

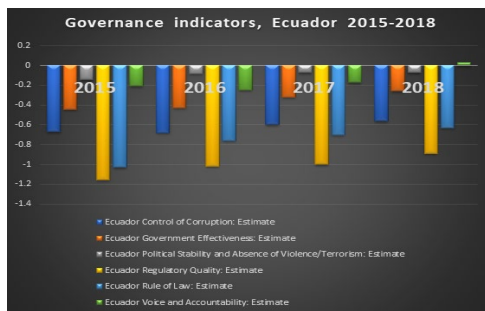
# Building capacity to strengthen access to housing microfinance in Ecuador – COAC Jardín Azuayo

## 1. DEVELOPMENT RELEVANCE

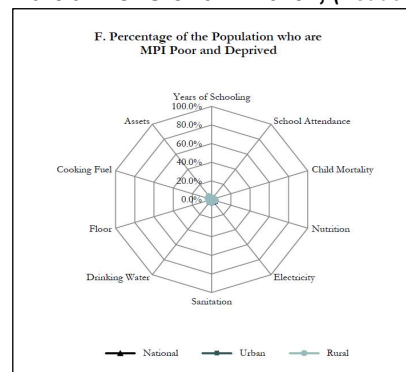
Ecuador has the 8<sup>th</sup> largest economy in Latin America, but the economy has been driven by the country’s oil resources. To promote increased stability, Ecuador has launched a radical transformation of the economy. In March 2019, Ecuadorean microfinance institutions (MFIs) entered into an agreement with the Ecuador government for a 3-year “Prosperity Plan”, which would inject USD 10B in support for the economy, between 2018 and 2021. On October 1, 2019, the president announced a set of economic measures as part of a deal with the International Monetary Fund (IMF). The measures included termination of fuel subsidies, removal of some import tariffs and cuts in public workers’ remuneration. The measures provoked a series of demonstrations and riots from unions opposing the government’s approach. Protests ceased after a compromise agreement, which launched a broader dialogue on tackling the public debt.

Table 1 <sup>1</sup> : Population and economic indicators	
Population in million (2019) <sup>2</sup>	17.3M
GDP growth (2018) <sup>3</sup>	1.4%
Inflation (2018) <sup>4</sup>	-0.224%
Trade balance (% of GDP) (2018) <sup>5</sup>	-0.227%
Foreign direct investment (net) (% of GDP) (2018) <sup>6</sup>	1.299%
Net ODA received (% of GNI) (2017) <sup>7</sup>	0.199%
Remittances received (% of GDP) (2018) <sup>8</sup>	2.804%
Economic Freedom Index <sup>9</sup> (Rank among 186 countries) (2019) <sup>10</sup>	170
Poverty indicators	
GDP per capita (USD) (2018) <sup>11</sup>	6,344.9
Gini Index (0= equality 100= inequality) (2017) <sup>12</sup>	44.7
International poverty rate (2017; at 1.90 USD/day) <sup>13</sup>	3.2%
National poverty rate (2018) <sup>14</sup>	23.2%
National rural poverty headcount rate (2014) <sup>15</sup>	35.3%
Multidimensional Poverty Index	0.013

Governance indicators chart<sup>16</sup>, (Ecuador, 2018)<sup>17</sup>



Multidimensional Chart<sup>18</sup>, (Ecuador, 2018)<sup>19</sup>



## Financial sector

As of September 2019, the private Ecuadorian financial system (without non-governmental organizations - NGOs) holds a total of USD 56B of assets, USD 49B of liabilities and USD 6B of patrimony. In 2018-19, the gross portfolio of the financial system registered an annual growth of 11%. The Ecuador Superintendent of Banks supervises 24 banks, 4 mutual banks and 151 cooperatives. The microloan portfolio is USD 5.6b; banks

<sup>2</sup> INEC, Ecuador, Proyección de Población por Años en Edades Simples, 2010-2020. <https://www.ecuadorencifras.gob.ec/proyecciones-poblacionales/>

<sup>3</sup> World Bank, Ecuador GDP growth: <http://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG>

<sup>4</sup> World Bank, Ecuador Inflation. Inflation: <http://data.worldbank.org/indicator/FP.CPI.TOTL.ZG>

<sup>5</sup> World Bank, Ecuador Trade balance: <https://data.worldbank.org/indicator/NE.RSB.GNFS.ZS?end=2018&locations=EC&start=2010>

