



**The FLISP Lower-Gap Serviced Site
Subsidy - Issues and Approaches**

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The Urban Real Estate Research Unit

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Abbreviations

BNG	Breaking New Ground Subsidy Programme
CAHF	Centre for Affordable Housing Finance
CAHF	Centre for Affordable Housing Finance
CBO	Community Based Organisation
CIDB	Construction Industry Development Board
DAG	Development Action Group
FLISP	Finance Linked Individual Subsidy Programme
FNB	First National Bank
HMF	Housing Micro Finance
IRDP	Integrated Residential Development Programme
NGO	Non-Governmental Organisation
NHBRC	National Home Builders Registration Council
NHFC	National Housing Finance Corporation
NIMBY	Not in My Back Yard
PHP	Peoples' Housing Process
PGWC	Provincial Government: Western Cape
RCC	Rates Clearance Certificate
RHLF	Rural Housing Loan Fund
UISP	Upgrading of Informal Settlements Subsidy Programme
USDG	Urban Services Development Grant

Executive Summary

One of the main challenges to addressing the current housing backlog in the Western Cape is the inability to supply housing products that are affordable to most of the population. This affordability problem is largely driven by the high cost of housing and the inability of households to afford the upfront payment of housing. An incremental approach could, however, overcome some of these drivers. As a result, this report investigates why there has been a limited roll-out of FLISP-related incremental housing policies despite the perceived benefits thereof. The policies allow the provision of free serviced sites to households in the lower gap housing market which qualify to receive the sites in lieu of FLISP mortgage deposit subsidies.

The report finds that there are both supply-side and demand-side issues undermining the successful roll-out and take-up of this programme and therefore any proposed housing delivery system will need to be designed in a manner that addresses them. The main supply-side constraints include the limited land supply, high product standards, finance costs and availability, contractor capabilities, infrastructure constraints and the lack of household technical support. The demand-side constraints include community and consumer resistance, the inability of households to raise affordable finance, and the limited quantum of the subsidy amount.

As a result, the report proposes two broad housing delivery models, namely, “The new serviced site property owner takes the lead” and “Contractor builds starter and complete houses”. Both models rely on the state drawing on the National Housing Programme: Integrated Residential Development Programme (IRDP) to take a strong lead in the supply and delivery of serviced sites. In the first model, the households are primarily responsible for the construction of the housing top-structures, whereas in the second model, this is the responsibility of contractors.

Regardless of the option chosen, a number of policy amendments should be considered, including:

- Providing land for FLISP lower-gap market housing at no/nominal cost; and applying the government’s fee structure and VAT provisions applied to BNG projects to FLISP lower-gap properties/projects;
- Increasing the subsidy allocated to beneficiaries of the serviced site option by up to R60,000.
- Formulating a FLISP lower-gap market housing policy which includes specifications regarding the contractor built starter housing options supported by the subsidy programme, which can be sold to serviced site beneficiaries at prices discounted at the value of the serviced site subsidy; and
- Reviewing of the income ceiling of the lower-gap serviced site subsidy.

1. Introduction

From 2017 to 2018, the Urban Real Estate Research Unit (URERU) undertook research into the micro-developer housing market in township areas in Cape Town. From this research, it emerged that opportunities may exist for greater incremental development on vacant sites in lower-income areas that are targeted at the lower-gap market (households with monthly incomes between R3,501–R7,000). The focus on the lower-gap market is important as these households do not qualify for Breaking New Ground (BNG)/RDP houses and as they also struggle to access mortgages, they often are unable to access state subsidies associated with mortgage products.

In 2012, the Finance-Linked Individual Subsidy Programme (FLISP) was amended as follows (Hoek-Smit, M. and Cirolia, L. (2016):

- Set household income qualification at R3,501-R15,000 per month;
- Established a maximum house-price of R300,000 (removed subsequently);
- Allowed both newly constructed houses and resale houses to be included;
- Increased the maximum subsidy for the lowest income segment to R87,000;
- Removed the savings/down-payment requirement;
- Appointed the National Housing Finance Corporation (NHFC) as programme administrator; and

Importantly, it also gave subsidy housing developers the option of making a free serviced stand available to a qualifying household with an income between the R3,500 and R7,000 in lieu of the FLISP deposit subsidy.

However, high household indebtedness, the lack of affordability of housing debt, administrative challenges, structural deficiencies in the mortgage finance market, and poorly functioning housing markets, resulted in there being limited roll-out of the mortgaged-based FLISP instrument. Although it was expected that the more incremental serviced site instrument would address some of these issues, it too has had limited success. The lower-gap market beneficiaries have generally only benefited from the FLISP serviced site option when they have been classified as “non-qualifiers” in a BNG project that involves the relocation of an informal settlement or is the outcome of a service delivery protest.

As a result of the above, URERU approached the Western Cape Department of Human Settlements to provide resources to extend research into housing constraints at the subsidy level by investigating:

- Why serviced site subsidies aimed at the lower-gap market have not been rolled out.
- The development of housing delivery models that could facilitate the development of incremental housing in the lower-gap market.

- What policy amendments may be required to successfully implement such delivery models.

The Urban Real Estate Research Unit and the Western Cape Department of Human Settlements entered into a Transfer Payment Agreement where the Department provided resources to URERU to extend URERU's research by conducting short term research to understand the limited roll-out of serviced site subsidies aimed at the lower-gap market (households with monthly incomes between R3,501–R7,000) in order to inform changes needed to better support the supply and creation of housing in this market.

2. Background

The Western Cape has an estimated 1,870,000 million households. Of these, it is estimated that about 420,000 households are living in inadequate conditions¹. The performance of housing should however be measured more broadly on how it contributes to households economically, financially, socially and physically. Furthermore, there needs to be an expanded understanding of how housing contributes to society, economically, and in the creation of sustainable, efficient and viable cities. The housing “solution” therefore is not just a “numbers game”.

Notwithstanding this, there is clearly a need to deliver more houses at scale in an appropriate manner. To address the backlog in a 10–15-year period, approximately 40,000 houses need to be supplied annually. Unfortunately, this is currently not the case, with new housing supply per annum estimated to be about 1% of the total formal housing stock– approximately 13,500 houses². However, household growth is increasing at between 1,5–2% per annum, resulting in an increasing shortfall.

The reasons for this growing shortfall are historical and complex but the Urban Real Estate Research Unit argues that the issue of affordability is central to the problem. This is because for a new house to be supplied, the price (value) that a household is willing and able to pay must be greater than the cost to build the house– **the “Value versus Cost Challenge”**. If this is not the case, the project will not be financially viable and a developer will not be able to sustainably provide housing over the long term. Broadly speaking affordability is a function of two main factors. Firstly, the ability of a household to pay for a house, which is in turn a function of a household’s income, credit worthiness and the value of existing assets they may own. Unfortunately, many households are asset poor for historical reasons, many have high levels of indebtedness and or impaired credit records and generally have low levels of income. Secondly, affordability is a function of the cost of a house, which has been increasing due to the inelastic supply of land, complex development processes, rising building costs, and at times, inappropriate high standards.

In response to this affordability challenge, the state has implemented a predominantly supply-side subsidy housing programme. However, whilst delivering an impressive number of housing units, this programme has been unable to address the housing problem at the right scale for the following reasons.

