

HOUSING FINANCE FOR RETURNEES
WITH REFERENCE TO THE WEST BANK AND GAZA
ISSUES AND POLICY OPTIONS

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Abbreviations and Acronyms

CHF	Co-operative Housing Foundation
HAF	Housing Assistance Fund
MoF	Ministry of Finance
MoH	Ministry of Housing
PA	Palestinian Authority
p.a.	<i>per annum</i>
PCBS	Palestinian Central Bureau of Statistics
PECDAR	Palestinian Economic Council for Development and Reconstruction
PHC	Palestinian Housing Council
PMHC	Palestinian Mortgage and Housing Corporation
UNRWA	United Nations Relief and Works Agency (for Palestinian Refugees in the Near East)
WBG	West Bank and Gaza

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Housing Finance for Returnees Issues and Policy Options

March, 2002

I. INTRODUCTION

1.1 *Purpose.* The purpose of this study is to explore options available to donors for assisting in financing housing for returnees from Middle Eastern host countries. The study has been completed in the context of returnees vis-à-vis the West Bank and Gaza (WBG),¹ but the logic is intended for application is a variety of geographical situations. To this end, the study reviews what is known about WBG housing demand and supply, the constraints to a more balanced private activity in the sector, and past public housing policy programs. Lessons for the success of any housing program for returnees are drawn from this sector background; general principles for such a program are established; and some options are proposed for consideration. As noted, while the options are proposed in the context of WBG, many of the principles could be applied elsewhere.

1.2 *Sources.* The study is based on existing literature, as described in Annex 1, as well as on long-term staff and consultant experience in WBG. Text references are given to tables and figures in the Statistical Annex (Annex 2), which summarize some of the more detailed information available.

1.3 *Organization of the paper.* The first chapter describes the conditions in the housing and housing finance sector in WBG, looking at housing demand and supply, and at the likely impact of returnees. The second chapter deals with policy-related issues, including the agenda for sector reform, the policy on housing provision to date, and issues related to designing housing programs to benefit returnees under current sector conditions. The scope of the analysis is limited to understanding the market and policy implications of an exogenous demand shock. The last chapter outlines specific proposals for donor assistance, in the form of funding ‘baskets’, designed to respond to the anticipated housing needs of returnees, while avoiding adverse impacts on the functioning of the housing market and on the sector development agenda.

1.4 *Caveat.* During the production of the paper, the political conflict continued to have a major impact on the economic situation in the WBG. It is estimated that as a result of economic deterioration during the Intifada, the median monthly income of WBG households has roughly halved between the fall of 2000 and the summer of 2001. This would put 61% of the household population below the poverty line as of August 2001, indicating the need for a radically different approach to the housing sector under these changed conditions. This study assumes that the current political and economic deterioration is temporary, and that a political agreement determining both the quantitative framework and the administrative procedures necessary to repatriate Palestinian refugees from Middle Eastern host countries will eventually be reached.

¹ Some of the concepts discussed in the paper are, however, also relevant to housing solutions for Palestinian households opting to remain in host countries.

II. SECTOR ANALYSIS

2.1 *Chapter overview.* The first section of the chapter looks at several aspects of housing demand in WBG, starting with a review of demographic trends, and the potential contribution of natural population growth and net migration to the number of new households. Household income and consumption patterns; housing preferences; prices and affordability; and availability of finance are all briefly reviewed, within the limitations imposed by the scope of the paper and availability of data. The second section reviews what is known about housing supply in WBG, starting with a look at the current stock and construction trends. The importance of the construction sector to the WBG economy is summarized, and some of the main constraints within the housing market are outlined. The last section looks at what is known about returnees and their impact on the housing market.

A. Housing Demand

Demographic Trends

2.2 *Population structure, natural growth and immigration.* The WBG population is characterized by a very young age structure, typical of countries with high fertility and relatively low mortality. Table 1 summarizes the WBG population structure, showing a high proportion of refugees, which is typical of a post-conflict population profile². A large local concentration of refugees is in UN-managed camps. The population has a very high natural growth rate of around 3.5% per annum, reflecting the very high total fertility rate of 6.1³, and causing total population growth to remain high, even at times of strong net *emigration* to the Gulf states, e.g., a growth of 3.2% p.a. between 1982 and 1991. With net *immigration*, population growth has been extremely high, as evidenced by a rate of 6% p.a. after the 1993 Oslo peace accord enabled a large returnee influx, and demand for Palestinian workers in the Gulf subsided.

2.3 *Population projections.* The ‘middle scenario’ published by the PCBS for the period 1997 to 2010 assumes a decline in the fertility rate to 4.65 in 2010, and projects a total population growth rate of 4.5% p.a., taking into account an assumed 500,000 returnees. This growth rate compares with the rate of 5% experienced by Jordan over the 1990 to 1998 period, but is significantly higher than other rates experienced in the region during the 1990s (i.e., Syria 3.3%, Egypt 2.3%, and Lebanon 2.1%). Under this scenario, the Palestinian population in the Palestinian Territory would increase from 2.8 million in 1997 to 4.9 million in 2010 (Table 1). An addition of another 100,000 net migrants would add only 0.2-0.25% to the 1997-2010 growth rate. Population growth, taking into account the PA’s scenario for the inflow of immigrants, is clearly dominated by natural increase.

2.4 *Housing demand projections.* No official projection for the number of WBG households is available to provide the missing link between projected population and future housing demand. There were about 450,000 households in WBG in 1997, the latest year for which data are

² The 1997 ratio of refugees to total population is 40% when only refugees within the WBG are considered, and 75% when (external) refugees located in the Middle East are included. This compares to a share of roughly 50% internal and external refugees in Bosnia and Herzegovina around 1995.

³ PCBS. The total fertility rate (TFR) is a measure of the average number of live births per woman.

available (Table 2). Average household size in WBG has been consistently high and, at 6.5 persons in 1997, is one of the highest in the world. In the author's view, the large average size reflects a degree of cohabitation and overcrowding, with 28% of households living in extended families;⁴ and indicates a high level of pent-up housing demand (para. 2.9). For the purposes of this paper, average household size is assumed to decrease to 5.0 persons by 2010; i.e., an acceleration of new household formation would follow a political settlement.. Clearly, the pace of the decline in household size would interact with the number of returnees and the rate of expansion of the housing supply. Used in combination with the PCBS middle population scenario, this would result in an annual increase of some 42,000 households to around 1 million in 2010 (Table 3), including an assumed 500,000 returnees. This would mean that the growth in *resident* housing demand for the period of 1997 – 2010 by far exceeds the expected additional demand generated by future *returnees* from Middle East host countries: new returnee households would contribute just about 1-1.5 % p.a. to a total household growth rate of about 6.5% p.a., whereas natural population growth and accelerated household formation would contribute about 3.5% p.a. and 2% p.a., respectively. Even if household size were assumed to remain high, the returnees' contribution to growth in housing demand would not exceed 1/3.

Housing Affordability & Finance

2.5 *Income & employment.* Prior to the Al Aqsa Intifada, about one fourth of WBG households were living in poverty⁵ – a key determinant being the employment status of the household head. The 1997 census reports 17% of WBG households with no employed household member; the proportion is higher in the camps (21%). A quarter of households have more than one employed member; the proportion is lower 22% in the camps, and household size is larger.

2.6 *Housing expenditures.* Table 4 shows key housing sector data for WBG. Housing consumption appears to be high relative to other countries with similar income levels⁶ Also, the average number of persons per room is relatively small. In contrast with developed economies, housing's share of expenditures *rises* with income, with the top 30% of the distribution spending 4.5% more of their expenditures on housing than the bottom 55%, hinting at the high cost level of formal housing. Consistently, housing expenditures are highest (about 23% of total expenditures) in the surroundings of Jerusalem and Gaza which provide the easiest access to the Israeli and local labor markets, and have seen the largest influx of relatively well-to-do returnees.

⁴ Figure 1 in Annex 2 illustrates the possible pent-up demand through lagged household formation; i.e., existing or planned nuclear families living in the same household as part of an extended family.

⁵ World Bank (2001), referring to the year 1998.

⁶ Mayo (1995) points out that WBG at 15 sq. m. per person seems to have a comparatively high consumption level. Newly constructed units at 133 sq m in 1987 are among the largest in the world, whereas the average for existing buildings, at 98 sq m. is at par with Singapore and Norway. Neither average sq m consumption nor its distribution are known with certainty. The high space consumption is usually associated with social factors, such as high preference for homeownership (e.g, Massar, 1998), absence of long-term financial investment alternatives, and with political risks such as confiscatory taxation or expropriation of undeveloped land.

