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PROMOTING HOME OWNERSHIP USING RETIREMENT BENEFITS

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Executive Summary

This study has looked at various ways in which retirement benefits funds have been used to enable scheme members acquire home ownership in different parts of the world through use of retirement benefits. Retirement benefits funds form an innovative way of promoting effective demand for housing by enabling retirement benefits scheme members to purchase houses. Singapore permits members to use up to 75 per cent of pension savings for securing mortgages, for the purchase of specific houses. Mauritius and South Africa allow schemes to issue loans directly to members as well as allowing scheme members to use an equivalent of 2/3 of their future benefits as security for obtaining loans from banks and housing finance institutions. Accumulated benefits are left intact. Borrowers only pay interest through the lifetime of the loan and access benefits to pay the principal amount at normal retirement. In South Africa, pension administrators raise housing finance through the capital markets by issuing pension-backed securities to enable members to acquire home ownership.

Kenya does not allow members of retirement benefits schemes to access their accumulated savings for purposes of securing a house. The existence of only five housing financing institutions in Kenya makes them uncompetitive and allows them to set very stringent conditions for one to qualify for housing finance. To many scheme members, borrowing from such institutions remains unreachable. While the option of accumulating own savings provides an alternative means for financing one's home ownership, it can only be realised after a very long time. To alleviate the above problem, accumulated benefits could be used as security for procuring housing finance. The industry can negotiate for favourable terms with willing credible financial institutions.

Homeownership is relevant to the retirement benefits sector because it hedges retirees against bad investments and cash flow requirements for rent, besides creating a sense of dignity and status.

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HOUSING AND RETIREMENT BENEFITS

1. INTRODUCTION

In Kenya today, housing requirements outstrip supply. Immediately after independence, the government, through designed public housing schemes, made efforts to develop houses to boost supply and contain the deficit. As a result, the housing deficit was contained at 60,000 units per year until the 1980s. Over the years, the shortfall has cumulatively increased. 750,000 and 1,500,000 households in the urban and rural areas respectively are in need of housing (National Housing Policy, 2004). The production rate of new houses, on the other hand, is estimated at only 20,000 - 30,000 units annually, mostly by the private sector. This rate implies that Kenya is faced with a housing crisis. The road to solving the housing problem remains a challenging one.

Key factors among many that have contributed to this unprecedented housing shortage include the government's low expenditure on public housing and infrastructure, high rural-urban migration and the limited and high cost of housing finance.

Faced with declining economic performance since the 1980s and into the 2000s and consequent declining in revenue collections compounded with donor funding embargo, the government was faced with a shortage of development funds. As a result, it could no longer continue developing houses to the required scale. Following therefore, the government significantly reduced its finances towards public housing. Over time it has been slowly downsizing its civil service in order to reduce its associated housing obligations. The government is currently selling its stock of houses at market rates to the public or requiring public servants occupying public houses to pay market rents.

Migration studies take cognizance of migration as one of the chief causes of housing problems in urban areas. People migrate from rural to urban areas in search of better economic prospects. Rural–urban migration in Kenya has been high. From only 7.8% of total population living in urban centres in 1962,

it increased to 16.8% in 1989 and is estimated to increase to 26.4% by 2010. This high rate of urban population growth has escalated requirements for housing. Unfortunately housing supply has not grown at the same rate. The rural population has been able to afford housing through use of traditional and available building materials, which affords the majority shelter, however deplorable.

Access to housing finance has been limited by existence of few profit-led mortgage-lending institutions, stringent conditions that borrowers have to meet (See appendix 1) and the high interest rates regime in Kenya. The banking crisis of the 1980s and 1990s saw more than 15 registered mortgage-lending institutions close down, leaving only five such institutions in operation (See appendix 2). To fill the gap, banks began to issue mortgage loans using short-term savings, culminating into high interest rate charges for housing finance.

