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HOUSING INVESTMENT GUARANTY

ZAIRE

Audit Report Number 79-34

Issue Date January 26, 1979

Area Auditor General, Washington
Agency for International Development
Washington, D.C. 20523

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Z A I R E

Project No. 660-HG-001

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AGENCY FOR INTERNATIONAL DEVELOPMENT

Washington, D.C. 20523

HOUSING INVESTMENT GUARANTY - ZAIRE

Project No. 66-HG-001

INTRODUCTION

The Housing Investment Guaranty Program is the principal means by which the Agency for International Development provides shelter assistance to the developing countries. Under this program, the U.S. Government provides a "full faith and credit" guaranty of repayment for long-term commercial-rate loans made by private U.S. lenders for housing projects in developing countries.

In January 1972, AID authorized the issuance of a contract of guaranty for a $10 million housing loan in Zaire. On July 31, 1972, the $10 million loan agreement was executed between the Federal Home Loan Bank of New York (Investor) and La Caisse Nationale D'Epargne et de Credit Immobilier (Borrower). On the same date, a guaranty agreement was signed by the Government of Zaire (GOZ) and AID, whereby the GOZ pledged itself to pay to AID any amounts not paid by the Borrower under the loan.

The rationale of the project grew out of the results of feasibility studies conducted in Zaire by the Office of Housing during 1971. The major thrust of the project was to assist in the establishment of a new mortgage institution (Borrower) to promote accumulation of local savings to help meet the demand for home loans. Secondly, the project provided funds for the development of a housing project to benefit lower and middle income families.

AID and its consultants agreed that the complexities involved in simultaneously undertaking a building project the size of Cite Salongo and establishing a new mortgage institution were beyond the management capabilities of the newly formed Borrower. This is a conclusion with which we concur. A major portion of the Borrower's energies were initially absorbed by the housing construction program, leaving little time for concentration on the institutional development of the overall organization. Price escalations during the mid-70s also had a serious impact on getting the project on a paying basis within the time envisioned.

The final loan drawdown was made on December 30, 1975, with the first of 85 principal repayments scheduled to commence on April 1, 1976. However, as of July 31, 1978, the GOZ owed $2,360,946 under its guaranty agreement for accumulated principal, interest and fees which had not been paid. (See Exhibit A for details.)

SCOPE OF AUDIT

This is the second audit of the Zaire HIG project, and covers activities from March 31, 1975, the cut-off date of our prior audit, through July 31, 1978. Our examination included such tests and site visits as we considered necessary in the circumstances. The purpose of our audit was to inquire into actions taken since the prior audit and also to identify areas requiring management's attention for improved operation of the project.

SUMMARY

The Borrower and the GOZ are in default on their required payments to the U.S. Investor and to AID. The total amount due and unpaid at June 30, 1978, was $2,360,946, which AID had paid to the Investor. In addition, as of July 31, 1978, AID had a contingent liability for unpaid loan principal of $9.4 million, plus interest. In May 1976, the AID Administrator waived the application of Section 620(a) of the Foreign Assistance Act (U.S. assistance to any country in default on any U.S. laon) as it applied to Zaire, and authorized a continuation of AID's bilateral program in Zaire. This waiver continues to remain in force at this time.

Attempts to obtain required payments have been earmarked by senior level exchanges and actions. Included was the U.S. Ambassador's February 1978 notification to the GOZ formally invoking the terms of the HIG guaranty agreement and requesting that the GOZ promptly pay AID all sums due from and unpaid by the Borrower. Although the GOZ did not make payment of the more than $1.6 million due as of October 1, 1977, as requested by the U.S. Ambassador in February 1978, it did make subsequent payments of $178,985 on September 27, 1978, and $231,324 on October 13, 1978.

The Borrower did not meet the major objective of developing into a viable mortgage institution in the country. The Borrower is neither financially nor operationally sound and has adopted several questionable management policies and practices, such as spending inordinate amounts on fixed assets, employing excessive numbers of staff, failing to cover costs with housing sales prices, and failing to insure properties despite AID's advice to the contrary. In February 1978, the Borrower requested additional assistance from AID in the form of three technical advisors. We are recommending that no further assistance be given to the Borrower until the Agency obtains firm assurances that the Borrower will improve its management policies and practices.