2.7 *Housing prices.* Prices appear⁷ to have risen through the 1990s as demand increased faster than supply; with relatively large price swings in Gaza, but more stable prices in the West Bank. It is likely that transaction prices have been less volatile in the secondary market -- where vacancies are lower -- than prices for new apartments. Ask prices for vacant apartments seem to have dropped lately, partly below costs. During the 1990s, sale prices appear to have fluctuated more than construction costs, which have been stable and high. House price to median income ratios are estimated to be above 10 for new housing, and between 5 and 6 for existing housing.⁸ This would put WBG into a high bracket compared to the US or Latin America, but roughly in line with Middle Eastern standards with their high consumption and construction costs.

2.8 *Housing finance.* Figure 2 gives an overview of the channels for housing finance in WBG. Housing finance is relatively undeveloped, with virtually no long-term financing available for homebuyers. Commercial bank finance is limited to short-term loans to developers.⁹ As is the norm in such situations, housing developers (both private and public) in WBG support the demand for newly constructed units by entering into pre-savings and leasing or installment sale arrangements with prospective homebuyers. If finance is not provided by developers, the funds come from equity sources such as domestic bank savings, remittances, and sale or swap of land already owned by prospective homeowners. It is reported that over 50% of homebuyers in WB towns already own land, and almost a quarter already own a building.¹⁰ Commercial banks have been slow to originate mortgages for the secondary market institution – the Palestinian Mortgage and Housing Corporation (PMHC) created in 1998. A USAID funded program for short-term modernization and home extension loans was set up in Gaza in 1995 and managed by the Co-operative Housing Foundation (CHF). In this program, commercial banks operate as loan servicers and fund a small portion of the loans *pari-passu*.

Latent Housing Demand

2.9 *Consumption and quality gaps.* The 1997 PCBS population and housing census identifies housing consumption and quality gaps, concentrated both geographically (Gaza, rural West Bank) and socially (camp dwellers, unemployed). There are three indicators for a high latent housing demand: overcrowding; cohabitation of nuclear households within an extended family; and the level of informal or substandard housing:

- *Overcrowding.* The available data indicate an average of about 2 persons per room, which does not seem to indicate general overcrowding in regional perspective. However, with 28% of households having more than 3 persons per room, there is clearly significant local overcrowding, particularly in Gaza and in camps (Table 4). Overcrowding is partially correlated with cohabitation of nuclear families, but the extent is not known. When the cohabitation factor is disentangled, the impact of overcrowding is likely to be

⁷ There is no transaction-based database.

⁸ Mayo (1995)

⁹ See Table 5 for estimates of credit for the construction sector.

¹⁰ Massar (1998).

largest concerning demand for enlargement of existing units, which currently accounts for between a quarter and a third of new construction.

- *Cohabitation.* About one quarter of WBG households are living with extended families. This, together with relatively high per capita consumption, may indicate housing market distortions, in particular the unavailability of rental housing for young households and a scarcity of low-cost construction options. It is unclear to what extent cohabitation can be transformed into actual housing demand, but indications are that willingness-to-pay of these households is relatively large, and that, with reductions in cost and increased availability of housing finance, significant demand potential could be unleashed. Although some of the demand would go into housing enlargements, most would likely be for new units.
- *Quality deficit.* Most structures in WBG are permanent; 95% having permanent walls.¹¹ On the other hand, according to a study by the Co-operative Housing Foundation,¹² 60% of units in the camps cannot be upgraded. This means that, together with other such units, about 16% of all structures would eventually need to be replaced, many through joining currently separated adjacent units. Construction tends to be monotonic and over-dense, with lack of privacy and inadequate public spaces, particularly in camps. Another critical quality issue is inadequate physical infrastructure, particularly sewerage in the West Bank. It is unclear to what extent quality deficits are correlated with poverty, and hence difficult to quantify the demand impact under different scenarios.

2.10 After a political settlement, income is expected to rise, converting latent demand into effective housing demand. A certain counterbalancing effect may be exercised by expected greater mobility and lower transportation costs.

B. Housing Supply

Stock Characteristics

2.11 *Size of the stock.* The census reports the number of housing units in the Palestinian Territory (excluding East Jerusalem) to be 390,000 units, of which 256,000 (65.9%) are in the West Bank and 133,000 (34.1%) are in Gaza.¹³ WBG is highly urbanized, with the urban stock accounting for 53.4% of the units, and the camps (almost all urban) for an additional 14.7% of units.

2.12 *Vacancies and stock losses.* Strong production since the start of the peace process has created a significant number of unsold, currently vacant, upscale apartments. An estimated 16% of new construction is vacant in Gaza (Table 6); and a much higher proportion in the West Bank (about 50%); however these units tend not to be available as a flexibility reserve because they do not match the quality and affordability characteristics of the bulk of the demand. Stock losses of

¹¹ Mayo (1995)

¹² CHF (1993).

¹³ According to Aronson (1998), the number of units in Israeli settlements at the same time reached about 50,000.

about 300 units in Gaza are reported by the Ministry of Housing (MoH) as having occurred during Intifada II through acts of war, and nearly 700 public housing units in Gaza have been allocated to the internally displaced.¹⁴

New Construction Activity and Costs

2.13 *New construction activity.* WBG experienced strong construction in the 1982-1991 period, with an official growth rate of 3.2% p.a. However, it has been estimated that informal construction activity of an equal size was also taking place during the period.¹⁵ The higher proportion of informal construction before the Oslo agreements probably reflects the greater difficulty of obtaining a building permit from the Israeli authorities. Anecdotal evidence suggests that the share of licensed and registered construction in 1998 was around 80% of the total, promoted *inter alia* by a moratorium on construction permits.¹⁶ Using this estimate to adjust the figures on licensed construction (15,600 units p.a., or 5.6 per 1000 inhabitants in the 1996 – 2000 period)¹⁷ gives an estimate of about 6.6 units per 1,000 inhabitants. Translating into a stock growth of between 4 and 5% p.a., this construction activity would roughly match population growth (4.1% p.a., 1996 to 1999), but leaves little room for reduced household size. Construction licenses have dropped by more than half, comparing the last quarter of 2000 (the first three months of Al-Aqsa Intifada) with the last quarter of 1999.¹⁸

2.14 *Investment, employment impact.* Housing construction is highly important to the Palestinian economy, which has a very small tradable goods sector. The share of construction in GDP has consistently increased since the 1970s and peaked at about 25% in the mid-1990s, when housing and construction investment made up about 75% of private investment¹⁹. About 22% of employed people work in the construction sector, including those employed in Israel.²⁰ Table 7 shows that domestic labor supply rose fairly steadily until the Oslo agreements, but later became subject to high volatility due to the dynamics of border closures and substitution of Palestinian labor in Israel by immigrants from Russia. Lack of access to construction work in Israel has been a main cause for unemployment in WBG,²¹ and has recently put downward pressure on construction wages.

2.15 *Cost levels.* WBG new construction types and costs are relatively uniform. Cost levels for urban apartments, net of developer profit, reach about \$40,000 in Gaza, \$50,000 in Nablus and \$65,000 in Ramallah. Reasons for the high costs of new construction are reviewed below:

¹⁴ 2001 figures.

¹⁵ Mayo (1995). It has proved difficult to confirm this estimate empirically.

¹⁶ Massar (1998).

¹⁷ Figure 3 shows quarterly construction licenses during the period.

¹⁸ New construction in Israeli settlements on the territory of WBG reached about 5,000 in 1997. Aronson (1998).

¹⁹ PEC DAR (1997), data for 1994.

²⁰ PCBS. Figures (for the end of 2000) include construction workers in Israel.

²¹ The macroeconomic indicators in Table 8 include estimates of unemployment from 1995-1999.

2.16 *Supply distortions in the urban land markets.* Regulatory distortions increase the premium for converting agricultural into residential land:

- municipal restrictions on land use, some of which appear to be the result of overly formalized planning standards;
- land use restrictions imposed by Israel, e.g., in proximity to Israeli settlements,
- insufficient size of subdivisions for large-scale housing projects,
- a high share of public land ownership and control, especially in Gaza.

2.17 *Backlog in land surveying and property registration.* In WBG, only 25-30% of properties are registered,²² severely reducing the scope for collateralized lending, and rendering transactions insecure.²³

2.18 *Low government investment in infrastructure.* The state of infrastructure in WBG is a constraint to the rapid growth of serviced land. In addition to Israeli control over sources and distribution of energy and water, weak governance and poor cost recovery by Palestinian utilities are among the largest problems. For instance, only 2 out of 28 water companies cover full maintenance costs, only 1 covers capital costs. Frequently, the developer is required to provide feeder infrastructure, in an inefficient manner, increasing the price for developed land;²⁴

2.19 *Constraints in construction input markets.* Constraints on imports and local import substitution capacity add an estimated 50% to the price of construction inputs in WBG; for some materials (cement and iron bars) the percentage is even higher.²⁵

2.20 *An inefficient developer industry.* The inefficient scale and financial structure of the developer industry is an important cost factor. Due to lack of construction finance (para. 2.22), developers primarily self-finance new construction projects out of the cash flows of finished developments. Since long-term finance for end-users is also not available, the typical entrepreneur remains constrained to a small number of projects with low capital turnover, and consequently high capital and operations costs. Developers thus have low leverage and remain small, which in consequence impedes the exploitation of scale effects. The problem is particularly pronounced as far as low-cost unit production is concerned.