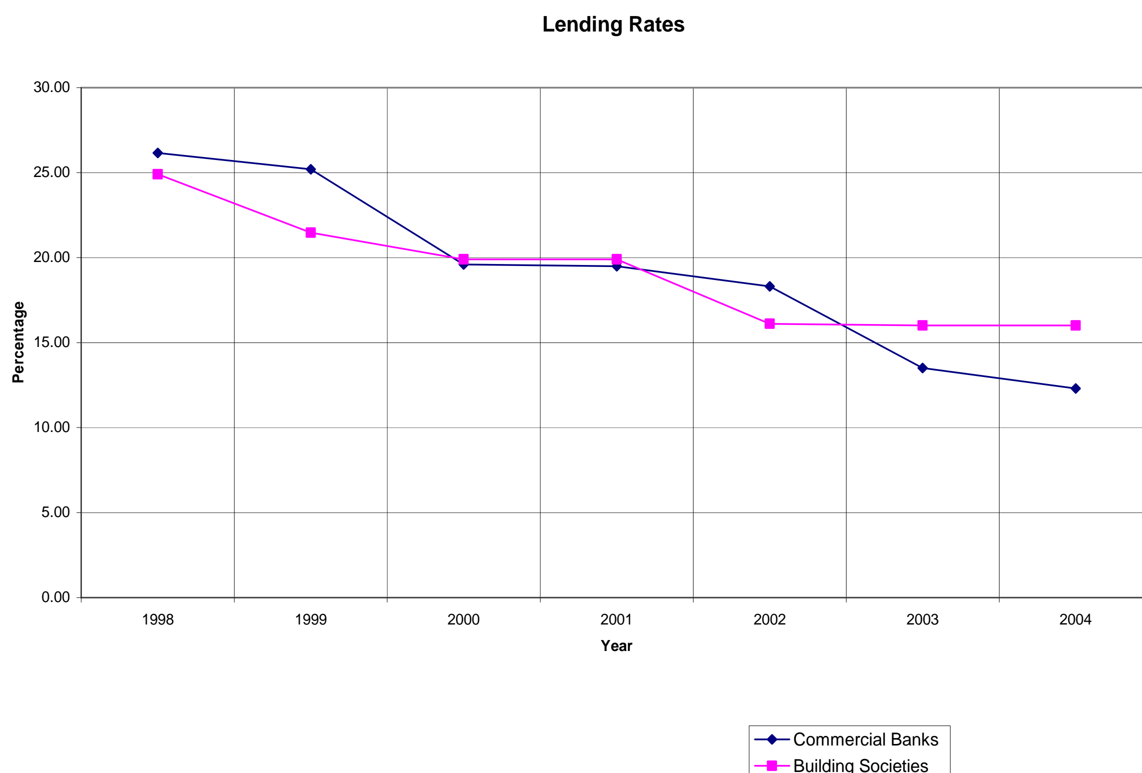


Fig 1: Graph showing the difference between commercial bank lending rates and building society mortgage rates

To address the housing shortage, the government in 2003 came up with a policy in which it documented its commitment to facilitate production of

150,000 new housing units per year in the urban areas. The government's role would be to directly engage in production of housing and to provide an environment that is conducive for the private sector to engage in house production. In its 2005/2006 budget, the government increased mortgage relief from Kshs 100,000 to Kshs 150,000 per year, a manifestation of its good intention to resolve the housing problem.

The housing problem can be addressed from two dimensions; Demand and Supply. The demand dimension deals with the promotion of home ownership through effective demand – supporting the desire for housing through economic ability. That is enabling people acquire finance to buy houses. Supply, on the other hand, promotes the construction of needed numbers of houses or repair of existing housing conditions to the required standards. While the government has addressed the latter, little has been done to promote the former. "The government is viewed to have failed in its objectives of providing adequate housing through promotion of home ownership. Households without effective demand have been left out. Households that afford to buy houses may not necessarily be in need of housing (Muthaka 2001).

According to the Economic Survey 2004, out of the estimated number of 1,727,644 Kenyans in wage employment, 96% earn less than Kshs30,000.00 per month. This is indicative that majority of Kenyans cannot easily afford to purchase housing. Meaning, the effective demand for housing is very low.

Resolving the housing problem through effective demand is evident in Kenya today. Institutional developers build a few showroom houses which are advertised for sale. Interested buyers commit to buy a house by making advance purchase payments even before the houses are completed. The institutional developers then utilise these funds to construct the houses. In actual sense the buyers' funds are used to construct the houses as opposed to developers raising money for construction then sell to recover the costs.

2. PURPOSE OF THE STUDY

Recognising the need to increase housing production to cater for the growing population, the government is increasingly looking for various sources of finance as well as encouraging private sector participation at individual and corporate levels to achieve this goal. Availability of affordable finances for both developers and buyers has been one among many factors that have contributed towards the housing deficit.

After taking cognizance of the economic value that the retirement benefits industry holds, the government undertook to reform the sector in 1997. Nearly a decade later, the government is looking to the retirement benefits industry as one sector that could significantly contribute towards providing finances for the housing industry.

The retirement benefits regulations permit retirement benefits funds to engage in property investments including housing/residential property albeit limited to a maximum 30% of total funds. Schemes can undertake to construct or purchase the property. Retirement benefits funds however, cannot be issued as housing loans or used to secure mortgages for the benefit of individual members of the scheme.