<sup>6</sup> World Bank, Ecuador Foreign direct investment (net): <https://data.worldbank.org/indicator/BX.KLT.DINV.WD.GD.ZS?end=2018&locations=EC&start=2010>

<sup>7</sup> World Bank, Ecuador Net ODA received: <https://data.worldbank.org/indicator/DT.ODA.ODAT.GN.ZS?end=2017&locations=EC&start=2013>

<sup>8</sup> World Bank, Ecuador Remittances received: <https://data.worldbank.org/indicator/BX.TRF.PWKR.DT.GD.ZS?end=2018&locations=EC&start=2010>

<sup>9</sup> Heritage.org, Ecuador Economic Freedom Index: <https://www.heritage.org/index/explore?view=by-region-country-year>

<sup>10</sup> World Bank, Ecuador GDP per capita: <https://data.worldbank.org/indicator/NY.GDP.PCAP.CD?end=2018&locations=EC&start=2010>

<sup>11</sup> World Bank, Ecuador Gini Index: <https://data.worldbank.org/indicator/SI.POV.GINI?end=2017&locations=EC&start=2010>

<sup>12</sup> World Bank, Ecuador International poverty rate: <https://data.worldbank.org/indicator/SI.POV.DDAY?end=2017&locations=EC&start=2010>

<sup>13</sup> World Bank, Ecuador National poverty rate: <https://data.worldbank.org/indicator/SI.POV.NAHC?end=2018&locations=EC&start=2010>

<sup>14</sup> World Bank, Ecuador National poverty rate: <https://data.worldbank.org/indicator/SI.POV.RUHC?end=2015&locations=EC&start=2010>

<sup>15</sup> Data from database: Worldwide Governance Indicators, Last Updated: 11/07/2019. <https://datatank.worldbank.org/reports.aspx?source=Worldwide-Governance-Indicators#>

<sup>16</sup> Data from database: Worldwide Governance Indicators, Last Updated: 11/07/2019. <https://datatank.worldbank.org/reports.aspx?source=Worldwide-Governance-Indicators#>

represent 74% of this sector, followed by cooperatives (24%). There is limited participation from other types of financial institutions (2%).<sup>20</sup>

### Summary of Ecuador's performance<sup>21</sup>

Ecuador does not have a financial inclusion strategy, an official working committee, nor organisations in the private and social sectors advocating for a national focus on financial inclusion. Non-banking financial institutions serve low-income populations, but a moratorium on creating new savings and loan cooperatives has been in place since 2015 due to concerns about solvency of some institutions. In June 2019, the Central Bank announced joint efforts with the World Bank on a year-long technical assistance programme to create and implement a national financial inclusion strategy. For example, new regulations that will allow banks to offer mobile wallets are expected in 2020.

Category	Score	Rank	Average score
Overall score	53	=26	52
1 Government and policy support	45	34	54
2 Stability and integrity	58	=36	65
3 Products and outlets	60	=22	57
4 Consumer protection	72	=19	60
5 Infrastructure	67	=17	59

Ecuador: strengths		Ecuador: areas for improvement	
Indicator	Rank	Indicator	Rank
3.1 Accounts at financial institutions and e-money	=1	3.4 Inclusive insurance	=25
2.3 Customer due diligence	=1	3.3 Emerging services	=31
3.2 Credit portfolios for middle- and low-income customers	=1	2.4 Supervisory capacity	49

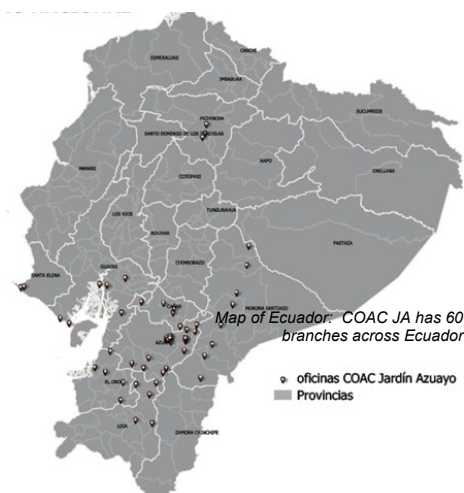
## Housing

Ecuador has the 4<sup>th</sup> largest housing deficit in Latin America. More than 1.7M houses are considered inadequate (unsafe conditions, inadequate construction materials, lack of basic sanitary services, overcrowding, etc.). The government funding programmes for housing do not address access for the low-income population. Ecuador's financial regulation establishes an interest rate cap for all mortgage housing products at 11%, with requirements and guarantees that exclude the low-income families. Because of the limitations around mortgage products, MFIs, cooperatives and NGOs, who typically serve low-income households, design their housing finance products for incremental construction. The construction industry declined last year due to slowdown in the issuance of housing loans and an increase in unemployment. The government took a key step in January 2020 by enabling banks to place credit in housing credits and mortgages at a rate of 4.99% and with a 5% entry. A social bond of USD 400M was issued to form a trust, which will allow financial institutions to place loans for some 24,000 homes in this segment<sup>17</sup>; however, only traditional banks can participate.