2.21 *High minimum building standards.* High standards, especially in urban areas, have contributed to high construction costs, *inter alia*, widespread masonry construction, setbacks, lot coverage and height restrictions²⁶.

²² Compared to 80-90% in Jordan, for example. Source: Diamond et. al. (1999)

²³ The use of power of attorney as an alternative instrument substituting land titling in the past has led to fraud, and has now been banned by the courts.

²⁴ According to PECDAR (1997), the combination of high land conversion and development premiums drives up the share of developed land costs in total costs of detached housing to about 50%, by far exceeding the international rule of thumb of about 30%. In high-density urban construction, land costs will still account for a fifth to a fourth of total construction costs, depending on density levels.

²⁵ PECDAR (1997) estimates.. "cement and iron bars are respectively 2 and 3.5 times higher in Palestine than in Jordan."

²⁶ PECDAR (1997)

2.22 *Lack of construction finance.* Limited availability of construction finance adds to construction costs. Because of the high risk environment, bank lending is mainly short-term, and associated with strict collateral requirements.²⁷ Also, in order to find buyers, developers have to extend loans to consumers.

2.23 *Sufficient supply elasticity despite structural impediments.* There is some indication that, despite the cost barriers discussed above, new housing construction activity has interacted fairly closely with price signals in WBG in the past decade; however, the causality is unclear.²⁸ The main bottlenecks for new construction on the margin appears to have been land scarcity and conversion constraints in high-demand locations (Ramallah, Bethlehem, Gaza), the provision of public infrastructure for land development, and housing finance. It is, nevertheless, likely that, in a scenario of economic recovery, cost constraints would become more strictly binding, as housing will tend to lose the current function of wealth storage it has for many investors, with little regard to yield; and housing demand will pick up.

Housing Stock Efficiency

2.24 *Inefficiencies in the use of the stock.* In an efficient housing stock, low-quality units are readily vacated by households as their incomes rise over time and they realize demand for higher-quality units. Making aging or depreciated units available to low-income, young and mobile households through these moving chains (a “filtering down” of housing²⁹.) reduces the pressure for both new construction and government intervention. In WBG, general mobility constraints for households (largely imposed by the occupation regime) and the cost of new construction tend to be important impediments to this filtering process. Particularly challenging is the lack of diversification of tenure forms that tends to block moving chains.

2.25 *Small rental sector.* Rental housing is the traditional target sub-sector for young and mobile households. The home-ownership rate is about 78% in WBG, a very high figure if compared with neighboring Arab countries (e.g., Jordan 64%)³⁰. The share of rental housing in Gaza is officially reported at only around 5 % of units, and the ratio is only somewhat higher in the West Bank, at 12%. While there is evidence of a higher share in some West Bank towns where rents have drastically increased after 1993³¹, rent control and taxation problems limit the sector’s size:

²⁷ Credit constraints in WBG are described in the Finance Reform Project documentation (World Bank, 2001), including the difficulties of using land as collateral (problems with clear title, lack of registration, multiple owners, non-resident ownership, etc.)

²⁸ Comparing construction data (Figure 3) and housing costs (Figure 4) would suggest at least that strong construction activity slows the housing cost increase, and vice versa.

²⁹ Housing units can also “filter up” as they are renovated or rehabilitated. Filtering can also be seen from the perspective of households who during their lifecycle will upgrade their housing solutions, from cohabitation and informal solutions, to rental housing, to the homeownership sector.

³⁰ PCBS.

³¹ Massar (1998).

- Rent control in the current rigid form inherited from Jordanian and Egyptian law not only creates a bias of long-term over short-term rental yields, it also creates high levels of legal informality. A result has been rent level overshooting in new contracts, particularly in Ramallah and Gaza.³²
- Taxation of rental units is perceived to be high: investors are allowed only a limited deduction of operating and capital costs from rent revenues for income tax purposes; and the introduction of a gross rent tax is a revolving political issue. Both undermine the sense of investment security for investors.³³

2.26 *Insignificant co-operative homeownership.* A second key sub-sector for access of low-income households to homeownership is the co-operative housing sector. Although this is strongly developed in neighboring Jordan, no figures are available for WBG. Anecdotal evidence suggests that the formation of housing co-operatives is currently limited to public sector employees, where it is triggered by the incentive that beneficiaries receive public land as an in-kind wage. Legal, regulatory and tax reasons seem to pre-empt a broader development.

C. Housing Demand Profile of Returnees.

2.27 *Demand profile of past returnees.* An understanding of the socioeconomic characteristics of future returnees is key for successful planning, including planning for housing. There is evidence that past returnees have accounted for an estimated one-fourth of new home buyers, and have been relatively wealthy in comparison to resident homebuyers³⁴. Their role as housing seekers was particularly pronounced in areas with a labor market for the formally employed, e.g., Gaza and Ramallah.

2.28 *Likely demand profile of future returnees.* The housing decisions of future returnees after a political settlement will depend to a large extent on the relative strengths of economic and social factors prevailing under a peace agreement, including the decisions made by current host countries and other potential future host countries involved in the settlement. Under these circumstances, it is more useful to describe the potential housing demand in a qualitative way rather than attempting to calibrate demand. One important group is likely to be ‘*emergency returnees*’, for whom local push factors in their current host countries may dominate over economic migration incentives. Another group could be described as ‘*economic migrants*’ -- Palestinians who may be able to make migration decisions based primarily on options and economic opportunity, and face no disincentives to staying in their current host countries.

2.29 ‘*Emergency returnees*’. This group may require fairly extensive social programs and economic integration efforts: i.e., a comprehensive social or community approach, supporting social services and income generation, as well as housing, may be the appropriate integration model to consider for this group. Housing solutions will likely feature both a high preference for

³² See Figure 5.

³³ A full overview of tax issues would go beyond the scope of this paper; World Bank (1998) and PMHC (1998) both provide - incomplete - overviews.

³⁴ Massar (1998).

homeownership and the need to provide new construction in new developments, leading to relatively high subsidy/household ratios.

2.30 *'Economic migrants'*. These will primarily respond to economic opportunity, and thus place additional stress on the housing markets of Gaza city and the middle governorates surrounding Jerusalem. These markets are at the same time the primary target markets of resident families living in cohabitation, especially young families, who rely on traditional filtering chains that function well. The possibility of demand spillover to the northern or southern governorates or Rafah/Khan Yunis will depend on significantly improved transportation (e.g., liberal use of roads that currently feed Israeli settlements). The key housing issue for this group is sufficient growth of the target markets and filtering capacity of the housing stock to provide affordable rental units.

2.31 *Housing investment priorities and sequencing*. Current construction activity appears to be able to cope with WBG's natural population growth. But an economic upturn, leading to a significant decrease in household size or a larger inflow of returnees, could lead to a renewed acceleration of prices, as witnessed immediately after the Oslo agreements. It is important to manage a housing program in a way that avoids price overshooting (see Situation A in Figure 6). In general, public intervention should avoid over-stimulating demand, linking any subsidy programs with steps that reduce new construction costs and mobilize the significant reserves in the housing stock (rental, accelerated renovations and extensions, etc.).

III. HOUSING SECTOR REFORM AGENDA

A. Reform Priorities

3.1 *Long-term growth strategy*. In the long-term, the central housing policy goal should be new construction. Considering the bias of private investment in favor of real estate in the transfer-dominated economic environment that characterized the past decade, it would appear that a stimulation of growth in the sector is not a priority³⁵. However, we expect that the conclusion of a political agreement would significantly raise the attractiveness of investment alternatives to housing, and at the same time would accelerate the realization of the high latent housing demand. A swift acceleration of prices, more pronounced even than during the first half of the 1990s, could be the consequence -- if distortions that limit the growth capacity of the sector are not addressed. Priority reform areas in order to promote growth are:

- removal of supply constraints that keep new construction costs persistently high, especially in land supply, servicing with infrastructure and construction standards.
- on the demand side, an increase in the availability of finance for consumers and developers.

³⁵ See also the comments of Mayo (1995) on requests for public housing programs along these lines with the goal to pump-prime the sector.