This study endeavours to discuss the various possible ways in which the retirement benefits industry could enable individual members use their accumulated retirement benefits savings to acquire housing, based on world practices, as an innovative contribution towards resolving the housing shortage in Kenya. As an extension of this study, computation will be done to show the contribution retirement benefits funds can make to the housing sector by enabling individuals to use their savings for housing purchase. Data on benefits accumulation by individuals, the rate of existence and entry of members, rate of return on investments, characteristics of beneficiaries and cost of housing will be collected to give more insight.

The rest of the study is organised as follows section 3 briefly discusses the role of Housing; section 4 gives an overview of the housing sector in Kenya;

section 5 outlines some of the housing initiatives that have been undertaken by different players; section 6 details the Retirement Benefits Sector's investments in Housing; section 7 details the experiences of other countries; and section 8 concludes.

3. THE ROLE OF HOUSING IN RETIREMENT BENEFITS

Housing has economic, social and political roles, and is an indicator of development and welfare in a country. As such it is an economic investment that contributes towards reducing poverty, generating employment, raising incomes, improving health and increasing productivity of the labour force.

Housing to an owner and occupier is an asset with an exchange value (equity) and use value respectively. Socially, housing plays the role of promoting privacy, dignity, safety and status among people. Politically, proper housing reduces political unrest emanating from deprivation and frustrations of people living in slums and informal settlements.

From the retirement benefits perspective, home ownership is part of retirement planning. Owning a house at retirement hedges the retirees against cash flow requirements - the need for income or cash to be spent on rent payment is consequently reduced. In addition, it hedges the retirees against bad investment decisions, poor investment returns and inflation. It also provides the retiree with social status and a dignified life. Home ownership greatly contributes towards supporting retirees' livelihoods and in maintaining the lifestyle of their earlier years.

4. OVERVIEW OF HOUSING IN KENYA

Kenya's National Development Plan of 2002 – 2008, affirms that shelter and housing are basic needs. This conforms to the UN declaration that everyone has a right to housing. Emphasising further the importance of shelter and housing, Nabutola, equated shelter to food which is a human need, so much so that those who cannot afford, still need it (Nabutola, 2004).

Since independence, the government of Kenya has aimed at providing affordable housing to all its citizens. To achieve this aim, the government, with the help of the United Nations, prepared the National Housing Policy of 1968/1969 to guide the development of housing in Kenya particularly in the urban areas. Until the mid-1970s the government, with the support of other government-related institutions – parastatals, central and local government bodies and the municipal councils - participated in direct development of houses to meet the housing needs. The government put in place the civil service housing scheme. At the time, since the civil service employed the largest workforce (one out of two wage earners was a civil servant), therefore meant that a large population had their housing needs catered for.

To further boost housing development, the government established the National Housing Corporation (NHC) in 1963 as an agency to tackle issues relating to housing and implement housing policies set by the government. The broad mandate of the Corporation included that of housing research, constructing low-cost houses and providing loans for rural housing to Kenyans. Since its inception the NHC has constructed only 40,000 housing units worth over Kshs 4 billion for mortgage, rental, tenant purchase and rural housing that cater for different segments of the population. NHC's performance has been severely affected by lack of funds, as evident in 1999 and 2001 when it was unable to complete any of its housing units. The lack of funds was exacerbated by lack of effective demand for some of the NHC houses as happened in Malindi and Thika.

All these efforts put together, Kenya continues to suffer a growing housing deficit that has grown from the maintained deficit of 60,000 houses per year in the 1980s to the current cumulative number of 750,000 and 1,500,000 houses in the urban and rural areas respectively.

5. HOUSING INITIATIVES

Following the government's inability to provide housing on the scale required, a number of housing initiatives have been tried by individuals, corporate institutions, development partners and Non-Government

Organisations (NGOs). Individuals mostly construct houses for own occupation. The rest provide funds to developers who contract or directly construct houses either for rental or sale.

Majority of households have had to contend with living in poorly constructed rental houses. 76% of the urban non-poor and 80% of the urban poor rent their dwellings (National Development Plan 2002-2008). Over 47% of the urban population seek shelter in informal settlements. Informal settlements are mostly constructed with undurable materials that do not conform to official housing standards. Houses are constructed and rented on room by room basis with many dwellers occupying single rooms.

In the last 10 - 15 years, households have taken the initiative to build houses for self-occupation (self-build). This number of households has been few. According to a study by Muthaka, 2001, majority of the population in Nairobi are tenants, indicating a low level of owner occupancy and citing reasons of high cost of finance and inadequate credit facilities. As a result, self-build housing takes an incremental approach. Household savings play a significant role in construction of self-build houses, which implies that to build a house one has to have a reliable source of income. Kamau et al, who noted that only 1% of the households that had self-build houses were unemployed, confirmed the importance of the ability to save.

