FEASIBILITY STUDY FOR A LAND DEVELOPMENT FINANCING FACILITY
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A. Introduction

The main purpose of this study is to propose solutions and mechanisms to meet the needs of urban land development and provide for more efficient and focused use of government financial resources, while attracting greater private financial sector participation. A related objective is to ensure full cost recovery from beneficiaries.

This study is based on Government of Tunisia (GOT) land development policies. These policies are comprised of the following four main elements:

- The GOT will stop financing investments that can be financed by the private sector and balance public finances.

- Municipalities will play a larger regulatory role in decentralizing state functions, avoiding financial and operational responsibilities that are beyond their means.

- Public and private sector roles will be redefined to ensure greater private sector participation and increase economic and developmental transparency and efficiency.

- Social development and the cooperative sector will receive special attention.

The current task is to resolve the problem of financing land development and associated trunk infrastructure. This task, however, cannot be disconnected from issues involving the eventual use of developed lots. Consideration must be paid to the fact that such lots will be purchased for commercial or residential use, with purchasers obligated to cover all associated costs. This is of primary importance in the case of social housing.

To directly benefit low-income households, this study focuses on replacing the current system of indirect state subsidies for urban infrastructure and housing with a transparent, better targeted system. Replacing the current practice of indirectly subsidizing physical and financial costs with direct subsidies to beneficiaries will allow for full development and construction cost recovery. This idea is explored more fully below.

B. Land Development

Municipalities have the responsibility and mandate to implement urban land development programs. For implementation, municipalities use the following instruments: the urban development plan (Plan d’aménagement urbain or “PAU”); the land intervention perimeter (Périmètre d’intervention foncière or “PIF”); the detailed development plan (Plan d’aménagement de détail or “PAD”), etc. Today, other state agencies, such as the Housing Real Estate Agency (AFH) and the Urban Rehabilitation and Renovation Agency (ARRU), share urban land development responsibilities with municipalities.

One possible and desirable solution would be for municipalities to establish PIF’s to benefit private developers. Ideally, PIF terms would be longer and evolve over time.

Increased private developer participation frees municipalities from having to act as direct developers—a role for which they are ill prepared—and the need to search for required financing. This allows municipalities to concentrate on their proper main role as regulators and facilitators of the urban land development process.

C. Making Real Estate Subsidies More Efficient

In the current system, purchasers of serviced lots and social housing benefit from subsidies on physical and financial assets. These subsidies include below-market prices for publicly owned lands; infrastructure provided by municipalities below cost; public agency-provided loans at subsidized interest rates; and generalized tax exemptions.

Such supply-side subsidies do not necessarily reach targeted population groups, such as low-income households. By their very nature, supply-side subsidies are non-transparent and global, often unintentionally benefitting higher income groups. Subsidies produced by equalization mechanisms within planned housing developments suffer from similar distortions even when they seem to directly benefit the targeted population.

But if supply-side subsidies are replaced by demand-side subsidies—that is, if subsidies are directly given to intended beneficiaries—they can target low-income households in a direct, quantifiable, and transparent manner. Demand-side systems, successfully implemented elsewhere, have a number of advantages for both the state and intended beneficiaries. These advantages include:

- Subsidies exclusively benefit the targeted population
- Subsidies can be targeted to specific development zones, such as rural areas, spontaneous neighborhoods, and specified geographic locations
- Mortgages can be made at market interest rates (see example below)
- Increased private sector initiatives in real estate development lead to greater competition, increased supply, and decreases in cost margins and prices
- Beneficiaries can choose the conditions and location of their housing, leading to greater satisfaction (not always the case when the state provides its own solutions)
- Beneficiaries recognize state assistance, which is manifested by individual subsidy certificates

Direct demand-side subsidies can be facilitated by well-defined social policies. A system of qualifying points can be set up to establish priority for accessing the subsidy. Such a grading system can include applicant income level and household size, down payment amount, and housing development and construction costs.