3.2 *Short-term restructuring strategy.* In the short-term, demand pressure should be less pronounced and housing policy should focus on improving the efficiency of use of the stock and its affordability. This has also an important growth perspective, since improved use of the stock reduces the need for new construction. Currently, there are numerous legal, regulatory and taxation impediments to producing a greater share of rental and co-operative units for low-income households. Restructuring the housing stock by enhancing the share of these sub-sectors could enhance also housing supply for young and mobile households significantly. An improved use of public finance is instrumental in that regard; public housing policy has conceptually remained in for-sale developer categories since its inception in the early 1990s. The priority areas for a restructuring are:

- on the supply side, measures to remove the constraints to the development of diversified tenure forms, in particular for rental housing.
- on the demand side, an improved allocation of public resources, which are so far mainly invested into new public housing construction, to households in need of affordable housing; and promotion of low-income housing finance.

B. Agenda

Reducing Housing Costs

3.3 *Land use and urban regulations.* Most of the issues could be addressed either within a local government reform or urban institution-building program with the goal of improving urban regulation and planning instruments. Under the World Bank supported Palestinian Housing Initiative, MoH's work program includes improving the management of public land.

3.4 *Land surveying and property registration.* The World Bank is currently assisting in this area, and the moratorium on registration costs has been an important first step. However, the recent Condominium Law (1998) regulating individual ownership of apartments has an inconsistency in that only a *pro-rata* share of the underlying land, but not the unit itself, is registered.

3.5 *Infrastructure markets.* The Bank has reviewed infrastructure issues and developed a corresponding local government and utility reform agenda (World Bank, 1999).

3.6 *Construction input markets.* Backward linkages need further development, e.g., a new cement factory is needed³⁶. The constraints should ease as import restrictions are lifted in connection with the peace process, and a policy of enhancing competition is developed. Taxation of import duties for housing inputs should be reviewed.

3.7 *Building standards.* A review of building standards and overhaul and streamlining of local regulations, possibly in the form of a new Construction Code, are needed.

³⁶ PECDAR (1997).

Increasing the Availability of Finance

3.8 *Consumer finance.* An important first step has been taken under the Housing Initiative. The project's objective is to develop long-term mortgage lending by commercial banks and provide assistance to low-income households. Low-income housing finance has not developed so far beyond the CHF/USAID pilot project; plans for the creation of a micro-finance institution are being discussed. Consumer finance related legislation issues have been studied,³⁷ but as yet there appears to be no consistent reform agenda.

3.9 *Construction finance.* The development of a long-term finance system, as under the Bank-supported Housing Project, would partially alleviate developers' funding constraints by reducing their need to provide finance to buyers. However, without more steady access to capital for developers, small size and low profitability would remain a problem. Access to financial markets, in particular for those in low-cost housing development, could be supported by various instruments, including bond issues, credit lines, and venture capital. In the short-term, legal reform could improve the financial relations between developers and consumers³⁸.

Improving Stock Efficiency and Tenure Diversification

3.10 *Enabling legislation for the housing sector.* An important step for sector diversification would be to promulgate enabling laws that, similar to the Condominium Law, lay out the legal framework for the entire sub-sector. The two most important are (a) a Rental Housing Act, amending the Civil Code provisions in specific areas such as rent level assessment, rent adjustment, impact of renovations, and creation of a simplified litigation process, etc.; and (b) a modernized version of the old Jordanian legislation on housing co-operatives. Also, an overarching Housing Act might help to determine the principles of public housing operations and define the role of different levels of government in housing policy.

3.11 *Specific civil law reform.* A Rental Housing Act should be supported through a modernized rent section in the Civil Code. The Jordanian law prevailing in the West Bank features overprotection for sitting tenants. Leases are currently indefinite, with highly limited termination options for the landlord. While eviction of a tenant is legally possible, refusal to pay a reasonable rent increase or even non-payment of rent are not eviction grounds. On the other hand, renting provides an alternative to the Islamic interest constraint for the landlord. Short term and rent step-up leases need to be introduced as a concept.

3.12 *Tax reform.* High formal tax rates on property ownership, transfers and income encourage tax evasion and have a negative signaling effect for investors, *even if and although*

³⁷ Present shortcomings include slow land registration, impossibility of registering a second mortgage, absence of consumer bankruptcy legislation, lack of clarity about the ability to evict, and about priority for mortgage claims over other liens. See also IFC (1998).

³⁸ Important consumer protection issues such as rescission, indemnification, etc.. are not addressed in the sales contract. There is also no regulation governing developer finance schemes, and typical contractual features biased against consumers include: land title is given only upon full payment of installments; financing can be called in by developer; if the consumer leaves the contract there is uncertainty over the size of the reimbursement of paid installments (typically 50% up front, very short terms); and, there is no transparency about the costs of the financing.

they are not properly enforced. The funding function of property-related taxation, which is currently highly relevant for both Palestinian Authority (PA) and local governments, should be de-emphasized and the system re-designed with the goal of creating neutrality between tenure forms. At the same time, collection and enforcement should be improved. Rental for-profit housing investment should be treated as other financial or real investments, i.e. allowing for deduction of costs from revenues. Mortgage interest deductibility for homes without computation of imputed rents should be discontinued; here a consumption good approach would be preferable. Co-operative ownership and direct ownership should be treated at the same level. In addition, a future system should avoid double taxation by different levels of government.

Refocusing Public Housing Policy

3.13 *Past PA and donor funded housing programs.* Before the Oslo agreement, there was little development of a public sector strategy to meet housing needs.³⁹ From 1992 on, the first phase of Palestinian Authority (PA) housing policy focussed almost exclusively on public housing construction through the Palestinian Housing Council (PHC), funded by land-to-housing swaps with developers or by donors. From 1994 on, the newly created MoH developed its own projects, acting similarly to PHC as a housing developer.

3.14 *Efficiency issues with past programs.* Even donor-funded housing projects have in the past been executed under high engineering standards and were not geared to the affordability of low- and even middle-income households.⁴⁰ When MoH started its programs, implementation costs were somewhat lower than those of PHC, but the programs still featured some inefficiencies such as subsidized retail sales prices and below market rate retail finance with low recovery ratios. In both cases, the targeting of the subsidies was problematic, as was the amount of subsidies involved: most projects were earmarked for particular groups, e.g., to police and government employees who were not necessarily low-income earners. Projects that were not earmarked were targeted according to waiting lists.

3.15 *Reform of public housing institutions.* MoH has so far not focused on housing policy formulation, including taxation, infrastructure, justice and housing assistance; institutional development is pursued under the Housing Initiative. The Initiative has also proposed a Housing Assistance Fund (HAF) with the goals of introducing cash grant assistance for households with housing needs and providing financial incentives to induce for-sale development. While there is a commitment by MoH and the Ministry of Finance (MoF) to provide PA resources and public land to support this Fund, the disbursement of funds has been delayed. MoH should be converted into a lean policy institution, which implies outsourcing of non-core functions, such as

³⁹ The Palestinian view is that attempts to develop public housing were ‘deliberately obstructed’ (PECDAR, 1998). Beneficiaries declined to move into housing units built by Israel in Gaza, which still stand empty. The infrastructure to support the private housing construction market was also very limited, due to the poor fiscal position of local governments.

⁴⁰ Rabenau (1995, p.1) analyzed EC funded projects administered by the Palestinian Housing Council (PHC) at that time: “The first generation of EC-supported housing units is of a size and quality that makes it impossible to reach low or medium income households while recovering cost.... It is therefore recommended to recover cost to the fullest, and to satisfy the needs of low income households through a second generation of projects.”

project management, land use planning, etc. PHC should be privatized, likely as a pure developer or project manager, along the lines of proposals made by von Rabenau (1995).

C. Housing Program Implications.

3.16 *Efficiency enhancement of public programs.* To make a housing program viable, regardless of the proposed type of program, it is crucial to lower the costs of publicly supported housing solutions and increase cost recovery. The subsidy-per-household ratio would need to be significantly reduced below the levels seen in the 1990s (subsidies under past projects have reached levels of USD 30,000) in order to gain sufficient program reach. Under the financial constraints of a possibly large housing program, benefits would have to remain relatively low, and be carefully targeted towards those in need -- a goal that would be supported with a successful introduction of the HAF.

3.17 *Stimulation of low-cost housing supply.* To render a low-cost housing approach effective, measures to stimulate the supply of low cost units would need to have high priority in the reform agenda. In the area of restructuring, constraints to converting units to low-cost units for market use should be systematically removed; for instance, for converting a unit into (legally formal) rental housing use, a landlord could receive an initial income and property tax break. Similarly, for extensions or for rehabilitating existing buildings, licensing procedures could be simplified or in some cases removed, and property tax could be initially reduced or exempted. For new low-cost projects, the overhaul of the land management system would be pivotal, which would include assessing public land resources, creating priority for land registration of low-cost projects, and improving the planning capacities of local government.