To construct, individuals accumulate own savings and those who can afford borrow loans from co-operatives, banks and financial institutions. Individuals start by purchasing mostly subdivided land in the suburban areas, from where they proceed to build houses after accumulating additional funds or have fully repaid the initial loan borrowed. Individuals occupy own constructed houses before completion to avoid rent payment and instead use the funds in construction. Self–build houses take as long as 15 years to complete. Despite the constraints, self-build houses continue to be an important source of affordable shelter (Kamau 2004).

Employers have also contributed towards enabling their employees own houses through employer-supported housing schemes. The employers

contract financial institutions to administer some fund set aside for housing. Normally, special interest rates and down payments are negotiated.

At the corporate level, the Shelter Afrique Company has been directly involved in financing housing. Shelter Afrique Company hosted in Kenya, is a regional housing finance institution set up to promote housing and urban development in Africa by African governments with the support of African Development Bank. Shelter Afrique provides debt, equity finance and technical assistance to both private and public institutions for housing and related development.

Initially, Shelter Afrique was funded through equity from its shareholders. The equity enabled Shelter Afrique to mobilise resources from various donor agencies, international banks and multilateral development institutions for on-lending to developers with viable projects in member countries.

In 1998, Shelter Afrique broadened its resource mobilisation strategies by issuing debts in the debt markets of countries of interest. The first country where Shelter Afrique raised finances through a debt issue was Kenya in 1998. The debt issue target was to raise Kshs 350 million (US $ 4.6 million). The issue was a success, and although the debt was unsecured, there was an oversubscription. This opened a promising opportunity for mobilising funds for housing in Kenya and other regions.

Donor communities too have been at the forefront of funding slum upgrading programmes which aim of improving the informal settlements. Not discouraged by the little success achieved with slum upgrading initiative for Dandora in the 1970s , the German Government in 1992 extended a grant of about US $ 150 million for the improvement of housing conditions in Mathare 4A slums. Mathare 4A slums, just like other slums, were densely populated and houses had been built of temporary materials that did not meet acceptable building standards. Water supply and waste disposal systems were also of unacceptable hygienic standards.

The Mathare 4A slum upgrading exercise was faced with a number of challenges. US $ 800,000 and more was spent as compensation to "slum lords" who owned 90% of the houses, built on land they did not even own. It was necessary to have the slum lords adequately compensated since they made their life earnings from the rents.

However, a more serious challenge was in establishing affordable rents to the slum dwellers who were the eventual beneficiaries. Ideally, the rent charges were to be set at levels that would raise sufficient funds for maintenance and operations of the slum. In the face of increasing unemployment, this was difficult to achieve. Any efforts to increase rent were always met with resistance fanned by local leaders who took advantage of the situation for political mileage and agitated for rent reduction or rent boycott. The Nyayo Highrise slum upgrading programme, a tenant purchase scheme funded by the National Housing Corporation (NHC), while meant for the Kibera slum dwellers, ended up displacing the intended beneficiaries in favour of higher income groups.

6. THE RETIREMENT BENEFITS SECTOR'S INVESTMENT IN HOUSING

Until 1997, the economic and social significance of the retirement benefits sector in Kenya was not well recognised. Yet, in many western countries retirement benefits sectors are held dear because retirement benefits provide an avenue of mobilising domestic savings and hence are a source of cheap "patient" or long-term capital funds needed for long-term development. Following this recognition, the government of Kenya embarked on reform of the retirement benefits sector by enacting the Retirement Benefits Act and Retirement Benefits Regulations to govern the operations and administration of the sector. The new legislations, very specific to the running of retirement benefits schemes, first and foremost ensured legal separation of scheme assets from those of the sponsors, implying pre funding of schemes. The regulations also aimed at injecting professionalism and prudent investment of scheme funds through competent fund managers and at the same time introducing accountability for scheme operations.

Retirement benefits schemes enrol individuals who make periodic contributions to the scheme. The schemes invest and preserve the savings in the most prudent fashion in order to guarantee retirees a reasonable standard of living in retirement. Investments of scheme funds are guided by investment guidelines provided in the Retirement Benefits Regulations Table G. The table itemises the permissible assets schemes can invest in and gives the quantitative limits that should not be exceeded (see Appendix 3). Schemes are required to diversify their assets, except for:

- Schemes that opt to invest 100% in registered pool funds because they are inherently diversified; or
- Schemes with a value of Kshs 5 million and below who opt to invest 100% in government securities.

The quantitative guidelines aim at ensuring investments are made prudently and that schemes attain at least minimum diversification in their investments.

Schemes must develop an investment policy as an investment road map. The policy documents the schemes' investment objectives, risk tolerance and asset allocation options. Schemes have different investment portfolios because of their unique underlying circumstances (the age structure of the members, accumulated fund value and the contributions inflows). Asset allocation is very important in determining the returns on investments. Schemes with similar underlying circumstances and fund values may achieve differing investment performances because of the different asset allocation options. Because of their expertise, fund managers are mandated not only to assist scheme trustees tactfully select a range of assets, but also to specify how much of the total fund value will be invested in each of the selected assets at any one time. The Retirement Benefits Authority does not dictate specific investments for schemes.