- Firstly, for equity reasons, the need to achieve economies of scale and keep costs in check, a standardised house has often been delivered in poorly-located areas,

¹ Figures escalated from the WCDHS. (2015). “A Human Settlements Demand Study in the Western Cape”

² This figure is extrapolated from the Cape Metropolitan housing supply figures.

which means that the employment and social facility needs of many households have not been met.

- Secondly, the state's institutional structures, supply-chain requirements and project planning, have undermined its ability to deliver as is evidenced by the inability to meet housing delivery targets year-on-year.
- Thirdly, rationing housing subsidies and selecting subsidy beneficiaries is an inherently fraught exercise, given the extremely high levels of housing need in the target market and limited subsidy resources. Furthermore, many poor households have not been eligible to receive subsidised housing on the basis of income, lack of dependents, nationality and so on.
- Fourthly, the densities of new subsidised developments have usually been too low to accommodate existing populations, resulting in community resistance, dislocation and issues surrounding temporary housing.
- Fifthly, the sale restrictions and allocation processes embedded in the model, have undermined economic and labour mobility, which is highly problematic considering the high unemployment rate in South Africa.
- Lastly, national fiscal constraints will increasingly challenge the ability of the state to roll-out the programme as envisaged.

Similarly, efforts by municipalities and Social Housing Institutions (SHIs) to supply subsidised rental housing have had limited success due to project viability, funding constraints and stock management issues. However, in the last decade, a significant number of rental residential units have been supplied by small-scale "micro-developers" in low income areas. McGaffin et al. (2018) argue that the success of these developers is due to the fact that they have managed to overcome the "Value versus Cost Challenge" by keeping building costs low enough to meet the affordability levels in these areas. This has been achieved by building smaller units at a basic specification using locally-based contractors. Notwithstanding this, many of these units are still too expensive for those households at the bottom of the income pyramid and generally only cater for those seeking rental accommodation.

The ability of small-scale developers to address the "Value versus Cost Challenge" through the development of smaller, basic units, often on an incremental basis, does however conceptually suggest that similar successes could be achieved through an ownership, incremental model targeted at those households lower down the income pyramid. However, attempts by the state to facilitate such developments through the serviced site subsidy within the National Department of Human Settlement's Finance Linked Individual Subsidy Programme (FLISP) have been met with limited success. As a result, one of the main objectives of this report is to better understand the constraints that have limited the roll-out of this programme as a means of providing a base to develop solutions to the challenges associated with the limited roll-out of FLISP.

3. Research Objectives & Methodology

The research was aimed at meeting the following objectives:

- Briefly describing the existing lower-gap policy instruments;
- Assessing the degree to which these instruments have been successfully implemented;
- Identifying the key constraints undermining the success of these instruments and incremental housing development in the lower-gap market;
- Undertaking a literature review to identify generic housing delivery models that have been used to deliver housing in this target market;
- From this review, proposing how the existing delivery systems could be amended to deliver housing in this target market and what policy amendments are required in this regard.

The above was achieved by undertaking a literature review and interviewing a series of role-players in the lower-gap market including officials, developers, financiers and non-profit organisations. In particular, issues relating to finance, technical support (construction/transactional), regulation, and the nature of the target market were discussed in the interviews through a series of development scenarios.

4. Description of Current Lower-gap Policy Instruments

The FLISP was initially designed as a demand-side housing subsidy³ where a qualifying beneficiary purchases an affordable property in the market by raising mortgage finance and using the FLISP subsidy as a deposit. This form of FLISP subsidy is therefore referred to as the FLISP deposit subsidy hereafter. The FLISP deposit subsidy is income graded. A household earning R3,501 per month qualifies for a subsidy of R121,626, while a household with an income of R7,000 per month will qualify for a R102,893 subsidy.

In 2012, an amendment was made to the FLISP subsidy to make it possible for qualifying lower-gap market households, with incomes of R3,501–R7,000 and who are unable to obtain a mortgage, to qualify for a FLISP lower-gap serviced site subsidy.

This subsidy can be accessed in the two following ways:

4.1. IRDP Funded Serviced Site

Firstly, a qualifying beneficiary can apply to the municipality or provincial department, as the case may be, for a free vacant A-grade serviced stand developed through the National Housing Programme: Integrated Residential Development Programme (IRDP). The beneficiary does not qualify for any further housing subsidy and is responsible for financing the top structure on the site. The maximum current value of the serviced site is R45,985 (depending on the geotechnical conditions) plus a transfer fee of R1,000 and beneficiary administration fee of R300. The availability of sites depends on the availability of subsidies, the planning of projects, the municipality's allocation policy and the like.

4.2. Private Sector Purchased Site

Secondly, if the qualifying beneficiary can purchase a serviced stand via the private sector, they can apply for the FLISP subsidy to the value of the development cost of a state financed serviced stand. The beneficiary does not qualify for any further housing subsidy and is responsible for financing the top structure on the site. The maximum current value of the subsidy s/he can secure to buy the serviced stand is R45,985 (depending on the geotechnical conditions) plus a transfer fee of R1,000 and beneficiary administration fee of R300.

³ A demand side subsidy is a, "transfer made to a household with the specific purpose of increasing their willingness and ability to consume better housing or housing of a particular type" (Hoek Smit and Cirolia, 2016: p.5).

5. Review of the Constraints Undermining the Roll-out of the FLISP Lower-gap Serviced Site Subsidy

The delivery of FLISP related housing opportunities has been via the delivery approaches outlined in Table 1 below.

Table 1: Housing Delivery Models Related to All FLISP Projects

	Government led mixed income and upgrading projects	Public land release proposals to private sector developer	Market led
Site financing	Urban Services Development Grant (USDG)/ Human Settlement Development Grant (HSDG) ⁴ funding used for site servicing. Serviced sites for FLISP mortgage beneficiaries and market housing sold to developer at cost. Sites transferred directly to the FLISP lower-gap subsidy beneficiaries.	The developer raises project funding to service the sites and recoups costs via the purchase price.	The developer raises project funding to service the sites and recoups costs via purchase price.
Who undertakes the site servicing	The appointed turnkey developer/civils contractor.	Developer	Developer
Top structure financing	Recipient of the FLISP serviced site subsidy raises own top structure finance. With regards to the mortgage-linked FLISP subsidy beneficiaries, the top structure contractor raises the project finance and recoups costs via the purchase price.	Developer raises the project finance necessary to develop the top structures and recoups costs via purchase price.	Developer raises the project finance necessary to develop the top structures and recoups costs via purchase price.
Top structure construction	Property owner (lower-gap serviced site recipient)/Appointed developer/implementing agent (FLISP mortgage beneficiaries).	Developer	Developer

⁴ The USDG grant is only applicable in the Cape Town metropolitan area.

The roll-out and take up of serviced sites targeted at the lower-gap market has however only really been via municipal/provincial government-led mixed income and informal settlement upgrading projects. This is due to a number of the supply and demand related constraints experienced by developers and homeowners. While this market has, by and large, been responsible for its own top structure construction, it is believed that the potential exists for the private sector to play a greater role in top structure construction in the lower-gap market if the constraints outlined below can be addressed. The constraints inhibiting the roll-out of the subsidised sites are a function of factors impacting on the delivery of the sites (supply-side) and the ability and willingness of the households to pay for the sites and any subsequent top structure on them (demand-side).