IV. PROGRAM OPTIONS

A. Goals and Design Principles

4.1 *Program goals.* Experience has shown that it is difficult to address competing objectives i.e., mitigating property loss incurred during past conflict phases, providing housing solutions based on need, and stimulating additional housing production where returnees are likely to settle, within a single comprehensive program. Given the size of the Palestinian refugee population relative to residents in many host countries and WBG proper, the loss mitigation goal could create strong competition over resources with the housing policy goals. If all goals were to be addressed through one traditional housing program, competition would emerge over resource allocation. However, excluding the goal of loss mitigation and focusing on a pure housing program could create distortions in key variables of the final settlement process, e.g., in terms of horizontal equity among refugees, or in incentives to return to WBG. A set of separate sub-programs would allow these goals to be addressed individually, while offering a choice for donors' consideration. Below are some principles that could be useful in designing such a set of sub-programs, followed by a description of some possible sub-program features.

4.2 *Design principles.*

- *Incentive neutrality for refugees with regard to the moving decision.* Incentive neutrality is difficult to achieve in practice because of other household decision elements such as income generation. However, a good allocation of program benefits would be one where a particular refugee household's decision to relocate is financially equivalent to the alternatives, i.e., staying in the current location or opting for a new host country. In terms of instruments to minimize perverse incentives, it would be best if general *financial and housing benefits* were paid to the entire refugee population, regardless of their decision to move; whereas, *moving costs* would be paid only to those who actually relocate. Ideally, for the sake of equity and to avoid distortions, a returnee housing program in WBG would be mirrored by similar regional programs, at least in those host countries that currently have limited housing program capacity. For practical purposes, the discussion in this paper focuses on the WBG program elements only; but would also apply to such mirror programs.
- *Consistency with local housing policy.* Individual programs should be as consistent as possible with the local housing sector reform agenda, limiting distortions to the market. A clear separation between subsidy and finance instruments is best, since full cost recovery is the only way to stimulate the additional private capital flows needed to fully fund the program. A relatively low housing subsidy-to-household ratio allows larger program reach and reduced queuing among beneficiaries. Also, for horizontal equity, equivalent housing subsidy treatment between returnees and resident young and overcrowded households in need of low-cost housing is indicated. This implies, *inter alia*, that refugee status would affect prioritization rather than serve as an exclusive eligibility criterion for housing benefits.
- *Efficiency of design and administration.* As mentioned earlier, it is proposed that program elements be designed and administered to pursue a single goal only, e.g. either loss mitigation or housing assistance. Focus on one goal helps to maximize the efficiency of resource use, facilitates cost recovery from beneficiaries (where intended), and makes conflicts over resources explicit. In contrast, programs attempting to reach several goals with one design and administrative body have been typical for historical post-conflict situations. Empirical evidence in these cases indicates that the loss mitigation goal has often been reached only very incompletely⁴¹. In a structure with several independently administered program elements, benefits can also be better targeted by creating a single application flow and a personalized benefit account.

⁴¹ Two case studies of housing finance programs for refugees were reviewed for this paper: Bosnia after the Dayton agreement (Emergency Reconstruction Project), and Germany in the immediate post WW II period (Lastenausgleich). In the initial designs created under the impression of the conflict, the loss mitigation goal in both programs absorbed a large part of financial and administrative resources. In practice, however, the program focus tended to change quickly to reflect more traditional housing policy goals, in particular swift production, benefiting also non-refugee groups. Refugees thus typically ended up being treated in principle as other households with housing needs, and general financial benefits for loss mitigation became nominal.

- *Self-selection of donors.* Sub-programs can be arranged in a way that enables individual donors to (self-) select between distinct uses of funds, and distinct goals, according to their preferences. For instance, some donors may want to support a loss mitigation goal explicitly, while others may wish to limit themselves to housing policy goals. However, it would be beneficial for one office or agency to retain the overall financial co-ordination and administration of the individual programs. Full funding for each individual sub-programs would enhance credibility; and a funding equalization mechanism could be established to deal with major imbalances.

B. Program Features

4.3 The program features presented here follow directly from the design principles. The several independent sub-programs are termed “baskets” to indicate their nature as alternative funding options available to donors. The figure below shows how beneficiaries could feed into the sequence of options.

Basket 1, for example, could address the issue of benefits *based on legal status*, i.e., a grant related to compensation⁴² for property loss or a lump-sum payment, for individuals determined to be eligible. This benefit would be unrelated to their housing needs, or the decision to relocate.

Basket 2 could assist refugees deciding to relocate, by, for example, reimbursing moving costs. It could also provide housing assistance in the destination country; however equity considerations may imply that returnee households would need to fulfil the same general wealth and income limits applicable to all residents.

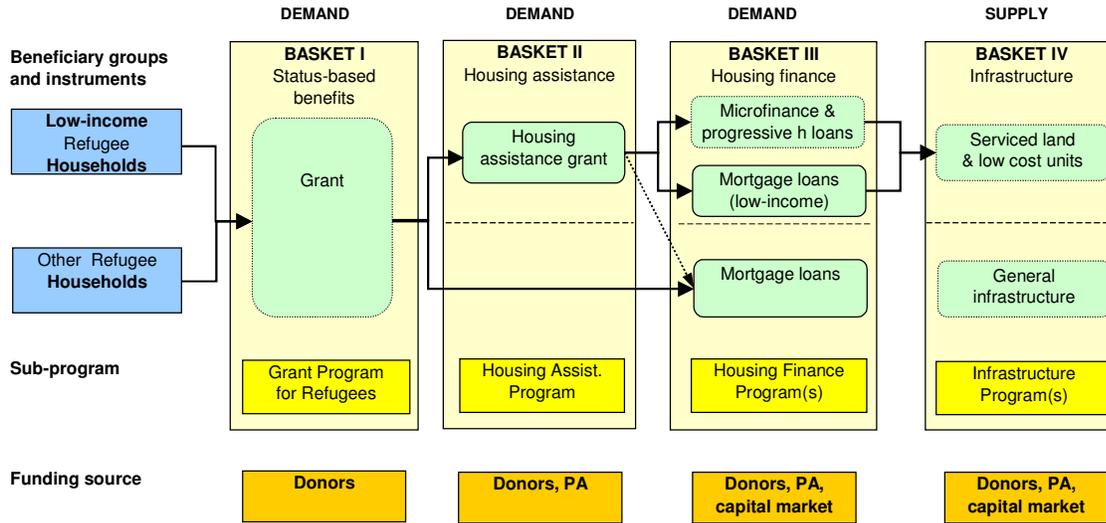
Basket 3 could make available a selection of housing finance programs to enable *all* households in a destination country, regardless of their refugee or housing beneficiary status, to upscale their housing solutions. Finance programs, as distinct from grant assistance programs, are most effective when there is full cost recovery to enhance their funding base. A full range of finance programs can be considered, including short-term and micro-credit programs for those households with a low debt service capacity that cannot be absorbed by the rental market. For housing finance programs, capital market mechanisms could be established that would enhance the range of funding options.

Basket 4 could support the housing demand enhanced by these three sub-programs by stimulating the supply of low-cost units: e.g., through investment in land conversion and development, including infrastructure.

⁴² This paper does not analyze the many complex issues involved in compensation, including, for example, the identification of beneficiaries, the definition of the asset base or the method of computation of individual losses, or alternative loss mitigation mechanisms.

4.4 Some ideas on possible instruments, eligibility, and administration for these various options are outlined in Annex 3. As noted earlier, although they pertain to WBG, the reasoning could be applied in a variety of locations.

Figure 1: Returnee Housing Program Options



Note: dotted lines indicate instruments to be created.

LITERATURE REVIEW AND REFERENCES

Literature Review

A first internationally comparative housing sector analysis was undertaken by Mayo (1995) as part of the WB housing indicator project. The latest currently available housing sector analysis was prepared by the Palestinian Economic Council for Development and Reconstruction (PECDAR) in 1997. A national report in the framework of Habitat II is pending.

Some isolated analyses of the legal and regulatory and financial environment of housing finance have been undertaken; and analysis of first-time buyer intentions and characteristics for the newly founded Palestinian Mortgage and Housing Corporation was undertaken by Massar Associates (1998). PMHC analyzed the legal and tax situation of housing finance in its business plan PMHC (1998).

During the preparation of the Bank sponsored Housing Initiative, consultant reports focussed on feasibility analysis and identification of beneficiaries for housing assistance Duebel (1996). Literature on the housing situation of refugees living in UNRWA camps is relatively plentiful; an example is Waltz and Badaway (1999). Donors of housing projects have commissioned assessments of both the project and the sector environment, e.g., the critical review of a PHC project by von Rabenau (1995).