Before the Retirement Benefits Act (1997) and Retirement Benefits Regulations (2000) were established and implemented, scheme trustees had no guidelines to follow when investing scheme funds. The most common type of

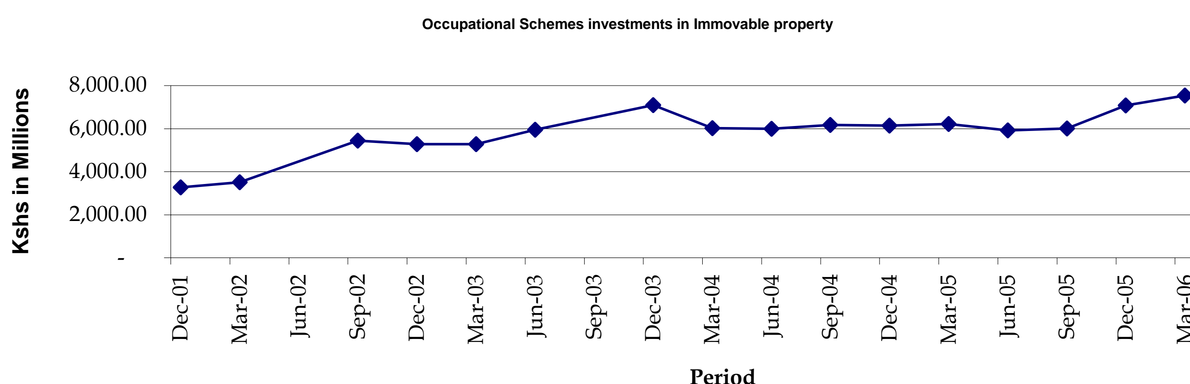
investments were in property – commercial, residential and land. Scheme funds were also used to secure loans for housing and mortgage facilities.

Sadly, investments in property provided a loophole for seepage of funds out of the scheme. Schemes fully paid for construction of buildings that never got completed; acquired properties at inflated prices, acquired non-productive pieces of land (old quarry sites) and sponsors and their peers who owned property found an easy avenue to dispose of their property to schemes at profitable margins. As a result, the returns on property were low. For example, on disposal, properties failed to fetch their cost prices. Further, in cases where mortgages were secured, not all the members of the scheme benefited. Sponsors and trustees were more privileged to secure better houses, sometimes many more times before other members got a chance, yet the scheme as a whole bore the liability. Because of these historical reasons, more stringent rules needed to be applied to protect scheme funds from such unscrupulous acts. For example, schemes need not be involved in actual construction of property but rather purchase already developed property that generate returns. It is not the core function of schemes to undertake construction.

The introduction of Retirement Benefits legislation has streamlined the industry. As at 2005, the sector has managed to mobilise Kshs 175 billion in retirement benefits savings an upward from an estimated amount of Kshs 120 billion in 2001. These savings are held in different forms of financial and real assets.

The retirement benefits investment guidelines categorises housing under the sub assets of broad category of investments termed "immovable property". The sub-assets include residential, commercial, land, property, unit trusts and collective investments schemes in Kenya. Collectively, schemes can invest a maximum of 30% of their total fund value in immovable property. In addition schemes can invest scheme funds up to 70% on equities and 30% in debt securities related to housing. Of the total industry fund of Kshs 175 billion, Kshs 37 billion (22%) is invested in immovable property. The National Social Security Fund (NSSF) accounts for the largest share of 82 per cent worth Kshs

32 billion in immovable property. Occupational schemes have invested the rest 18% or 7 billion. The NSSF had an more grand plan of investing in more residential estates, had it not been for the economic reform of 1996. Going by this data, retirement benefits schemes have up to Kshs 14 billion (8%) to invest in property to explore the maximum allowable limit of 30%. However, investing the remainder of the funds in property cannot be imposed on schemes. Schemes will invest in accordance with the interest of the members. Countries such as Zambia that forced schemes to invest in social housing activities are now moving away from such policies.



The table below show some of the residential estates retirement benefits schemes have invested in.

