing through the capital market.
- Better quality and cheaper financing thanks to safe property titles issued by either MVF or other agencies.
- Reduced cost of default provisions by eliminating the lenders' portfolio risk.
- Lower intermediation costs to the final borrower, by reducing the cost of access to the system and consequently increasing the number of potential beneficiaries.
- New long term investment options to institutional investors.
- Increased funds to replenish MiVivienda sources.

To the extent possible, market makers should act decisively to guide the financial market to adopt the structure described in the following chart:

For that purpose, the following initiatives may be taken:

- Removing government from first-tier financing operations and allow free private competition in this environment.
- Creating a financial fund with private participation (multilateral entities to reduce the risk perception, among others) to provide funds for mortgage financing, since MVF 's remaining resources, at the projected rate of loan awards, would be depleted by the end of 2005. Replenishing the MVF is not possible from the resulting margins because the subsidized borrower rate does not allow to reach the minimum profit rate required by investors. In future, this fund would necessarily be aimed at developing the secondary mortgage market, by securitizing mortgages bought from the

Chart 5
Peruvian financial market

Lists	First tier	Second tier	Subsidy	Segments
Type of investment				
Non productive investment (lower borrower repayment capacity)				
Mortgage	Banks	Cofide (Coficasa) (Secondary market fund with private/ MV participation)		A, B1, B2 (B2, C1, C2)
	IFIs	MiVivienda I roof Own (MVF improvement and supplier subsidy)	PBP	B2, C1, C2
			BFH	C3, D
	Banmat (exit)		Banmat (Merged with improvement fund)	D1, D2
	Banmat (exit)		Banmat (Natural disaster insurance fund)	Natural disaster victims
Consumer Loans	Banks			Payroll and self-employed workers
	Consumer Banking			Clerks (B2-D1)
Productive investment (increased borrower repayment capacity)				
Commercial credits	IFIs	Cofide		Companies Self-employed workers (A-B)
Micro-credits	IMFs	Cofide (IDB, CAF)		Self-employed workers (C-D)
	Banmat (exit)	(MVF improvement and supplier subsidies)	Banmat (Productive housing voucher)	

banks, and thus lure government and private capitals. It would also help avoiding short and medium term investment and fast turn over of a significant portion of these financial resources (through financial leasing and corporate bonds, among others).

- Operating the MVF as a credit quality improvement agent through the greater long term stability provided by the private fund described above. Better credit resulting from increased stability provided by the private fund would allow reducing investor risks and con-

sequently use the resulting mortgages for the poorest income groups.

- Creating a special insurance fund against natural disasters, thus removing the implicit risk created by natural disasters affecting the normal flow and direction of future funds' capitals.

- Enhancing productivity among the neediest to reduce the default risk during the mortgage loan's life. A special voucher for micro-credits may improve the beneficiaries' ability to honor their repayment commitments and reduce default risk since the final risk would fall on the credit quality improvement fund.

In its role as mortgage market promoter, the MVF has taken steps to develop housing solutions along the production chain, from the early builder/developer stage, through demand organization and induction, to linkages with private financing.

Since its inception, the MVF has been able to create a link with citizens, manufacturers and financing entities in the production chain. Now, it should grow to become a market catalyst, because surviving housing price and purchasing process distortions preclude potential buyers from making purchasing decisions based on quality information.

To correct the present situation, the MVF must promote market transparency for buyers to make better purchase decisions. In addition to transparent dissemination of price and process information, research about and involvement of large scale passive investors in this industry should be encouraged.

To adopt its new role as information broker, market catalyst, risk improver, and champion of the secondary mortgage market, the new MVF must address the need to create the necessary capacity to gather information about potential housing clients, suppliers, tender bidders, and open the option for very-large scale projects involving other organizations that can support using new products in developing the mortgage market.