The sector is excellently described in statistical terms through a population and housing census undertaken by the Palestinian Central Bureau of Statistics in 1997; however, there are gaps in the very recent statistical data. The World Bank (1999) analyzed public infrastructure investment and local government issues, including taxation, and World Bank (2001) analyzes poverty and social development.

World Bank documentation referred to in this paper include the Housing Project Staff Appraisal Report (March, 1997); and the Financial Institutional Development Project (Project Appraisal Document (November, 2001).

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Statistical Annex

Table 1: WBG Population and Palestinian Refugees in 1997

Population 1997	WBG Sub- population		located in ..				Registered outside Palestine		Total Population	
	*1,000	%	*1,000	%	*1,000	%	*1,000	%	*1,000	%
Refugees	1162	40%	496	27%	665	65%	4000	100%	5162	75%
Other	1733	60%	1377	74%	357	35%		0%	1733	25%
TOTAL	2895		1873		1022		4000		6895	
PCBS Forecast 'middle scenario'	WBG Sub- population*		located in ..				Forecast assumptions			
	*1,000	chg p.a.**	*1,000	chg p.a.	*1,000	chg p.a.	Fertility rate	Net immigration *1,000 during		
1997	2783		1761		1022		6.1	500	1997 - 2010	
2010	4938	4.5%	3011	4.2%	1921	5.0%	4.7	0.0	2010 - 2025	
2025	7402	3.6%	4186	3.1%	3054.962	4.0%	3.1			

*excl. Jerusalem ** 1997 - 2010 and 2010 - 2025 respectively

Source: PCBS 1997 Census. Note: West Bank includes Jerusalem. Registered outside Palestine PA estimate.

Table 2: WBG Household Distribution in 1997, and Projections

Households 1997	WBG Sub- population		located in ..				Registered outside Palestine		Total Population	
	*1,000		*1,000		*1,000		*1,000		*1,000	
Persons per hh	6.5		6.2		7.1		7.0		6.8	
Refugees hh's	174		80		94		571		746	
Other hh's	272		222		50		0		272	
TOTAL	447		302		145		571		1018	
Forecast										
Persons per hh										
2010	4.9		4.7		5.3					
2025	3.2		3.1		3.5					
Households	*1,000	chg p.a.	*1,000	chg p.a.	*1,000	chg p.a.	Chg p.a.			
2010	1016	6.5%	648	6.0%	362	7.3%	1997 - 2010			
2025	2284	5.6%	1350	5.0%	864	6.0%	2010 - 2025			

Source: PCBS 1997 Census. Note: Registered outside Palestine own estimate. Own assumptions concerning persons per household, forecast based on PCBS middle population scenario.

Table 3: Benchmark Projection Household Growth in WBG 1997 - 2010

Source of Growth	Impact on household growth	Additional housing demand
Natural population growth	3.5% p.a.	22,500 units p.a.
Net immigration/return (net: 500,000 1997 – 2010)	1% p.a.	6,500 units p.a.
Reduction in household size from 6.5 to 4.9	2% p.a.	13,000 units p.a.
Total:	6.5% p.a.	42,000 units p.a.
Approximate impact of additional 100,000 returnees	~ 0.25-0.3 %	~ 1,600 –1,900 units p.a.

Source: author's estimate based on PCBS, 1997 Census.

Table 4: WBG Key Housing Sector Data, 1997

Key sector data	WBG Sub-population		located in ..				located in ..	
			West Bank*		Gaza		Camps	
HOUSEHOLDS	407	100%	263	100%	144	100%	63	100%
TENURE								
Owners	318	78%	198	75%	120	83%	55	88%
Rental	39	10%	32	12%	7.5	5.2%	2.5	3.9%
Without payment	46	11%	30	12%	15.4	11%	5.0	7.9%
CROWDING								
av. persons/room	2.0		1.9		2.1		2.1	
> 2 persons/room	221	57%	136	52%	85	59%	39	62%
> 3 persons/room	114	28%	74	28%	41	28%	19	30%
Nuclear families	298	76%	194	74%	104	72%	n.a.	n.a.
Extended families	94	24%	57	22%	37	25%	n.a.	n.a.
Units with > 1 HH	13.8	3.5%	5.2	2.0%	8.6	6.5%	4.1	7.2%
QUALITY								
House	203	52%	134	52%	69	52%	40	63%
Apartment	176	45%	114	45%	62	47%	23	36%
Tent or marginal	2.9	0.7%	1.8	0.7%	1.0	0.8%	0.3	0.5%
Water	325	83%	204	79%	122	92%	55	96%
Electricity	369	95%	242	94%	127	95%	56	98%
Public sewage	130	33%	63	24%	67	50%	34	60%
* w/o Jerusalem	critical values							

Source: PCBS, 1997 Census. Note: West Bank excludes Jerusalem. Critical values are the author's assessment.

Table 5: Credit for the Construction Sector in WBG

	1996		1997	1998	1999	2000	
	mln USD	%	mln USD	Mln USD	Mln USD	mln USD	%
Bank Credit for Construction	46.6	11.0%	75.3	104.6	124.0	124.2	9.2%
<i>by purpose</i>							
Building	14.8	3.5%	23.0	27.9	42.6	52.8	3.9%
Public Contracting	29.7	7.0%	48.8	70.6	69.8	60.8	4.5%
Purchase of Buildings & Land	2.1	0.5%	3.5	6.1	11.6	10.7	0.8%
Memorandum Item:							
Total Bank credit	423.8	100.0%	612.9	833.1	1005.5	1346.2	100.0%
Developer credit to consumers	n.a.		n.a.	n.a.	n.a.	250 - 500	

Source: PMA. Note: developer credit author's estimate. Note: data for end of December. Borrower definitions not available.

Table 6: MoH estimate of Gaza New Construction 1994 – 2001 and Vacancies by 2001

Investor	Newly Built Units	Investor Distribution	Vacant Units	Vacancy Rates
Ministry of Housing (MoH)	1,740	23%	475	27%
MoH in cooperation with investors	1,063	14%	185	17%
Palestinian Housing Council (PHC)	922	12%	-	-
Cooperatives and Associations	1,300	17%	70	5%
Private Sector	2,467	33%	484	20%
Total	7,492	100%	1,214	16%
Of which asking price under \$ 30,000 and under 120 sqm (HAF eligibility)			609 (20% private sector)	

Source: Ministry of Housing (2001). Note: stock vacancies n.a.

Table 7: Employment of Palestinians in the Israeli and Domestic Construction Sectors

Item /year	Total employment (1)	Employed in Israel (2)	Construction worker in WBG (3)	Construction workers in Israel (4)	Share of (4) in total employment	Share of (3) in total employment
1970	173.3	20.6	12.8	11.2	6.4%	7.3%
1974	210.4	68.7	8.8	36.1	17.2%	4.2%
1980	215.7	75.1	13.5	35.6	16.5%	6.2%
1986	260.8	94.5	18.9	45.4	17.4%	7.2%
1991	287.4	97.8	19.7	66.88	23.2%	6.8%
1992	319.1	115.6	23	85.92	26.9%	7.2%
1993	315.8	83.8	34.6	60.94	19.2%	10.9%
1994	382	53	....	.....	.....	....
1995	374	32	73.5	.....	.....	19.6%
1996	361	25	40.3	.....	.....	11.2%

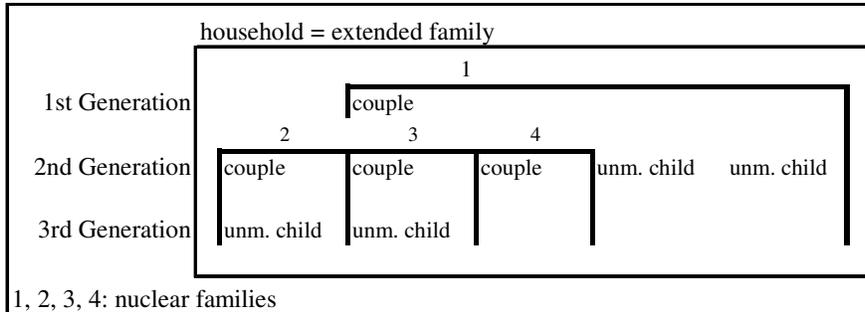
Source: [PECDAR \(1997\)](#). Note: thousands.