5.1. Developer Supply-side Constraints

5.1.1. Land Issues

Developers find it difficult to acquire suitably priced land in the private market and it is extremely difficult to set up public private partnerships especially on privately owned land. Furthermore, despite the three spheres of government (national, provincial and local) having considerable land holdings in the province, it is difficult for the private sector to access this land without a tender/proposal for the development of the land being issued by the relevant government department. To date, a limited number of tenders/land release proposal calls for housing targeted generally at the FLISP market have been advertised but the FLISP lower-gap market has not been specifically mentioned⁵ in these tenders/land release proposal calls.

5.1.2. Standards and Government Fees

Land release and market led projects are treated as private developments by the municipalities and therefore they must comply with higher service standards than those applied to BNG projects. They also are liable for VAT and all government fees e.g. developer contributions for bulk and link infrastructure (although sometimes discounted by the municipality), earth works, planning approval and National Home Builders Registration Council (NHBRC) registration. Many of these are waived or discounted in BNG projects. It is estimated that the government fees add approximately R50,000 to the cost of a house while VAT adds an additional R62,775 (refer to Table 2).

The private sector developers/contractors interviewed for this study indicated the

⁵ Anecdotal evidence was shared by Paul Whelan of Provincial Government: Western Cape

cheapest new serviced site provided by them is in the region of R80,000, a cost almost double the value of the subsidy for which the beneficiaries of the private sector purchase FLISP serviced site subsidy qualify. The implication of this is that beneficiaries of the private sector purchased site are only able to afford sites that may be available in the secondary market.

Table 2: Cost Breakdown of a Typical FLISP Project

Cost element	Cost
Earthworks	R 17,500
Civils & electrical	R 75,000
Government costs	R 50,000
Professional fees	R 38,000
Sub-total	±R 180,000
Building costs	R 238,000
VAT	R 62,775
TOTAL	±R481,275

(Source: Bothma, S. SAINV Presentation, 27 July 2018)

5.1.3. Finance Costs

The ability of developers to raise finance to fund land and project costs is a major challenge in the supply of affordable serviced sites. To begin with, financiers are generally reluctant to finance land acquisitions and if they do so, they will only fund 50–70% of the land cost. Furthermore, if the developer acquires state owned land via a Land Availability and Development Agreement, it is difficult to raise project finance as funders cannot register a mortgage over the property. As a result, developers have to carry a significant percentage of the project costs, including the interest charges on debt incurred, from project initiation to the transfer of the property into the beneficiaries' name.

The abovementioned project finance arrangement makes the financial viability of the project very sensitive to delays due to community dynamics and/or getting approvals from the municipality. For example, a transfer certificate⁶ is onerous to secure from the municipality. A transfer certificate is a precondition for the application to the Registrar of Deeds to transfer erven. The application process can only start once the installation of services on a land unit (which is to be subdivided) is complete. Municipal departments must sign off that all their conditions of approval have been met. This process can easily take 3 months despite the required information being supplied

⁶ In terms of Section 40(11) of the Western Cape Land Use Planning Act, 2014 and Section 54(1) of the Cape Town Municipal Planning By-Law, 2015.

timeously. At this stage, the developer's capital exposure is at the highest (land paid, lengthy rezoning process complete, professional fees paid, and services installed/paid for) and therefore the financial implications of delays can be substantial.

5.1.4. Project Scale and Sub-contractor Capabilities

The number of turnkey developers in the FLISP and BNG markets is very limited and they are usually only attracted to projects that comprise of more than 1,000 housing opportunities or more so that economies of scale can be achieved to ensure project viability. However, projects of such scale are limited. Furthermore, whilst the number of servicing and building contractors operating in these markets are much higher, they range from large and medium contractors to a labour-only, bakkie-builder who builds one house at a time. This raises an issue as the overheads and operational requirements of these different contractors vary and so does their building cost and building quality.

5.2. Home-owner Supply-side Constraints

5.2.1. Infrastructure Issues

One of the main challenges with the serviced site subsidy approach for home-owners is that electricity, water and sewer connections are only provided to the edge of the site. The Revised Enhanced Serviced Site Policy Guidelines, drafted by provincial government, makes it possible to supply prefabricated wet cores on-site and service projects targeted at the BNG market. The wet cores are linked to the sewer and water network and comprise of a structure, toilet and internal and external basin. These, plus the connection fees, cost in excess of R13,000. However, no similar policy exists for the lower-gap FLISP market. As the wet core constitutes a substantial capital outlay for the lower-gap market, the beneficiary is likely to delay occupation of the site until they are able to pay for it and some form of top structure.

5.2.2. Subsidy arrangements

Several horizontal and vertical inequities have crept into the subsidy programme over time.

Firstly, in July 2018 the upper income limit of the FLISP deposit subsidy changed from R15,000 per month to R22,000 per month. No upward adjustment was made to the lower gap limit of R7,000. This is unfortunate as the general feeling of a few the role players interviewed was that the upper income limit should be adjusted to about R10,000.

Secondly, the quantum of subsidy qualifying beneficiaries receive in the serviced site option is between R56,000 and R74,000 lower than that of households that make use

of the FLISP deposit option. Greater equity could be achieved by the inclusion a starter housing component that kick starts the house construction process in a sustainable manner.

The City of Cape Town (2015) has investigated a range of minimum site and service options in terms of the associated costs and management requirements. The outcomes of the study are summarized in Figure 1. Options 3-5 in Figure 1 should be explored further as a strategy to include a starter housing component using the a FLISP lower-gap serviced site subsidy.