Although the housing project, consisting of 765 homes, is in a generally good physical condition, the project is plagued by continuing homeowner loan delinquencies. General economic conditions and problems with the individual lease/purchase agreements are contributing to the condition. We are recommending that the Office of Housing improve its review procedures for mortgage agreement forms for use in future HIG projects.

The findings and recommendations in this report were made available to Office of Housing officials. Their comments were considered in the preparation of this report.

FINDINGS AND RECOMMENDATIONS

Status of Loan Guaranty

The Borrower and the GOZ are in default on their required payments to the U.S. Investor and to AID.

As of July 31, 1978, the following amounts were owed AID (see Exhibit A - Schedule of Delinquent Dept - for details):

Principal and interest on loan - paid to Investor by AID	$ 2,310,880.45
Guaranty fees	122,276.89
Interest on unpaid installments	186,703.72
Total	$ 2,619,861.06
Less amount withdrawn from final loan escrow account - partial payment to AID	258,915.50
Total due AID by GOZ	$ 2,360,945.56

In addition, AID had a contingent liability to the Investor of $9,492,836.65, the outstanding principal balance of the note, plus interest.

The Borrower and the GOZ are in default on the HIG loan for several reasons. For one, many of the individual homeowners have been delinquent on their payments to the Borrower. Also, some of the amounts collected were not used for required payments by the Borrower, but rather were used to construct a new office building. In addition, the GOZ finds it difficult to honor its guaranty agreement and pay anything to AID because of a lack of foreign exchange. For over three years the GOZ has been unable to meet its foreign exchange obligations.

The contract of guaranty between AID and the U.S. Investor specifies that AID agrees to pay to the Investor any amount of loan principal and interest which the Borrower does not pay. As compensation for this guaranty, the Borrower has agreed to pay AID a guaranty fee of one-eighth of one percent on the unpaid loan due to the Investor. Finally, the guaranty agreement between AID and the GOZ provides that the GOZ irrevocably and unconditionally guarantees to AID the payment of (1) any amounts of principal and interest due by the Borrower to the Investor under the loan agreement; and (2) the guaranty fee due by the Borrower to AID.

From July 1973 through December 1975 the loan interest and AID guaranty fees were paid. On April 1, 1976, however, the Borrower failed to make the first scheduled payment of loan principal and interest due to the Investor, and also the guaranty fee due to AID. Consequently, the Investor notified AID of the delinquent payment and that, pursuant to terms of the contract of guaranty, there had been a default under the loan agreement. AID then began making the quarterly amortization payments due by the Borrower to the Investor.

In July 1976, after the Borrower again failed to make the scheduled payments, AID notified the GOZ of the default. AID requested the GOZ to pay AID the total amount of principal, interest and guaranty fees then due, according to terms of the guaranty agreement between AID and the GOZ, but the GOZ did not respond.

In May 1976, the AID Administrator waived the application of Section 620(q) of the Foreign Assistance Act (U.S. assistance to any country in default on any U.S. loan) as it applies to Zaire. He then authorized the AID Mission to continue its bilateral assistance programs in the country. At the time of our audit we were advised that the waiver remains in force.

In June 1977, the United States Government agreed to a consolidation and rescheduling of certain AID and other debts owned by the GOZ. Under the terms of that agreement, the GOZ agreed to pay all arrearages and future sums, as and when due, on Loan 660-HG-001, which was not rescheduled by AID. In February 1978, the U.S. Ambassador notified the GOZ of the Borrower's delinquencies, formally invoked the terms of the HIG guaranty agreement and the bilateral debt rescheduling agreement, and requested that the GOZ make full and prompt payment to AID of the more than $1.6 million due as of October 1, 1977.

In September and October 1978, the GOZ paid $410,309 against the outstanding debt to AID. In addition, the new director of the Borrower visited the Office of Housing on October 11, 1978, and announced the Borrower's intention to make future payments.

We concluded that the actions taken by the U.S. Government to collect the debt have been reasonable.

The Borrower

During the six years of project life, and in spite of AID assistance, the Borrower did not become a viable savings and loan institution in the country, a major objective. The Borrower is neither financially nor operationally sound. The more important deficiencies and problems are summarized below:

AID-financed advisors have for years noted that the Borrower has a record of overstaffing, overinvestment in fixed assets, and excessive administrative overhead. One example is the 1976 construction of a new two-story addition to its home office building at a cost of 700,000 Zaires (US $840,000) which was financed using funds that should have been paid AID. In addition, the Borrower follows the practice of collecting one Zaire ($1.20) a month from HIG project residents for refuse collection and other maintenance services at the project which does not cover the cost of services.