To obtain a subsidy, the applicant must demonstrate his capacity to save on a regular basis and reimburse the loan. This requirement will create a large, new source of savings, which will increase bank balances in the country. In Chile, for example, there are almost 1 million savers registered as subsidy candidates out of a population of 14 million. The savings objective of the group is $950 million, with almost two-thirds already collected.

D. Participation By the Private Financial System

The private financial sector is currently excluded from participating in social housing financing, as it cannot assume supply-side subsidy costs now an inherent part of such operations. This is particularly true in the case of loans with subsidized interest rates.

However, if state directly subsidized beneficiaries, as described above, it would be easy to create favorable conditions for private sector participation in urban infrastructure and housing financing. This would open access to supplementary private financial resources, both at the primary level (commercial banks) and the secondary capital markets level (institutional investors).

When the state assists purchasers with a direct subsidy for acquisition costs, their mortgage loan requirements are reduced proportionately. As the reduced loan amounts can better support market interest rates, purchasers can pay back mortgages at market rates with monthly amounts comparable to what they would have had to pay for larger loans at subsidized interest rates. With a direct up-front subsidy, the purchaser will also start out with an equity stake in his home.

The resulting ratio of indebtedness to the value of the mortgage guarantee is greatly enhanced, presenting an attractive investment possibility for commercial banks and other financial institutions. In addition to being attractive for the issuing bank, this type of credit is also attractive in the secondary market.

Access to the secondary market is possible in two ways. The first is through rediscount facilities at second tier financial institutions. While not currently available in Tunisia, creating an ad-hoc institution to fulfill this role could be considered.

The second possibility is to use instruments and institutions that already exist in Tunisia to establish securitization. For example, SICAFs (closed-end mutual funds) could be adapted to act as a conduit.

SICAF organization and operations are already well established in Tunisia. In addition, the Tunis stock exchange offers a forum for negotiating secured mortgage securities. SICAFs could be used to acquire and hold mortgage loan portfolios originally established by banks or other financial institutions. By issuing SICAF shares through the stock exchange, a simplified form of securitization would be achieved. The SICAF shares would be more liquid, adaptable, and attuned to the needs of institutional and individual investors than the underlying mortgage instruments themselves.

A securitization system offers important advantages to banks and other lenders by providing long-term mortgage lenders with an opportunity to recycle loans several times after relatively short holding periods, thereby avoiding term risk exposure and the penalties (such as Basle/Cooke ratios and market ratings) of a highly leveraged, unmatched balance sheet. Also, by rolling over loan portfolio and collecting service fees or commissions, banks can generate off-balance-sheet revenues, as well as gain access to a larger client base.

A securitization system also offers important advantages to investors. It allows them to participate in a mortgage loan portfolio by investing in pertinent SICAF shares without the liquidity and negotiability constraints inherent in individual mortgages, while retaining the advantages of a real estate-secured, relatively high yielding credit. At the same time, a mechanism could be established to reassure investors concerning the market liquidity of the shares. The presence of a strong market-maker with stable, permanent purchasing power is of primary importance.

When seeking private participation in the financial sector, it is impossible to overlook the need for reliable and legal land titles. This is an issue that must be addressed and resolved.

E. Home Lease-Purchase

Another mechanism for consideration is home lease-purchase agreements. These agreements allow households without down-payment savings to have access to appropriate shelter. Home lease-purchase agreements can also be adapted to the above proposals on securitization and direct beneficiary subsidies.

Lease-purchase contracts generate a regular flow of cash payments and can be included in SICAF portfolios for securitization, in the same manner as mortgage loan contracts.

Qualifying individuals could receive direct subsidies under the same conditions as mortgage loans, but with one important difference: subsidy disbursement would take place on a delayed basis concurrent with monthly rental payments, instead of at the moment of purchase, as in the case of mortgage loans.