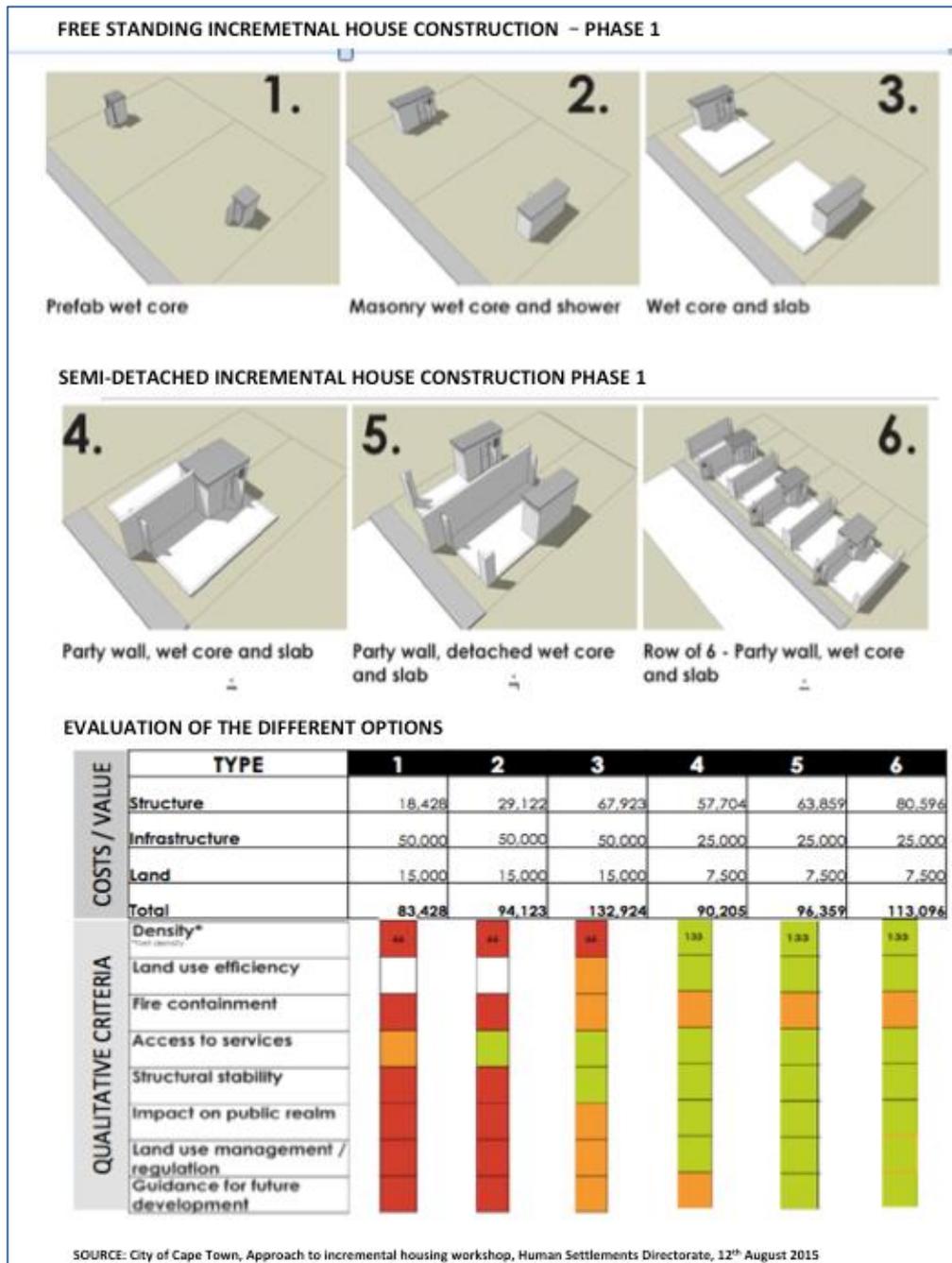


Figure 1: City of Cape Town’s Analysis of Different Phase 1 Incremental House Construction Options

5.2.3. Incremental house construction and technical support

Although self-build and incremental house construction help improve affordability, they are not without their problems, especially where they are not supported by adequate technical assistance and finance. On the positive side, labour costs constitute up to 40% of the construction costs of a dwelling unit and therefore the use of voluntary/unpaid labour can lead to a substantial saving in the cost of a house. On the negative side, the time lapse between acquiring materials and using them can lead to the deterioration of the materials or lead to leakage due to theft. Similarly, the phased construction of a house (e.g. one room, slab, walls or roof at a time) over a long period of time can lead to inefficiencies and increase the cost of the house. Lastly, low-income families, seeking to keep costs low, find it hard to justify the added expense of paying for technical plans and oversight. Consequently, the use of space, lighting, ventilation and structural soundness of the top structure may be compromised.

In response to this, homeowners have often obtained advice and support when undertaking home improvements from a number of sources. Figure 2 shows the results of a survey done by The Centre for Affordable Housing (CAHF) & EIGHTY20 in Khayelitsha and Cato Manor.

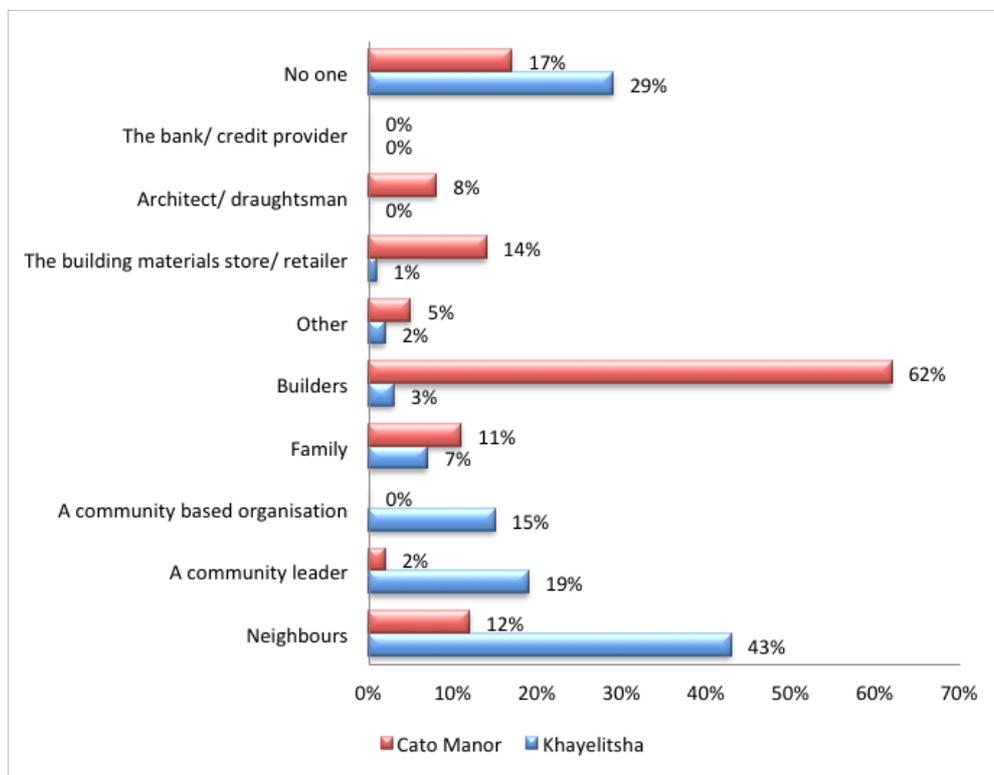


Figure 2: Sources of Advice Regarding the Building Process

(Source: Centre for Affordable Housing Finance & EIGHTY20, 2017)

Other examples of support include the following:

- The iBUILD (2018) and CAHF's case studies (Kruger-Levy, 2016; and de Jager, 2016) identify the valuable role building material supplier/micro-financier partnerships can play in providing advice and support and how this is mutually beneficial to the all 3 parties, including the owner-builder. It also helps increase the demand for loans and materials and manage risks associated with leakage (funds not used for intended purpose).
- Some local authorities are providing useful support to home-builders. For example, local planning offices in the City of Cape Town have played a helpful advocacy and advisory role with regards to the siting of the building and building plans. This service may however be undermined when the centralised, Development Application Management System (DAMS) electronic plan submission process is fully operational⁷. As a result, an alternative support mechanism may need to be put in place when this occurs.
- Municipal and NHBRC building inspectors provide useful support to the homeowner when overseeing the quality of construction on their site. Once again technological innovations, such as use of drone technology to monitor building activity to replace rather than complement building inspectors, may reduce the on-site technical assistance or quality control provided by building inspectors. If this is the case, an alternative support mechanism may need to be put in place.
- The Development Action Group (DAG), a Cape Town-based non-profit organization, offers contractor training support and links this to assistance with NHRBC and Construction Industry Development Board (CIDB) registration (DAG, 2018). Fix Forward (2019) also offers contractor development programmes. They go one step further by assisting the contractors to get work. For a project management fee, they act as the intermediary between people requiring building services and the general contractors and skilled labour they have registered.
- The Western Cape Department of Human Settlements (WCDHS) and the African Centre for Cities (ACC)'s incremental housing research paper (2013) talks to the importance of linking projects into broader networks. Technology presents an important opportunity to facilitate this networking. The iBUILD⁸ application under

⁷ Interview with City of Cape Town officials

⁸ Not to be confused with the IBuild Home Loans albeit IBuild Home Loans and iBUILD are in partnership with one another to launch iBUILD in Cape Town supported by Sofala Capital (ibuild, 2018)

development in South Africa could be a significant contributor to enhancing support to small-scale developers/builders in the South African housing market.