Of more serious concern is the Borrower's adherence to a policy of reselling foreclosed and abandoned housing units at their original sales price, which generally results in unnecessary losses for the Borrower. AID's regional housing advisor estimates that the houses could be sold at 50 percent more than their original sales prices. Although the original homeowners' ten percent down payment and all principal repayments are retained, the Borrower has to absorb such costs as loan arrearages and repairs on the properties. The Borrower's officials stated that, without GOZ approval, the unit sales prices could not be raised. The RHUDO/Abidjan has asked the Borrower to request such approval on numerous occasions. The problem continues to exist because the Borrower, for reasons which we were unable to determine, has failed to request such a change.

The foregoing factors contributed to the fact that the Borrower had accumulated an operating deficit at December 31, 1977, of about 2.1 million Zaires (US$2.5 million). The operating loss for each of the calendar years 1976 and 1977 was the same, about 700,000 Zaires (US$840,000).

Although the Borrower has established an adequate accounting system, and all ledger account cards were posted through December 31, 1977, financial statements for 1977 were not available at the time of our review. Furthermore, for the past two years, despite repeated efforts by AID, the Borrower has not submitted to AID the required reports on such items as project status, mortgage balances, and financial condition. In the absence of these reports, AID's knowledge of the project's status has been obtained by visits of AID-financed advisors. The Borrower's Accounting Director told us that the shortage of qualified personnel resulted in the delay in preparing financial statements and statistics.

Another example of management deficiency concerns the absence of insurance coverage against fire and casualty risks on the HIG housing units. At the time of each closing under the loan, the Borrower certified to AID that each housing unit was covered against loss, although, as we learned, no such coverage exists. The Borrower is collecting one Zaire a month from each of the project residents for this insurance coverage.

Although not a direct reflection of management practices, the growth of savings at the Borrower's offices has fallen far short of expectations. After growing to $3.3 million Zaires in 1975, the rate of increase in the dollar amount and number of accounts in Kinshasa deposits have declined radically. During 1977, savings accounts with the Borrower showed an average balance of just 40 Zaires ($48). Evidence suggests that savings accounts are being used as ordinary demand accounts and that few persons retain their savings over a long period of time, creating a liquidity problem for the institution.

The Borrower has recently attempted to obtain a 4 million Zaire (US$6 million) capital contribution from the GOZ to help ease its operating problems. Plans are to use the funds to construct 250 housing units for middle and upper income level families. At the same time, the Borrower has requested additional assistance in the areas of savings development, property management and statistics.

USAID/Zaire and Office of Housing have been aware of the Borrower's problems and provided various types of assistance. Notwithstanding this assistance, the Borrower continues to have serious difficulties.

The AID-financed assistance consisted of:

A resident advisor position was established and filled sequentially by three individuals, the last of whom departed Zaire in July 1976. However, there was a gap of nine months between the departure of the second advisor and the arrival of the third and last resident advisor.

An advisor with extensive background and experience in savings and loan management made five brief trips to Zaire between 1973 and 1975 for a total of about three months in Zaire.

DS/H provided for a construction management firm to be in residence during the construction of the housing project.

Between March 1977 and April 1978, the regional housing officer from Abidjan, Ivory Coast, made three visits and two visits were made by consultants with the National Savings and Loan League to review the status of the project.

In summary, the questionable management practices adopted by the Borrower are detrimental to the HIG project and to further institutional development for the housing sector in Zaire. DS/H has for years been reporting to Borrower management the problems and required corrective actions. The Borrower's top official admits to the problems and their seriousness. But the necessary corrective actions have not been taken. Under the present circumstances we question the feasibility of additional assistance until the Agency is reasonably assured that such assistance will be productive.

Recommendation No. 1

Office of Housing (DS/H) in conjunction with USAID/Zaire not provide further assistance to the Borrower until satisfied that the Borrower is prepared to adopt the management practices necessary to put itself on a sound financial basis.

Project Status

The HIG-financed Cite Salongo housing project is in generally good physical condition. However, the project is plagued by continuing homeowner loan delinquencies, a source of concern to the Office of Housing. The magnitude of the delinquency problem is troublesome, with the Borrower's records showing 340 (46 percent) of the 735 project loans over three months delinquent at September 30, 1977. Of this total, 232 loans were three to six months delinquent, and 108 loans were delinquent in excess of six months.