## Partner financial institution

The financial institution partner for this project is COAC Jardín Azuayo (COAC JA). COAC JA was founded in 1996 as a small initiative to support reconstruction of the local community in Paute, following a natural disaster. COAC JA is a regulated cooperative and its mission is to contribute to the socio-economic growth of its members by providing financial services in an inclusive and sustainable manner. The cooperative enjoys excellent brand and social recognition with almost 516,000 members through their network of 60 branches. Due to regulatory requirements, the cooperative categorizes and monitors the loans based on the source of payments and not based on purpose of the loans. Typical client/income profiles of COAC JA's are as follows:

- Microenterprise clients: USD 400-500;
- Formal sector employees: USD 600-700.
- Housing clients: USD 1,500-3,500.



With a gross loan portfolio (GLP) of US\$782M, COAC JA is the 2nd largest cooperative in Ecuador and ranks fourth among MFIs in the country. As a cooperative, COAC JA members are also the owners (as of December 2019, COAC JA has approx. 329,000 active depositors and 107,000 borrowers). COAC JA primarily lends individually with 45% female borrowers and 73% of clients from rural areas. The housing portfolio represents 39% of total GLP (USD 303M) with 37,000 active housing microfinance (HMF) loans and an excellent portfolio at risk over 30 days (PAR30) of 2.2%. The housing loans are distributed across the following categories: 40% home improvements, 30% small construction, 20% full construction, 10% land purchase / tenure.

<sup>20</sup> [https://content.centerforfinancialinclusion.org/wp-content/uploads/sites/2/2019/10/EIU\\_Microscope\\_2019.pdf](https://content.centerforfinancialinclusion.org/wp-content/uploads/sites/2/2019/10/EIU_Microscope_2019.pdf)

<sup>21</sup> [https://content.centerforfinancialinclusion.org/wp-content/uploads/sites/2/2019/10/EIU\\_Microscope\\_2019.pdf](https://content.centerforfinancialinclusion.org/wp-content/uploads/sites/2/2019/10/EIU_Microscope_2019.pdf)

## 2. INTERVENTION APPROACH

COAC JA has been covering housing finance needs primarily for improvements, expansions, and remodelling, and to a lesser extent for land, house purchase and full construction. Most of this was done through its traditional financial products: unsecured, short-term, and high interest rate loans. However, as of November 2017, COAC JA launched a new real estate loan product, intended for purchase of land or a house, with a term of up to 20 years, lower interest rates and guaranteed with a mortgage.

The institutional technical assistance provided by Habitat's TCIS<sup>22</sup> focused on improving the housing product portfolio with a specific focus on the micro-mortgage segment. The first activity carried out was a study on the housing needs across the COAC JA's members/clients. The study revealed an important barrier: the COAC clients often owned a piece of land but lacked affordable financial resources to build their house. As a result of the finding, Habitat's TCIS and the Frankfurt School worked together on designing a product prototype to fulfil this need and sit in between the current product offer: a "micro-mortgage". The new product presented attractive conditions: up to USD 40,000 for up to 15 years and a competitive yet affordable interest rate of 9%. With a CONAFIPS<sup>23</sup> funding commitment, the strategic decision was made to move forward with the product, and a pilot was launched across several branches nationwide.

Shortly after the product was launched, CONAFIPS announced important changes in their funding policies and regulations, which affects availability of funds for housing. Additionally, the economy of Ecuador worsened in December 2018 due to the political situation, causing high uncertainty in public-sector employees. As a result, demand for the micro-mortgage product decreased. CONAFIPS suspended the US\$20 million credit line for housing, which was previously approved and committed for scaling-up of the micro-mortgage product<sup>24</sup>. For these events, in February 2019, COAC JA announced the official suspension of its micro-mortgage product. However, it continues with its traditional housing microfinance product. COAC JA is still analysing other potential sources of funding for the micro-mortgage product; however, due to Ecuador's current political environment, the resources are very limited and restricted to specific activities and geographies within the country. Despite the above constraints, the SCBF project was successful in creating an attractive new product (disbursed 41 mortgages / USD 1.3M), and COAC JA is keen to continue providing it once additional investment capital is available.