“iBUILD is planning to be the world's first end-to-end home construction platform for whole house construction, incremental construction and repair. The iBUILD mobile application guides customers through every stage of the construction process however big or small, providing virtual project management for: housing finance, construction design, contractor and artisan bid management, materials and supply management and electronic payments. iBUILD offers the ability to pay based on verifiable project milestones and inspections, all within a secure, transparent ecosystem. Both formal and informal sector citizens have the ability to track and trace project costs and payments across all transactions within the ecosystem, delivering ultimate security and accountability” (iBUILD, 2018)

The exploration of building technologies that may make construction more affordable, quicker and easier, and may or may not be permanent, is being explored in the City of Cape Town's Upgrading of Informal Settlement Programme (UISP) and may equally be considered in the lower income gap market. Overall, however, there is a need for a more refined understanding of the quality of local contractors, resources available to support the improvement of contractor quality and opportunities for linking contractors to owner builders and broader networks of material suppliers, micro-financiers and local municipal officers.

5.3. Developer Demand-side Constraints

5.3.1. Consumer Resistance

The private sector sees a great market opportunity in the gap market but have, for the reasons mentioned above, found it impossible, to provide an affordable product that matches the BNG free-housing market. They are particularly concerned about the politics of starter housing provision. They fear that it will lead to community protests and loan boycotts. One of the developers interviewed indicated that their company was not prepared to provide starter housing without a clear government policy being in place that specifies what starter housing products are to be offered to beneficiaries of the FLISP serviced site subsidy.

5.4. Home-owner Demand-side Constraints

5.4.1. Subsidy Quantum and Bands

Several horizontal and vertical inequities have crept into the FLISP subsidy programme over time.

Firstly, in July 2018 the upper income limit of the FLISP deposit subsidy changed from R15,000 per month to R22,000 per month. No upward adjustment was made to the threshold of R7,000 for the serviced site subsidy. This is unfortunate as the general

feeling of a number of the role players interviewed was that the upper income lower-gap limit should also be adjusted. For example, if the limit was raised to R12,500, a household could theoretically raise an additional R93,000 through loan finance for a top structure⁹.

Secondly, the quantum of subsidy qualifying beneficiaries receive in the serviced site option is between R56,000–R74,000 lower than that of households that make use of the FLISP mortgage-linked option. Greater equity could be achieved by the inclusion of a wet core and starter unit component such as a slab to kick start the house construction process in a sustainable manner.

5.4.2. Access to Finance and Loan Affordability

The FLISP lower-gap market serviced sites subsidy beneficiaries have to finance the building of the top structure and will generally require savings and/or loan finance to do so. This is because housing finance increases the pace and efficiency of the house construction process as it *“fills the gap between affordable shelter that is inadequate and adequate shelter that is unaffordable”* (UNHABITAT, 2011: p.58).

Gardener (2008) identifies three tiers of end user finance suppliers. The first is formal financial institutions that are licensed and regulated. This includes for profit commercial and micro finance banks. The second tier is non-bank micro finance institutions. Some of these institutions only provide loans and others have a broader developmental agenda, for example NGOs that are involved in housing delivery and add credit to their service package. The third tier comprises unregulated informal money lenders e.g. group savings schemes that lend to their members, loans from neighbours, moneylenders and the like. All tiers are a potential source of finance.

End user financiers face real risks and cost constraints when servicing the lower-gap market. These include firstly, the high levels of indebtedness and low credit worthiness of aspirant borrowers. Secondly, the intermittent employment of many households in the gap market and their associated variable incomes (Graham, 2018; CAHF & Eighty20, 2017). Thirdly, community dynamics and, more specifically, the threat of bond/loan boycotts. Fourthly, the fixed transaction costs of underwriting and servicing small loans and regulatory costs. Lastly, the availability and cost of wholesale financing affects their operations and the interest rate charged. The wholesale financing costs of financial institutions, who do not have access to deposit funding, is much higher than those that do (i.e. banks). For example, wholesale finance from the National Housing Finance Corporation is currently provided at 13% p.a. That is 6.25% per annum higher than the repo rate used by deposit taking commercial banks.

⁹ Based on a 25-year loan period, a 12% interest rate and 20% of income being used to repay the loan.

As FLISP lower-gap market serviced site subsidy recipients tend not to qualify for a mortgage loan, access to an adequate quantum of non-mortgage credit, often referred to as Housing Micro Finance (HMF), on favourable terms is a major challenge. The essential difference between mortgage and non-mortgage credit is that the loans are not secured through mortgages and this increases the risks and hence borrowing costs of the loans. Generally, loan sizes are smaller and loan periods shorter. HMF loans tend to be granted through several loan cycles and enable the progressive improvement of the household's living conditions.

While HMF has historically been the preserve of second tier financial institutions, many first-tier financial institutions offer personal loans and credit card overdraft facilities, which is also not secured and is provided at similar interest rate to HMF. The types of loan schemes generally offered by the formal sector are personal loans, home improvement/building material loans, group credit schemes and hire purchase/instalment sale arrangements. Many of the HMF institutions in South Africa require their aspirant borrowers to be formally employed. Where the aspirant borrower participates in the informal economy and/or does not have steady and verifiable income, additional tools must be used to evaluate affordability and creditworthiness and manage default risk.

Many low/moderate-income households opt to use informal sources of finance to incrementally build their homes. The construction of their (usually informal) dwellings is financed by personal savings, loans or gifts from family members and friends, credit unions/stokvels, pawned family assets or loans from informal money lenders. The terms of such financial arrangements vary from person to person. Without exception, they are based on interpersonal relationships between the parties. The terms offered by moneylenders can be onerous. Interest rates can exceed 150% and their debt collections methods can be unscrupulous.

Figure 3 shows the results of a CAHF/Eighty20 (2017) study how households in Khayelitsha and Cato Manor finance building work.

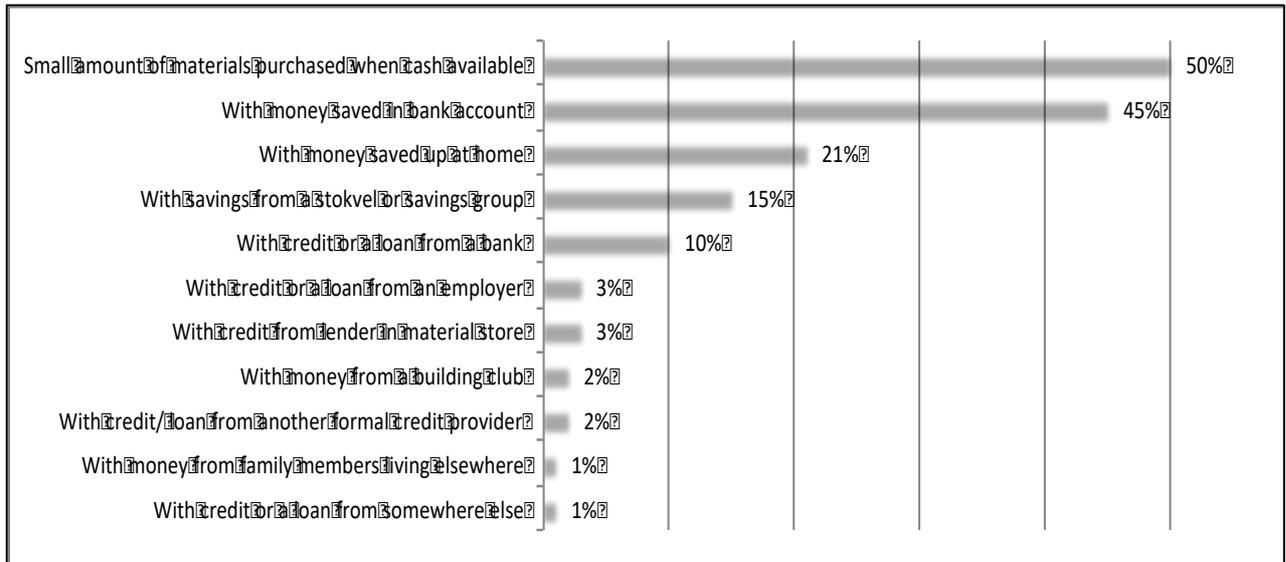


Figure 3: Sources of Finance

(Source: Centre for Affordable Housing Finance & EIGHTY20, 2017)