Table 8: Macroeconomic Indicators in the West Bank and Gaza, 1995-99

	Unit	1995	1996	1997	1998	1999
Population	Thousands	2,396	2,518	2,628	2,731	2,842
GNP	\$ Millions	3,984	4,070	4,442	4,906	5,255
GDP	\$ Millions	3,484	3,619	3,836	4,078	4,327
Real GNP	Per Capita Index 1994=100	93	88	90	97	101
Real GDP	Per Capita Index 1994=100	93	90	89	92	95
Unemployment	Rate Percent	18.2	21.8	21.5	16.2	11.6
Total Employment	Thousands	428	451	480	540	562
Employment in Israel	Thousands	69	73	77	119	126
Public Employment	Thousands	59	74	82	87	98
Closure Days	Number	57	89	57	14	7

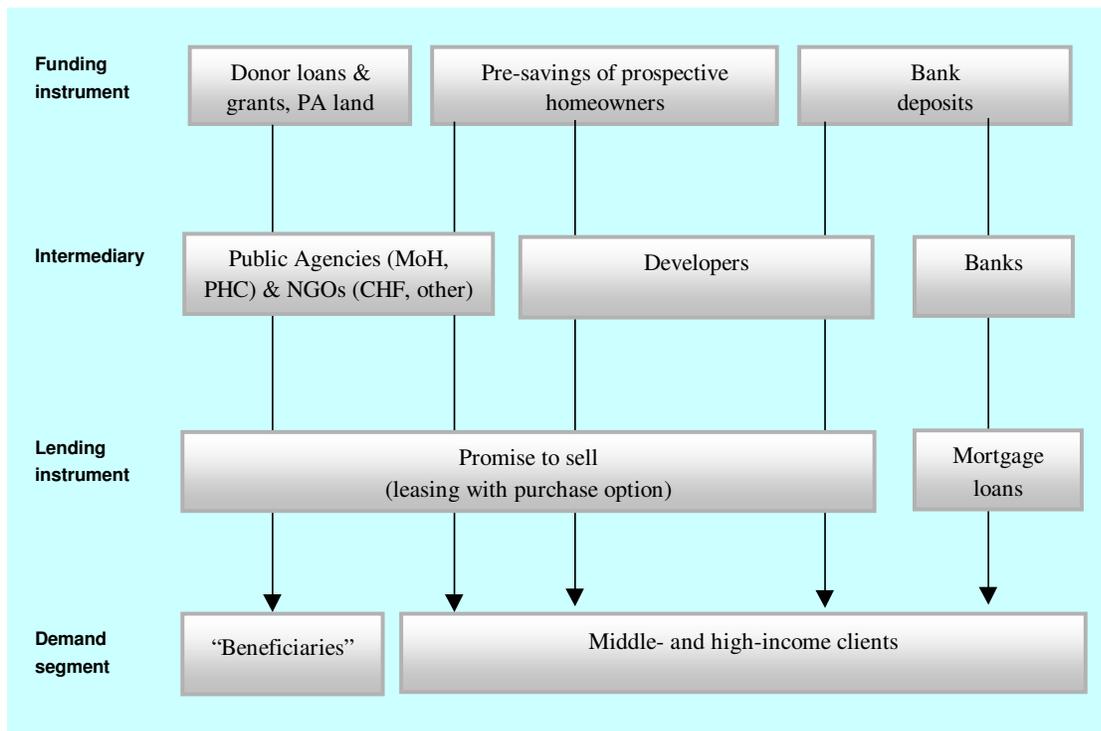
Source: World Bank (2001). Note: Macroeconomic aggregates and population figured do not include East Jerusalem. Population figures are mid-year figures. Employment figures are for the third quarter of each year, except for public employment for which end-year figures are reported.

Figure 1: Cohabitation and Housing Demand: Nuclear vs. Extended Family



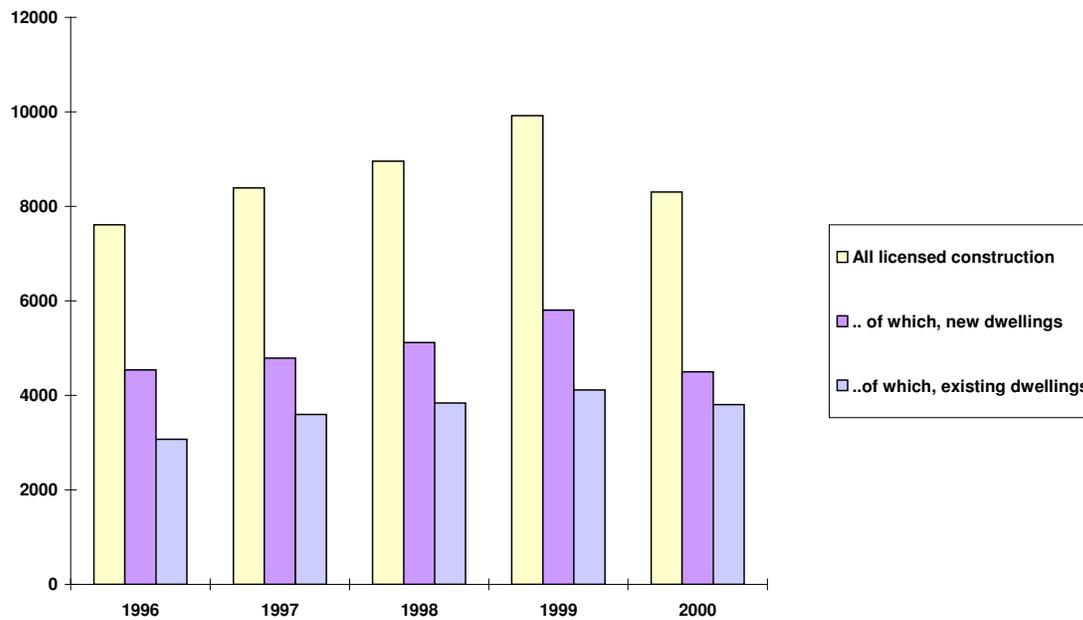
Source: Duebel (1996)

Figure 2: WBG Housing Finance Channels, around 2000



Note: NGO's use short-term loan instruments.

Figure 3: Dwellings Construction Licenses in WBG 1996 – 2000



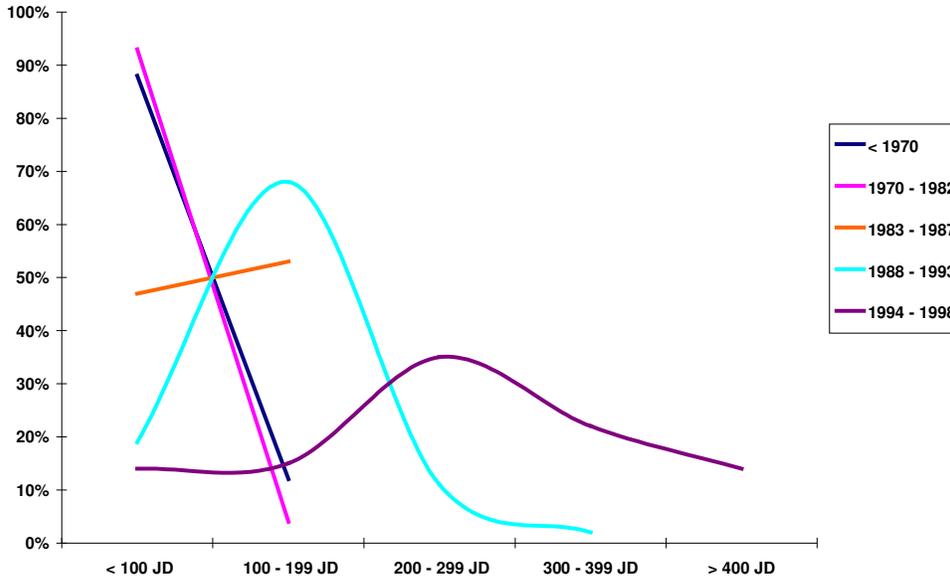
Source: [Palestinian Central Bureau of Statistics](#). Note: av. floor space = aggregate newly licensed sqm divided by number of licenses.

Figure 4: Housing Costs relative to Consumer Prices in WBG, 1996 – 2001, Index 1996 = 100



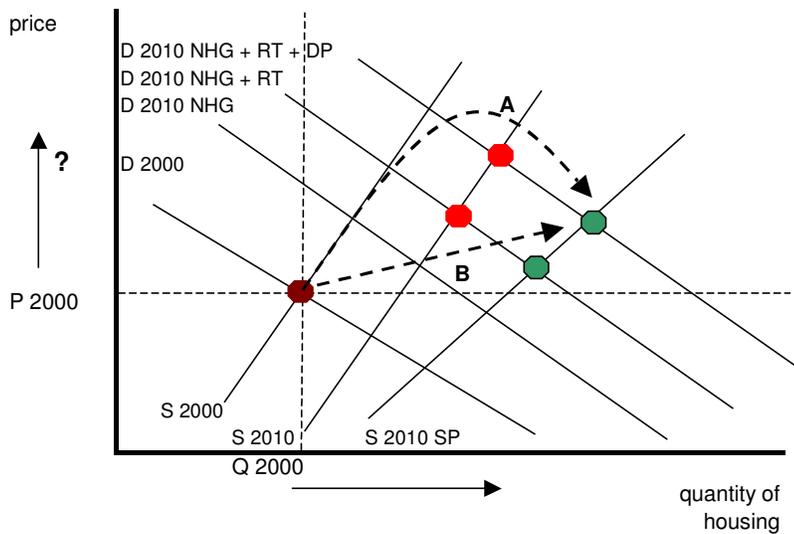
Source: PCBS. Note: Housing costs /CPI: Housing costs index divided by CPI index. Average Q I – Q IV 1996 = 100.