Residential Estates Constructed by Occupational Retirement Benefits Schemes			
Location/Name	**Value**	**Location/Name**	**Value**
Karen Residential	591,691,000.00	Kilimani	44,500,000.00
Muthaiga	83,563,165.00	Bendara lane	8,000,000.00
Ridgeways	72,000,000.00	Langata	40,195,000.00
Hurlingham	128,248,497.18	Loresho	62,500,000.00
Eldama Flats	26,500,000.00	Lower Kabete	145,000,000.00
Hatheru	72,000,000.00	Milimani Flats	103,562,000.00
Hazina Estate	1,105,164,000.00	Mountain View **	20,167,000.00
Hospital Development	132,174,000.00	Nyali Estate**	31,222,000.00
Kangemi Development	680,384,000.00	Ojijo Road	181,081,000.00
Kapsoya Estate	6,158,000.00	Rivatex Estate	28,411,115.00
Kileleshwa	33,200,000.00	Runda	3,600,000.00

Kitale Lane	31,599,990.00	Shauri Moyo Flats	77,000,000.00
Kitusuru**	89,511,000.00	State House Flats	719,274,344.03
Kisumu	1,479,084.00	Other	58,000,000.00
Simba Flats Nairobi*	773,000,000.00		

* *Under Construction* ** *have since been sold*

The Kenya Commercial Bank Staff Pension Fund is currently constructing residential property, "Simba Villas" worth Kshs 773 million. The Villas will comprise 192 flats, 60 maisonettes and a shopping complex.

Whereas schemes can invest in immovable property, clause 38 of the Retirement Benefits Act does not allow a scheme to use funds to enable individual members to procure housing, make direct or indirect loans to any person or invest with a bank or non-financial institution with a view to securing loans that include mortgages or any other consideration to the sponsor, trustees, members or managers of schemes. Further, the Retirement Benefits (Occupational Retirement Benefits Schemes) Regulations, 2000 section 22, restrict assigning of benefits for any purpose.

Much as property is a source of income that promises future capital gains, property investments are generally characterised as highly illiquid assets. Because of legal requirements, it takes a long time for property to be disposed of, therefore acts as a constraint to schemes, should large pay-outs suddenly be required. The absence of an open liquid competitive marketplace results in incongruent pricing. Property transactions are often at arm's length with different buyers quoting different prices. More often than not, property valuations - market value indicators - do not necessarily guarantee commensurate rental and/or disposal income earnings.

7. EXPERIENCES IN OTHER PARTS OF THE WORLD

i) The Case of Singapore

Singapore's retirement benefits scheme arrangement allows active members to access their accumulated benefits from their individual accounts or in some cases, to use future payments into that scheme while in employment and

before retirement. Access to benefits is strictly for housing, medical expenses and education.

Singapore runs a national provident fund – Central Provident Fund (CPF) whose genesis goes as far back as 1955. This fund was started as a strict fund for old age savings. Over the years, the CPF evolved into a fund that allows members to use the savings for other purposes other than for retirement. These include housing, education, investments and medical.

The CPF is a mandatory scheme for all employees who are citizens or permanent residents of Singapore. It is funded through joint employee and employer contributions, each making contributions of 20% of the employee's wages. The total contribution rate to the fund is a high 40%. These contributions are credited into three different accounts in specified proportions to allow for the access of benefits for the above mentioned uses. This means that members operate three different accounts: Ordinary, Medisave and Special at ratios of 30%, 4% and 6% of employee wages respectively.

The use of the funds in each of the accounts is dictated by the government. From the ordinary account with the bulk of savings, withdrawals can only be made to cater for housing, education, insurance-approved investments, and top-ups to parents and spousal retirement benefits accounts. Medisave account can be used for hospital costs and the special account for old age and contingencies. In addition, the government allows for withdrawal of a portion of their old-age money at 55 for members who have attained minimum savings level. Withdrawals for housing, medicine and education can be done at any time.

Despite the fact that ordinary accounts have helped boost Singapore's home ownership to around 90%, only about 40% of Singaporeans have managed to reach that savings threshold for retirement just a few years before retirement, because of not saving enough or withdrawing too much. Allowing social security contributors to tap into accounts could advance worthwhile goals but at a cost of reaching retirement very unsettled.

ii) The Case of Mauritius

Occupational pension schemes in Mauritius are allowed to use the scheme funds to give members housing loans. Schemes can allocate up to 26% of their assets for housing loans. There are no quantitative restrictions to the amounts of funds that can be issued as loans. For Example, the Central Electricity Board Scheme has 23% of funds issued as house loans and 75% issued to the employer. These combined effectively make the scheme under-funded.

Housing loans are in most cases issued at subsidised rates – rates below the prevailing market rates and at fixed rates, unlike Commercial Banks which issue loans at variable rates. In non-contributory private defined benefits occupational schemes, employers compensate their pension funds for the rate of the subsidy. The low default rate, long maturity and guaranteed returns are reasons for schemes' investment in housing loans. The benefits however come with the cost of servicing and origination (Vittas, 2006).