Ferguson and Smets (2009) have reviewed the different patterns of credit usage in developing countries. In Tanzania, they found that families used their savings in the initial stages and in the later stages they used a variety of funding sources including credit. Smets' case study (2004), as cited in Ferguson and Smets (2009), of house construction processes in Hyderabad, India, found that there was an average of five stages in the house construction process. Credit from friends and neighbours declined from stage 3 onwards (cited in *ibid*). They also found that as housing expenditures compete with other needs the time between each housing investment stage could vary considerably. It is highly likely that similar patterns of credit usage are evident in South Africa.

Table 3 compares the mortgage loan product with the non-secured loan products generally available to households that only qualify for the FLISP serviced site subsidy. It confirms that mortgage finance offers the best terms for large loans. The loan schemes that include the informally employed offer the worst terms but are often the only form of finance available to them.

Table 3: Comparison of Different Loan Products Potentially Available to the Lower-gap Market

			Mortgage Bond	building materials	building materials	building materials	(formal & informal)	(formal & informal)
		Rate	10,25%	26,00%	26,00%	26,00%	37,25%	37,25%
		Term Year	20	7	5	2	3	2
Income bracket	% of income available for housing	Monthly repayment	Approx. value of loan					
Household income of R3,501	15%	R525	R53 497	R20 233	R17 540	R9 748	R11 289	R8 795
	20%	R700	R71 329	R26 978	R23 386	R12 997	R15 052	R11 726
	25%	R875	R89 162	R33 722	R29 233	R16 246	R18 815	R14 658
Household income of R5,000	20%	R1 000	R101 870	R38 529	R33 400	R18 562	R21 497	R16 747
	22%	R1 100	R112 057	R42 382	R36 740	R20 418	R23 647	R18 422
	25%	R1 250	R127 337	R48 161	R41 750	R23 202	R26 871	R20 934
Household income of R7,000	22%	R1 540	R156 880	R59 335	R51 435	R28 585	R33 105	R25 790
	25%	R1 750	R178 272	R67 426	R58 449	R32 483	R37 619	R29 307
	30%	R2 100	R213 927	R80 911	R70 139	R38 979	R45 143	R35 169

Actual loan affordability may, however, be lower than that shown in Table 3 due to existing levels of indebtedness, household size and monthly household expenditure. The problem is that the quantum of the affordable loan is, in many instances, below what it would cost to acquire a prefabricated wet core or undertake formal housing construction.

In summary therefore, the roll-out and take up of the lower-gap subsidy sites are constrained firstly, by the fact that private developers find it difficult to supply these sites and top structures at an affordable cost and acceptable quality due to land, standards, financing and community acceptability factors. Secondly, the development of a wet core and formal structure on the sites is constrained due to beneficiaries having limited technical capacity and affordability to develop the sites.

6. International Overview of Generic Housing Delivery Models Targeted at the Lower-gap Market

In light of the constraints identified in section 5 above, a review of the literature was undertaken to identify the different housing delivery models used globally to provide incremental housing into this market.

A delivery system refers to the way housing production is organised. It is essentially the housing sector's ecosystem. Angel (1977: p.1117) defines a delivery system as “a *system of arrangements between people* (the beneficiaries) *on the one hand, and many other people that have access to housing resources, whether they be land, finance, materials, permits and information.*” Several different delivery systems can co-exist if the premises on which they are based are compatible. Each delivery system consists of activities, actors and premises, which are defined as follows:

- Activities are the operations or tasks that need to be performed to ensure that housing is built. Examples are planning, preparation, project management, preparation of a bill of quantities, plan approval, mobilization of project and end user finance, house construction, materials supply, and quality control, among others.
- Actors are the individuals, institutions and companies that control the resources or perform the activities needed to get home construction off the ground. A number of actors can usually perform a particular activity. The set of actors actually mobilised is determined by the delivery system.
- Premises are the ideological, political and economic presuppositions that underlie the design of the delivery system.

The table below provides an overview of four generic housing delivery approaches used to provide housing on serviced sites in developing countries. They range from informal house construction to large contractor built formal housing. The delivery systems are:

- Unaided self-help: This delivery system replicates the house construction processes commonly used in informal settlements.
- Supported self-help: In this delivery system, technical/project management support and advice is provided to individual property homeowners to facilitate the construction of formal housing.
- Community/project-based self-help: Individual property owners organise themselves into a group to facilitate the construction of formal housing on their

properties by a contractor or on a mutual help basis. This approach can be used by projects that make use of the government's People's Housing Process (PHP) subsidies.

- Supply/product driven house construction by small to large contractors: The state manages the servicing of the sites and the appointment of contractors to build subsidised or market-based formal housing on the sites

Table 4: Overview of Generic Housing Delivery Systems Commonly used to Provide Housing on Serviced Sites in Developing Countries

Activity/Delivery system	Unaided self-help	Supported self-help	Community/project based self help	Supply/product driven house construction by small–large contractors
Description	Individual site owner-initiated housing actions which initially or largely fall outside the regulatory framework.	Individual site owner-initiated housing actions related to the formalization of the top structure.	Community-based organization (CBO)/mutual help group actions related to the formalization of the top structure on the properties they individually own, with/without the support of a non-governmental organization (NGO) and/or the state.	Formal top structure construction initiated by the state or private developer/contractor on serviced land with or without consultation with the beneficiaries.
Product delivered	Informal unit, an incrementally built formal unit or where affordability allows a formal complete unit. Formal unit may/may not comply with building regulations.	Incrementally built formal unit or where affordability allows a formal complete unit which may/may not comply with building regulations.	Formal complete or starter house which complies with building regulations.	Formal complete or starter unit which complies with building regulations.
Project management	Individual site owner	Individual site owner/technical support provider.	Individual site owner and CBO /or mutual help group supported by state, NGO, consultants and/or loan provider.	Private developer/contractor