The following activities were implemented:

Activities	Outputs
1. <u>Diagnosis and Market Study of Existing Housing Products</u>	Habitat's TCIS with the Frankfurt School analysed COAC JA's existing housing products and client segmentation to identify key market gaps and opportunities - e.g. target population, local regulation, and potential construction partners for the new / adjusted housing product "micro-mortgage".
2. <u>Product Design and Pilot</u>	We designed a micro-mortgage product, and the pilot was launched in 2018. 41 micro-mortgages were approved with disbursements accounting for US\$1.3M (USD 31K average loan size). Other planned related activities provided by Habitat's TCIS included: commercial strategy, communications strategy, adjustments to the credit system, policies, and procedures.
3. <u>Capacity Building</u>	As of December 2019, 60 members of the sales force received training on delivery of the micro-mortgage product. Additional capacity will be produced via four training officers who will be sharing the knowledge in the future (training of trainers).

## 3. RESULTS ACHIEVED AND NOT ACHIEVED

**As of December 2019, COAC JA micro-mortgage product achieved disbursements of 41 micro-mortgages across 19 branches, reaching a total placement of US\$1.3 Million (average loan of US\$31,000).** Despite the suspension of the micro-mortgage product and the uncertainty to its reactivation, the **Housing Microfinance Product continues to be successfully placed nationwide. As of December 2019, 22,745 housing microfinance loans were placed, exceeding targets by 20,745. (reaching 10x the initial target was 2,000 housing microfinance loans in the first 24 months), reaching a total among of USD 2B. COAC JA received a US\$3 million loan from MicroBuild Fund to strengthen its housing microfinance product. Currently, the capital is mobilized through their own funding.**

<sup>22</sup> TCIS – „Terwilliger Center for Innovation in Shelter“ is Habitat for Humanity's arm for financial inclusion / market development. <https://www.habitat.org/impact/our-work/terwilliger-center-innovation-in-shelter>

<sup>23</sup> CONAFIPS - National Corporation of Popular and Solidarity Financial, the local fund provider for housing loans.

<sup>24</sup> The funding line to cover housing demand would only be restricted to cover geographical areas associated with earthquake areas in the coastal zone and COAC JA has no operations in these areas

## Client level

According to the onsite monitoring carried out by the cooperative and the Terwilliger Center, the COAC JA members who obtained this product have managed to build homes. These are now in a habitable state, with most of them having practically completed their houses. COAC JA and the Terwilliger Center visited clients from the Sigsig, Chontaleg and Troncal branches. For the most part, the houses have a good construction quality derived from technical supervision provided by professionals. The clients expressed gratitude to COAC JA and appreciated efficient process and agility in disbursements. Additionally, they appreciated additional construction technical assistance by the cooperative staff, who guided them in the process of obtaining building permits in municipalities.



The family **Pesantez Illescas** - Raúl Santiago Pesantez Alemán, 28 years old, private company employee, and his wife Amanda and their son. They owned a piece of land in Parroquia, but unfortunately, they haven't been able to save enough to build their house. Raul, being a member of COAC JA, learnt that he could apply for a loan to build a house for his family. COAC JA approved a \$30,930 loan in February 2019 with a 9% annual interest rate and a 15-year term. When asked about the experience, he replied:

*"We were waiting for years to have access to a construction loan and build our house in our land. I used to visit COAC Jardin Azuayo's office to see if there was any option that could solve my situation but there was not one. Suddenly, I got a call from them to tell me there was a new product available for me to build my house. My wife and I talked, and we decided to take the loan without hesitation. We were a part of this cooperative for many years and we thought it was a great opportunity. The process was pretty easy, and I was helped by the cooperative to fill the necessary documents and to coordinate with the local municipality (construction plans and permits). We hope the cooperative will also help other members like us", said Raul.*

## Level of financial institution partnership

Before this project, COAC JA offered housing solutions to members to improve their houses (housing microfinance products), targeting families with incomes up to USD 800, and offered a loan to finance a full house, targeting families earning between USD 1,500 and 2,500.