Existence of mortgage bonds and mortgage-backed securities would enable schemes to participate in indirect housing finance and avoid the cost of servicing the loans. The affordability of these arrangements and the security of benefits are however put at risk in the event of non-payment.

iii) The Case of South Africa

South Africa, like Kenya is faced with the problem of housing finance. Majority of South Africans are not able to afford a home of their own. Housing finance is unaffordable. To enable individuals to access housing finance, the Pension Fund Act allows retirement benefits schemes to use their funds to directly provide home loans at a minimum interest rate to its members because home ownership is regarded as part of retirement benefits planning. The home loan can be used to purchase, build, repair, improve or even redeem an existing house loan. The retirement benefits fund's role is strictly to provide security. Funds remain intact and are not disinvested from the fund. Members of the retirement benefits funds continue to make contributions to their scheme on periodic basis. The fund finances and administers the loans. In the event of default, the fund deducts benefits while in employment.

Recently, a bill was passed to allow pension funds to be used as guarantees to secure housing loans from specialised institutions that are better equipped to administer housing loans than the pension funds. The loan amount is limited to one third of the pension benefit outstanding at retirement age and should be repaid for a maximum period of 30 years. The loan must be repaid within the normal retirement date. Housing loans guaranteed by pensions attract favourable rates. Repayment of the loan is done in such a manner that only interest is paid at the lifetime of the loan on a monthly basis via salary deductions while members continue to make their monthly contributions to the fund. Repayment of the capital is paid through direct deductions from the accumulated benefits. Members are not restricted to which institution they should go to.

South Africa has further advanced fund mobilisation by developing a pension-backed securities market. In 2005, Alexander Forbes issued its first tranche of R750 of its R2bllion pension-backed securitisation programme to cater for 80,000 members of the 500 funds under its Housing Finance arrangement "Homeplan". The securitisation of the pension-backed loans will go a long way in sustaining Homeplan (Hogg 2005).

iv) The Case of United States of America

A number of pension funds in the United States of America, have created vehicles for the investment of public pension funds in a variety of national housing programmes for the benefit of pension fund participants. Through this arrangement the scheme participants acquire mortgages at favourable terms – both down payments and interest rates terms.

As early as the 1980s, public pension funds in various states of United States of America have been committing substantial portions of pension funds for construction of houses for low-income groups. The pension plans issue funds to developers who agree to construct houses at subsidised rates or enable low-income earners secure to mortgages at subsidised rates. The secured mortgages are used to purchase subsidised housing. Public Pension plans have also engage in renovating old abandoned houses that are in turn sold to members at subsidised rates.

8. CONCLUSIONS AND RECOMMENDATIONS

Kenya is faced with a severe housing problem. Currently 750,000 and 1,500,000 households in urban and rural areas respectively need housing. The production capacity is a dismal 20,000 to 30,000 houses per year. Lack of finance has been a major constraint in development of houses. Nearly a decade after reforming the sector, the government is looking towards the retirement benefits sector to provide housing finance. The housing problem can be addressed in two complimentary ways: promoting effective demand; and construction of houses for those in need of housing.

Retirement benefits schemes are permitted to invest 30% of scheme funds in immovable property, which includes – residential, commercial and agricultural estates and undeveloped land. The decision to invest in immovable property is made by each scheme depending on its unique characteristics - age structure, cash inflows from contributions and investment returns. Schemes cannot use scheme funds to advance loans directly to

individuals or use the funds for acquiring loans, including mortgages, from other institutions. To date the entire retirement benefits sector has spent 22 per cent of the maximum allowable amount of 30 per cent of total funds in immovable property, leaving Kshs 14 billion or 8 per cent unspent. Due to historical reasons the percentage amount has been limited to 30 per cent to give due protection to scheme funds.

High returns and long maturity nature of immovable property continue to attract retirement benefits funds for immovable property investments. However, immovable property is illiquid in nature and it lacks a common market, making it difficult for schemes to raise funds when immediate cash is required.

By amending clause 38 of the Retirement Benefits Act to allow schemes to use funds for lending to individuals as home loans or as security for mortgages financed by other institutions, retirement benefits funds will constitute a new source of capital for promoting effective demand for houses. Since individual and household savings play a crucial role in home ownership, individual and household retirement benefits savings can be used to facilitate home ownership for scheme members. Since housing loans have the potential of providing retirement benefits schemes with returns and long stability when structured with security for plan participants if default rates are low, the retirement benefits sector will achieve the double benefit of generating returns and hedging retirees against old age housing needs through the amendment of clause 38. Various methods can be used to realise the above.

Retirement benefits schemes could be permitted to issue housing loans to their members directly from scheme funds at prescribed minimum rates. Schemes would finance and administer the housing loan programme. Unfortunately, this exerts unnecessary burden to the schemes because it is not their core responsibility.