Activity/Delivery system	Unaided self-help	Supported self-help	Community/project based self help	Supply/product driven house construction by small–large contractors
Who provides technical support	Family members, friends, skilled labour and/or supplier of prefabricated dwelling unit. Limited advice/support provided by building materials supplier.	Different levels of support provided by NGO, materials supplier/loan provider/building inspector. Sometimes a fee is charged. The types of support include plans, bill of quantities, skills training and on-site technical advice.	State, NGO, loan provider, consultants and/or building inspector. Sometimes a fee is charged. The types of support include plans, bill of quantities, on-site material depots, project management, skills training and on-site technical advice.	Private developer/contractor/consultants.
Project finance provider			Individual site owner or mutual help group via savings, NGO or loan provider.	Private developer/contractor usually with bridging finance provided by a bank.
End user finance provider	Individual site owner from savings and contributions from family members and friends. Also, micro loans from HMF institution or informal lender.	State (where subsidy available for top structure). Alternatively, individual site owner via savings, donations/loans from friends, family and/or loan from HMF institution or informal lender	State (where subsidy available for top structure). Alternatively, individual site owner via mortgage loan, savings, donations/loans from friends, family and/or loan from HMF institution.	State (where subsidy available for top structure). Alternatively, purchaser via mortgage loan, savings, donations/loans from friends, family and/or loan from HMF institution.
Materials supplier	Building materials outlets (new and second hand).	Building materials outlets (new and second hand).	Building materials outlets (new and second hand).	Contractor negotiates bulk discounts with large manufactures of materials or building material suppliers.
Construction	Individual site owner and family members and friends, skilled artisans and/or informal builders.	Usually skilled labour, labour only contractor and/or small contractor with/without assistance from the individual site owner	Individual site owner working individually or in a mutual help group, skilled artisans, labour only builders and/or small/medium contractor.	Contractor

Activity/Delivery system	Unaided self-help	Supported self-help	Community/project based self help	Supply/product driven house construction by small–large contractors
Form of subsidy	Informal site ownership or serviced site subsidised and developed by the state. In some instances, site sold at a cost recovery price.	In many instances serviced site subsidised by the state. In some instances, site sold at a cost recovery price. Technical support provided for a fee and/or financed through hidden subsidy provided by state, NGO and/or loan provider.	In many instances serviced site subsidised by the state and a form of top structure subsidy provided by the state. Alternatively, top structure financed with a loan. Technical support a hidden subsidy provided by state, NGO and/or loan provider.	In many instances serviced site and a form of top structure subsidy provided by the state. Alternatively, developer finances the servicing of the site and top structure.

This research suggests that the supported self-help and supply/product driven approaches outlined in the table above offer the best starting points for the design of business models that will address the constraints identified in section 5 above and facilitate the construction of formal housing on the serviced sites. As the beneficiaries of the FLISP serviced site subsidy do not receive a top structure subsidy, the community-based self-help option is challenging to implement.

7. Development of Two Possible Housing Delivery Models Targeted at the Lower-gap Market

Drawing on the supported self-help and supply/product-driven approaches outlined in section 6, two delivery options are proposed. Table 5 shows the attributes that these delivery options have that can assist in addressing the issues in section 5:

Table 5. Delivery Options' Attributes

Developer Supply-side attributes necessary to address issues	
Land	Ability to access rights to develop top structures on IRDP funded serviced sites targeted at the FLISP lower-gap market on a programmatic basis.
Standards & Fees	Ability to improve affordability by applying BNG standards and fee structure.
Finance Costs	Ability to develop IRDP funded serviced sites in a manner that minimises bridging finance costs.
Limited number of Contractors	Ability to mobilise the capabilities of all types of contractors.
Developer Demand-side attributes necessary to address issues	
Consumer Resistance	Ability to construct a top structure that is affordable to this market and of a standard that is acceptable to this market and surrounding communities.
Home-owner Supply-side attributes necessary to address issues	
Infrastructure	Access to a serviced site with a wet core/incremental housing component.
Technical Support	Capacity and technical capability to construct a house.
Home-owner Demand-side attributes necessary to address issues	
Subsidy quantum & bands	Greater horizontal and vertical equity in the subsidy
Technical Support	The ability to raise the necessary finance for a top structure.

In addition, both of the proposed delivery options are dependent on the following:

- Government must assume greater responsibility for the initiation, design and implementation of projects that serve the needs of the lower-gap market. It must put in place a sustained pipeline of tenders for site servicing and/or top structure projects. This will facilitate a steady supply of housing opportunities at the right price and quality and sustain the private sector construction capacity that has been built up over time. It will also help financial institutions grow and maintain their loan books.
- State housing tenders should specify the proportion of housing opportunities to be made available to the FLISP lower-gap serviced site market. Where this market is

included in projects targeted at a range of housing sub-markets, the physical interface between the different sub-markets should be given careful design attention to ensure community acceptance. To protect the property owners' investments and minimise the lenders risks, credit-linked housing built to BNG specifications should not be scattered in between BNG housing nor should the BNG and FLISP lower-gap markets be mixed up within a site and service project.

- The BNG housing product and the lower-gap housing products should be differentiated by the lower-gap complete and starter show houses having optional extra add-ons, e.g. boundary walls, internal plaster, tiling on the floor and in the bathroom, kitchen cupboards etc.
- The tenders should also be designed to mobilise all the delivery capacity in the housing sector. They should make provision for housing delivery approaches that range from the construction of the top structure by Option 1 - the property owner (with or without the support of an intermediary organisation) to Option 2– different levels of private sector construction capacity delivering starter and completed housing at scale. Both these options can be accommodated by adjusting and enhancing existing (public sector initiated) housing delivery models to accommodate FLISP lower-gap serviced site beneficiaries.

Within each of the two options there are a number of different business models. The possible business models are discussed below and summarised in Table 6. A detailed description of the models is contained in Annexure 1.

7.1 Option 1: The Property Owner Takes the Lead

Beneficiaries of a FLISP funded serviced site drive the construction of their homes using one of the following business models:

- *Supported self-build*: The state appoints a contractor to develop serviced sites, which are then transferred to lower-gap FLISP subsidy beneficiaries. Each beneficiary takes responsibility for financing and managing the construction of her/his home drawing on limited external technical support and advice that may be provided by the state and/or building suppliers. The property owner relies heavily on her/his social network for support.
- *Intermediary facilitated self-build*: The state appoints a contractor to develop serviced sites, which are then transferred to lower-gap FLISP subsidy beneficiaries. Each beneficiary then appoints an intermediary organisation to facilitate the construction of a formal top structure.

In both business models, the new property owner is responsible for raising the end user finance required. Her/his ability to raise finance will determine the nature of the product developed and the construction process. Savings and financial contributions from other family members are usually the primary sources of end user financing in these models. Where loans are applied for they are most likely to be rotating small personal finance loans or housing/building material linked loans. A small proportion of the households may be able to secure a personal loan from the bank, an employer or via a pension backed guarantee.

The new property owner may select to build a temporary structure on the property and then over time build a formal house. The speed at which the house is built will depend on her/his affordability. To assist the property owners that opt for the self-build business model, basic technical advice could be provided by the state, with the redirection of resources within the housing programme away from other priorities. Local government could, for example, set up one or more housing advice offices. The staff in the advice office could:

- Provide standard house plans and bills of quantity for sites of different dimensions;
- Comment on plans prepared by draughtsman etc.;
- Advise on the positioning of the house;
- Advise how to optimise the construction of the house given their budget constraints;
- Assist with the electronic submission of plans on, for example, the City of Cape Town's DAMS portal;
- Supply a list of contractors accredited by the municipality;
- Provide advice on building contracts and contractor payment;
- Facilitate departure applications; and/or
- Provide advice on NHBRC registration.