Figure 5: The Impact of Rent Control: 1998 Ramallah Rent Distributions by Length of Tenure



Source: Massar Associates (1998). Note: 506 households interviewed. Some bracket values interpolated, curves smoothed.

Figure 6: Strategic Choice between Demand and Supply Policies under the Impact of Housing



Legend

P: Price, Q: Quantity, S: Supply, D: Demand
NPG: Natural Household Population Growth, RT: Returnee Households,
DP: Demand Program/Housing Finance, SP: Supply Program

Housing Assistance Program Options

A set of four potential separate sub-programs ('baskets') were outlined in Section IV. Separate sub-programs or baskets allow the several objectives of housing-related assistance programs for returnees to be addressed individually, while offering options for donors' consideration. This annex describes some possible features of the various options or sub-programs. These are preliminary ideas, included here to illustrate an approach to addressing the various objectives of assistance programs (loss mitigation, providing relocation and housing assistance based on need, and stimulating housing supply where returnees are likely to settle) within a framework which is consistent with overall housing policy objectives.

Basket I: Grant Program Based on Refugee Status. This paper does not analyze the many complex issues involved in compensation,⁴³ however, for the purposes of this paper, it is assumed that any such program would precede a housing program(s), since receiving a status-based financial benefit could affect eligibility for housing benefits. Ideally, adjudication of claims and disbursement would be fast, to allow the grant to become part of a down-payment for a house. From this perspective, a simple loss mitigation mechanism, e.g. a lump-sum payment, would be preferable.

- *Eligibility:* entitlement for Palestinians with the appropriate legal status, irrespective of whether located in WBG, Israel or host countries.
- *Instrument:* Assumed to be grant. Instrument design open, follows peace settlement.
- *Administration:* It is assumed here that refugee-status based benefits, as well as relocation costs, would be directly managed by a regional agency in charge of implementing the peace agreement and dealing with refugee affairs.

Basket II: Housing Assistance Program. Direct, transparent and equitable housing assistance grants are a flexible instrument of housing policy. They allow a more efficient distribution of subsidies than public soft loans or public rental housing, which tend to mix finance and subsidies, crowd out the private sector, and are often poorly targeted. The goal here would be to develop an instrument that could support the housing demand of both returnees and resident households with housing needs within a single conceptual and administrative framework.

- *Eligibility:* The assumption is that housing assistance would be an entitlement for all households with housing needs; with returnees who do not fulfill eligibility limits not receiving assistance. However, in a scoring system introduced to determine priority, returnees could receive additional points. Such a scoring system could, for example,

⁴³ Including, for example, the identification of beneficiaries, the definition of the asset base or the method of computation of individual losses, or alternative loss mitigation mechanisms.

assign higher scores to socially vulnerable, or high priority ‘emergency’, returnees. Maintaining a central ‘housing beneficiary data base’ would help to prevent “double-dipping” for subsidies, e.g. with other MoH programs or land allocations.

- *Instrument:* Grants could be in the form of personalized multiple-use vouchers. These could be cashed in as a down-payment for a house purchase or as interest buy-downs for loans. In the WBG housing situation, another relevant use would be rent allowance. The level of assistance could be determined, for example, by a fairly basic housing solution affordable in many locations of the destination countries, allowing returnees to choose among a – limited - range of solutions in the housing market. Eligible housing costs, either rental or debt service, as well as absolute levels of assistance could be capped, enforcing a scaling down of housing consumption levels and stimulation of supply in the low-cost market segment. Capping housing costs can also help to reduce the error of unintentionally including high income households. Interest buy-downs and rent allowances could be subjected to a time limit and eligibility be reviewed periodically. Benefits for vulnerable or emergency households might be enhanced, e.g. seniority allowances.
- *Administration:* Housing assistance vouchers could be issued by a public agency in charge of implementing low-income housing policy. The Housing Assistance Fund currently under implementation has been allocated to the Ministry of Housing; however, assigning the Fund to a special low-income housing agency could be an alternative⁴⁴. The regional agency in charge of refugee affairs could channel the housing assistance subsidies earmarked by donors, and be responsible for minimizing time lags between disbursement of status-based grants, relocation decision and disbursement of housing assistance grants. As a result of its global financial responsibility for individual refugees it could, through program agreement, monitor the housing assistance allocation process and individual allocation decisions, if violating the agreement. As permanent budgetary mechanisms are put in place to supplant donor commitment after a defined initial period, those special rights would be weakened and finally terminated.

Basket III: Housing Finance Program(s). Since the assistance grant is not likely to fully bridge the gap between household resources and housing costs, and only low-income households would receive such assistance under a grant sub-program, the demand for housing by refugees would need to be enhanced by housing finance. Providing equity or bond finance for a housing lender can be a very effective way for donors to leverage their support. Different designs for funding and risk sharing could be tailored to individual preferences. In WBG, a mortgage finance system

⁴⁴ A new agency could be a response to the weakness of current housing policy institutions in WBG, which can support the individual functions of a low-income program, but cannot cover the entire agenda, and would require extensive institutional development and changes in mandate. A new agency’s governance would need to send a strong signal of competence: for example, operations could be run initially under a management contract with one, or a group of, foreign low-income housing policy or finance agencies (e.g., operating in the US or Europe, ideally with simultaneous operations in developing countries). The additional costs of professional management could be recovered through enhanced program efficiency.

built around the wholesale lender PMHC has been designed along this lines. While it is primarily expected to fund property values over US\$ 30,000 with long-term loans; a second window for loans below this threshold has been conceptualized and could be used for those beneficiaries of housing assistance who have the capacity to service a loan for a modest, but still mortgageable unit. However, for many -- or even most -- returnees, the purchase of such a unit is still not likely to be affordable, or they may be unable to fulfill minimum underwriting standards. They may however, with the assistance amounts they received, be able to service smaller capital amounts spent to modernize or expand existing units, or acquire a core housing unit that can be gradually expanded. A micro-finance loan program could target this “progressive” housing market and complement the mortgage finance market.

- *Eligibility:* Since very limited or no subsidy is conveyed through programs run under market conditions, eligibility would not be an issue. Programs could be open to all WBG residents, not only returnees. Beneficiaries could self-select according to the capital amounts they are both willing and able to service, and the type of investment they choose.
- *Instrument.* PMHC could either activate its low-income window or lower underwriting thresholds for its standard program within tolerable limits. For those fulfilling some, but not all *minimum* underwriting conditions (e.g., mortgageable housing unit, but volatile income situation), a special window of PMHC’s mortgage insurance program could be created. For a micro-finance program, loan instruments would be of small volume, and initially short-term, in order to maximize program reach and limit default risk. As the CHF experience with these kind of instruments over the past six years has shown, commercial banks in WBG can reliably service such a portfolio and will gradually be willing to increase their funding and risk exposure.
- *Institution:* A finance basket would need to be clearly financially and institutionally separated from the assistance basket, in order to avoid confusion by beneficiaries between grants and loans. PMHC exists as such a separate institution. For the micro-finance program a new financial institution could be created that could ‘scale up’ the successful USAID/CHF’s modernization loan program in Gaza through expansion to the West Bank. Such an institution would have little or no overlap with PMHC, for which it could provide origination and servicing functions. Both institutions could manage relations to the Housing Assistance Fund through a master agreement which could include data sharing.

Basket IV: Infrastructure and Core Housing Program(s). A fourth basket could have the primary purpose of stimulating the supply of low-cost housing units. In a first approach, donor funds could be used to finance the provision of feeder infrastructure in water, sewerage, electricity and roads by local governments and utility companies “on demand”. Households could either buy core units from developers or build themselves. Investments in power and water generation, sewerage or related trunk infrastructure could be provided under ongoing general sector programs. Cost-based pricing for land servicing through the intermediary, and separated from the market-based pricing of the raw land in order to avoid luring excess demand

from returnees into certain locations, would be appropriate in this case. In a second approach, financial incentives could be linked to a cap on the unit costs of entire finished housing developments provided by private developers, again allowing for flexibility in land pricing. Instruments to reduce supply costs in either case could include the organization of sufficiently large tenders, provision of development or infrastructure loans, or provisions of guarantees to protect buyers and sellers from certain price and marketability risks. The creation of social (rental) housing stock could be considered, for example, for very vulnerable groups; and in this case, tenure rights could be bought in low-cost (seasoned) stock from private investors.