Alternatively, schemes could be permitted to use scheme funds as guarantees or securities for housing loans financed by specialised institutions at favourable interest rate terms. Engaging specialised institutions spares

schemes from the burden of administering the housing loans. Members' benefits are accessed while in employment in case of default.

As is the case of Singapore, members could be allowed to access a given percentage of their accumulated benefits to secure a mortgage for the purchase of specified housing such as those constructed by the government at subsidised rates. In addition, the government could use funds from the retirement benefits sector to develop housing and sell the same houses to the retirement benefits scheme members at subsidised rates.

Securitisation of loans backed by retirement benefits funds (pension-backed securities) provides another channel for obtaining housing finance to scheme members. Expanding the capital market by developing pension- and asset-backed securities provides a relatively large source of private capital for housing.

Retirement benefits schemes could finance a category of housing developers who agree to construct houses at concessionary rates and sell the same to scheme participants.

While all the above is possible, caution must be taken to ensure that retirees remain with sufficient savings for use during retirement because people cannot live on bricks and mortar.

RECOMMENDATIONS

To avoid a repeat of what happened in the past where schemes issued direct loans to members only benefited a few privileged members and due to the cost of administering housing finance by schemes, retirement benefits schemes should not be allowed to offer direct home or housing loans. Instead schemes should be allowed to use scheme funds as securities or guarantees for housing finance obtained from special institutions. Ideally money should not move from the scheme. The primary security should be the house. Access to the benefits while in employment should as a last resort in the event of default and if and only if the accumulated benefits will make good the default.

Double jeopardy of member losing both the benefits and the house should at all times be avoided. The scheme member should be allowed to continue building their fund for the future. This would allow for optimal investments of the funds and optimal accumulation.

Because interest payment takes a bigger portion of the repayments at the start, scheme members should be allowed to pay only the interest and repay the capital on retirement to ease the burden of repayment. The regulator should negotiate favourable interest rates and down payment of up to 5% down from the high of 30% on behalf of schemes.

9. APPENDIX

9.1 Appendix 1: Requirements for Loan Issue

In all cases, before financiers loan out money to individuals, certain requirements must be met. The requirements may vary slightly from one financier to another. These include:

1) The loan amount issued is tied to Financial Ability: an individual can only obtain loans 49% of net salary or 30% of gross, verified by Bank statement for the last three months.
2) Many Financiers prefer people in permanent or long-term contract employment
3) Individuals must meet 15 - 30% of the loan value. Financiers issue 70 - 85% of loan value.

Other costs a buyer must meet

4) Stamp Duty fixed at 4% of the value of the property
5) Valuation fees – though guided by the government schedule, they are negotiable
6) Legal fees inclusive of VAT
7) Negotiation fees with the financier – 1% of the loan
8) Insurance Cover – Fire and Mortgage protection

9.2 Appendix 2: Housing Finance Institutions

The main Housing Finance Institutions include:

1) Housing Finance Company of Kenya
2) (S&L) (formerly Savings and Loan Limited)
3) Equity Finance (formally Equity building Society)
4) East African Building Society
5) Family Finance Building Society

9.3 Appendix 3: Investment Guidelines

TABLE G **(r. 18)**

INVESTMENT GUIDELINES

Item	Column 1	Column 2
	Categories of Assets	Maximum percentage of aggregate market value of total assets of scheme or pooled fund
1.	Cash and Demand Deposits in institutions licensed under the Banking Act of the Republic of Kenya	5%
2.	Fixed Deposits, Time Deposits and Certificates of Deposits in institutions licensed under the Banking Act of the Republic of Kenya	30%
3.	Commercial Paper, Corporate Bonds, Mortgage Bonds and loan stocks approved by the Capital Markets Authority and collective investment schemes incorporated in Kenya and approved by the Capital Markets Authority reflecting this category	30%
4.	Kenya Government Securities and collective investment schemes incorporated in Kenya and approved by the Capital Markets Authority reflecting this category	70%
5.	Preference shares and ordinary shares of companies quoted in a stock exchange in Kenya, Uganda or Tanzania and collective investment schemes incorporated in Kenya and approved by the Capital Markets Authority reflecting this category	70%
6.	Unquoted shares of companies incorporated in Kenya and collective investment schemes incorporated in Kenya and approved by the Capital Markets Authority reflecting this category	5%
7.	Offshore investments in bank deposits, government securities, quoted equities and rated Corporate Bonds and offshore collective investment schemes reflecting these assets	15%
8.	Immovable property in Kenya and units in property Unit Trust Schemes incorporated in Kenya and collective investment schemes incorporated in Kenya and approved by the Capital Markets Authority reflecting this category	30%
9.	Guaranteed Funds	100%
10.	Any other assets	5%

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