Number of active borrowers	37,165
Thereof, number of active women borrowers	16,724
Thereof, number of active borrowers living in rural areas	27,130
Total number of loans disbursed	41 micro-mortgages 22,745 HMF loans
Total value of loans disbursed (in Local Currency or USD, please specify)	\$1,3 M micro-mortgages \$201.5 M HMF loans
Average loan size (in Local Currency or USD, please specify)	\$31,000 micro-mortgages \$7,700 HMF loans
Portfolio Quality (PAR 30)	2.20%
Total number of clients with payments due for over 30 days	n/a
Retention Rate	n/a
Number of clients trained in financial literacy and/or trained on SCBF-supported product	60 staff trained

OSS	109.9%
ROA	0.95
ROE	6.72
PAR 30	3.34%
PAR 30	2.2%
Average standing loan amount	US\$6342
Borrowers p/officer	670

The study conducted by the Terwilliger Center, in partnership with the Frankfurt School, discovered that nearly 35% of COAC JA's client base earns USD 500-1,500, own land, but lacked adequate financial resources for construction of their house. This population was requiring a specific housing product with

financial conditions, requirements, and basic guidance, which has not been provided previously by COAC JA, and almost impossible or very difficult to be accessed by the families through banks. Therefore, a "micro-mortgage" product was designed with this market segments' needs in mind. COAC JA had planned to allocate their own funds and had negotiated USD 20M from a local government source (CONAFIPS) to fund a pilot and further scale up. Unfortunately, CONAFIPS suspended the funding line for COAC JA, so the micro-mortgage product was frozen until new sources of adequate funding can be identified.

## Financial Sector Level

Potential demand for this housing product has been recognized by other stakeholders. There is potential, especially in the rural market to place this type of product. The problem lies in the sources of adequate funding required by the product and this population. COAC JA has initiated conversations both at the local level and with a few external sources, however, funding for this housing product has not yet been achieved. COAC JA internal resources come from its members short and midterm savings, and liquidity and other risk management requirements limit use of this type of funding for long-term lending. COAC JA requires leverage from other financial actors to scale up the product.

The social bond for US\$400M was issued to form a trust, which also has fiscal, which will allow financial institutions to place loans for some 24,000 houses of this segment, could alleviate the need. However, only banks could participate in this program, leaving out cooperatives and other types of financial institutions.

SCBF supported the technical assistance provided by Habitat's TCIS to COAC JA, initiated in February 2018 and concluded in December 2019. There were delays mainly due to the elaboration of its 2020-2023 strategic plan and adjustments to the Information System to track credit (initially short-term credit with monitoring and supervision and subsequently converted into a micro-mortgage once the home is finished). The total project expenses reached USD 111,565.68, of which SCBF contributed 70%, COAC JA 9% of own funds and Habitat for Humanity (from the Hilti Foundation) 21%.

## 4. LESSONS LEARNED

The following lessons learned were identified:

- Micro-mortgages (from USD 15,000 to 40,000), have proven to be needed and accepted among the COAC-JA's specific target population.
- COAC-JAs Research and Development Department Team designed a methodology to guide clients and to follow-up/monitor/supervise micro-mortgages.

### Critical challenges

There is no doubt that the critical challenge COAC-JA is facing is to identify funding sources with appropriate conditions. The survival of the micro-mortgages will depend on the availability of these funding conditions. It is noteworthy that COAC-JA has enough funding (own and external) to maintain the HMF placement as usual (term: up to 7 years and amounts up to USD 15,000 with no mortgage).

### Positive changes:

- COAC-JA developed an internal tool to verify the use of the micro-mortgage loan; this mitigates the possibility for diversion and validates the quality of the construction.
- COAC-JA Research and Development Department Team and sales force owned the follow-up process for the micro-mortgage by conducting a supervision and inspection of the disbursed micro-mortgage cases, proving a) construction progress, b) client's level of satisfaction.

### Critical success factors were:

- COAC-JA commitment: investing resources during the product design stage, capital investment, building capacities within sales force, systems adjusted and launched at a national level.
- Willingness to launch a housing product at national level with a different methodology and requirements (constructions permits, plans/budget of the construction, field follow-up/supervisions, loan use, validation of construction completion).
- Development of a validation process to supervise the loan usage.
- Despite having stopped the micro-mortgage placement, COAC-JA honoured the promise of the approved loans.
- Promotion strategy incorporated:
  - a. Lists of potential demand distributed to branches.
  - b. Communication strategy via activation by "word of mouth".
  - c. Promoted the product within clients from other products with housing constructions needs.