The housing loan delinquency problem can be attributed to a combination of factors. Some of the more important are the freezing of all wages in Zaire since 1975, a spiraling cost of living, and a lack of aggressive follow-up on mortgage delinquencies. In addition, we believe that certain defects in the lease/purchase agreements have contributed to the delinquency problem. For example, Article 5 of the lease/purchase agreement provides for a three-month lapse in amortization payments before the buyer is contacted. Then a month passes in written warnings and contract cancellations, after which the homeowner is given 90 days to vacate the premises. This seven-month period is excessive and often results in property destruction and high repair costs to the Borrower. Furthermore, there is no provision in the lease/purchase agreement for the collection of penalty charges on delinquent amortization payments. This factor smothers much of the incentive for prompt payment and also precludes the collection of a significant and valid source of income by the Borrower.

We believe the above two defects in the agreements should have been identified at the time the agreement forms were reviewed by the Office of Housing.

Recommendation No. 2

Office of Housing (DS/H) improve its review procedures for mortgage agreement forms to be used in future HIG projects.

EXHIBIT A

Schedule of Delinquent Debt

Zaire 660-HG-001

As of July 31, 1978

Date	Due Investor (Paid by AID) Interest @ 7.375% Per Annum	Principal Installments	Principal Balance	Due AID Guaranty Fee @ .0125% on Principal	Interest on Delinquency @ 7.375%	Total Delinquency Due AID by GOZ
1/1/76	$	$	$10,000,000.00	$	$	$
4/1/76	184,375.00 409.72 1/	46,383.68	9,953,616.32	12,500.00 27.78 1/		243,696.18
7/1/76	183,519.80 133.03 2/	47,296.86	9,906,319.46	12,442.02	4,493.15	491,581.04
10/1/76	182,647.77	48,228.01	9,858,091.45	12,382.90	9,063.53	743,903.25
1/1/77	181,758.56	49,177.51	9,808,913.94	12,322.61	13,715.72	1,000,877.65
3/17/77					15,788.15	1,016,665.80
3/17/77						(258,915.50) 3/
						757,750.30
4/1/77	180,851.85	50,145.69	9,758,768.25	12,261.14	2,018.04	1,003,027.02
7/1/77	179,927.29	51,132.93	9,707,635.32	12,198.46	18,493.31	1,264,779.01
10/1/77	178,984.53	52,139.61	9,655,495.71	12,134.55	23,319.37	1,531,357.07
1/1/78	178,023.20	53,166.11	9,602,329.60	12,069.37	28,234.40	1,802,850.15
4/1/78	177,042.95	54,212.82	9,548,116.78	12,002.91	33,240.05	2,079,348.88
7/1/78	176,043.40	55,280.13	9,492,836.65	11,935.15	38,338.00	2,360,945.56
	$1,803,717.10	$507,163.35		$122,276.89	$186,703.72	
				Total Due		$2,360,945.56

1/ Interest and fee for period prior to 1/1/76.

2/ Interest for 14 days - charged by Investor for late payment of the 4/1/76 installment.

3/ Partial payment to AID, as follows:

1/5/76 Final loan drawdown - deposited in escrow account		$1,000,000.00
5/10/76 Interest earned on account		17,184.83
		$1,017,184.83
5/10/76 payments, as directed by AID:		
Fiscal Agent - Interest and AID fees due 1/1/76	$178,632.83	
Lawyer's fees - Borrower's U.S. attorney	1,750.00	
Borrower	586,802.00	767,184.83
Balance		$ 250,000.00
3/3/77 Interest earned on account		10,358.10
		$ 260,358.10
3/3/77 Payments, as directed by AID:		
Lawyer's fee - Borrower's U.S. attorney	$ 1,442.60	
AID - partial payment on delinquency	258,915.50	260,358.10
Account closed		$ - 0 -

HOUSING INVESTMENT GUARANTY - ZAIRE

Project No. 66-HG-001

REPORT RECIPIENTS

Assistant Administrator, Bureau for Development Support (AA/DS)	1
Director, Office of Housing (DS/H)	5
Director, USAID/Kinshasa	2
Zaire Desk (AFR/CAWA)	2
Area Auditor General/East Africa	2
Auditor General	2
DS/DIU	4
AG/IIS	1
AG/PPP	1
AG/EMS	14