A property owner opting for the intermediary facilitated self-build business model appoints an organisation such as Fix Forward or the Development Action Group, to help her/him manage the house construction process. The intermediary organisation "acts as the glue" between the key role players and may/may not charge a cost recovery fee for its services. It could:

- Assist with securing end user finance and improving the property owner's credit score (if required);
- Assist with the drafting of building plans and a bill of quantities;
- Assist with plan submission and approval by the municipality;
- Check the quality of materials supplied;
- Appoint and pay the contractor;
- Assist with NHBRC registration; and/or
- Monitor the quality of construction.

Other facilitative state interventions that could support the self-build and/or the intermediary facilitated self-build business models include:

- Discounting the plan approval fees & NHBRC registration fees;
- Speeding up the plan approval process;
- Building inspectors providing on-site building advice;
- The preparation of an incremental self-building handbook that breaks up the construction process into steps that are linked to the loan amounts the market can potentially access;
- Setting up contractor/builder/skilled labour skills development and mentoring programmes to mitigate the risks of poor construction;
- Encouraging building materials suppliers to provide the following services:
 - Providing standard house plans and bills of quantity for sites of different dimensions;
 - Assisting with the estimation of materials required for plans prepared by others;
 - Advising how to optimise the construction of the house given their budget constraints;
 - Providing advice on building contracts and contractor payment;
 - Providing advice on where to apply for credit;
 - Providing advice on NHBRC registration; and/or
 - Helping to put in place an affordable fee structure for intermediary organisations supporting self-builders. The use of the intermediary should ideally be a condition of loan approval and her/his fee should be built into the loan amount/interest charge. In addition, the building materials suppliers could pay a commission to the intermediary.

Set out below are the advantages and disadvantages of this delivery option in addressing the issues and risks identified in section 5 above.

The advantages of this delivery option are:

- There is scope to provide technical advice in key areas in the supported self-build option while the provision of technical support in the intermediary supported option is substantial.
- Where the affordability exists, a formal structure could be developed within a reasonable time period.
- The property owner and/or family and friends can play a role in the construction of the house. This can lead to a considerable saving as labour costs constitute $\pm 40\%$ of the cost of building a house.
- The model facilitates the participation of small building contractors and skilled labour, who have relatively low overheads. The house, if well-constructed, may

therefore, provide better value for money spent than houses delivered by large and medium contractors.

- The property owner is likely to be more satisfied with the end product, even if the construction quality is inferior to mass contractor-built housing.
- The model is suited to projects where a small number of FLISP lower-gap top structures are to be built.
- The intermediary in the intermediary supported option helps reduce the risks of leakage and poor-quality construction. This may make it easier for the property owner to secure a larger amount of loan finance.

The disadvantages of this delivery approach are:

- Given that the serviced site is made available for free, it is possible to select households from the waiting list in registration date order and/or based on the project's allocation policy. Without the application of a filter to check affordability, a large proportion of the households in the lower-gap market, drawn from the top of the municipalities' housing waiting list are likely to be above 60 years of age and may find it too challenging (physically and financially) to construct their own home.
- The occupation of the site may be delayed as the service connections are only provided to the edge of the property.
- The property owner may not be prepared to pay a fee for the services of the intermediary and/or the intermediary's fee may be too high for this market to sustain. For example, Fix Forward charges 15% of the contract sum. Thuthukani Financial Services, on the other hand, estimated that three site inspections during the house construction process would cost R1,000 per house¹⁰.
- The property owner may not be able to secure sufficient loan finance for an optimal construction step of the top structure e.g. s/he may not have money to cover the costs of the required slab.
- The property owners' financial circumstances may result in the construction period ranging from 3 months to 20+ years.
- To avoid NIMBYism between the owners of formal properties and those with informal/incremental structures, the land parcel identified for serviced site only projects may result in being located on the periphery of cities and towns.

7.2. Option 2: Contractor Builds Starter and Complete Housing

This delivery system focuses on the construction of a formal house, by a range of developer types, that can be occupied immediately by the beneficiary of a FLISP serviced site subsidy. The product can range in size and quality. It could range from a

¹⁰ Interview with J. Cox of Fix Forward and M. Seymour of Thuthukani Financial Services

studio or one-bedroom starter house that can be expanded over time to a 40 m², two-bedroom unit with different levels of finish. At the project initiation stage, the municipality or provincial government will need to determine which business model best suits the project and prepare the appropriate tender documentation. The tender must specify the options to be constructed for households that qualify for the FLISP serviced site subsidy. The different submarkets would need to be identified in the tender to ensure that the lower gap market is addressed. Options may best be specified as the minimum deliverables required on the site based on what the subsidy can deliver and allowing the choice on the specifications on any addition structure to lie with the beneficiary as he or she will have to contribute to the top structure. Such choices can be made at the pre-sales stage, and “show houses” can be used to illustrate options and additions to (beneficiary) clients.

The business models that form part of this delivery system are:

- *Turnkey developer:* the model adapts conventional FLISP housing market features to the FLISP lower-gap and BNG subsidy provisions. The turnkey developer is appointed by a government tender and a Land Availability and Development Agreement is entered into by the parties. The turnkey developer takes responsibility for planning, bridge financing and implementing the site servicing and top structure components of the project. The turnkey developer is also responsible for marketing the properties, the selection of the beneficiaries and the transfer of the properties into the qualifying buyers' names. The turnkey developer receives payments for the site servicing component on a progressive draw down basis i.e. on the same terms as any other IRDP funded project.
- *Implementing agent:* the model adapts a typical BNG housing delivery approach to FLISP lower-gap subsidy provisions. A civils contractor is appointed by government tender to service the sites. Upon completion of the servicing, a second government tender is issued for top structure construction and a Land Availability and Development Agreement is signed with the successful bidder. The civils and building contractors are responsible for raising their own project finance. The implementing agent/building contractor is responsible for marketing the properties the selection of the beneficiaries and transferring them into the qualifying buyers' names.
- *Province/municipality as developer:* this model is based on a housing delivery approach that has been piloted by Western Cape Provincial Government and enables small contractors' participation in top structure delivery. As above, a civils contractor is appointed by a government tender to service the sites. Upon completion of the servicing, a second tender, asking for top structure proposals and cost estimates from small contractors, is issued. The number of top structures actually built by each of the successful bidders could be determined by the number

of qualifying beneficiaries with approved credit that select their show house or by their CIDB grading. The province/municipality¹¹ finances the top structure construction costs out of its own funds and is "repaid" when the property is transferred into the qualifying buyers' names. To facilitate the participation of small contractors it pays them on a progressive draw down basis e.g. slab, walls, roof and completion. The small contractors are therefore only responsible for raising project finance for a particular phase of the project. The province/municipality, with assistance of a marketing agent and conveyancer, is responsible for marketing the project and transferring the property into the qualifying buyers' names.

In all three models, the purchaser must meet the FLISP qualifying criteria to obtain the FLISP serviced site subsidy and be able to raise sufficient credit to purchase the product/s on offer in the project. Given that the top structure products are likely to cost more than R 45,000, the primary source of end user finance is likely to be loan finance combined with savings and contributions from family members and friends. The interest rate and loan term will determine the loan quantum beneficiary-purchasers are able to access. The loans are most likely to be personal or HMF loans. A small proportion of households may be able to secure a personal loan from a bank, an employer or via a pension backed guarantee. The FLISP serviced site subsidy takes the form of a discount/deposit on the product price as it is "paid out" upon completion of the top structure and registration of the property in the buyer's name i.e. not on completion of the servicing of the site.

Set out below are the advantages and disadvantages of this delivery option in addressing the issues and risks identified in section 5 above.

The advantages of this delivery approach are:

- Qualifying FLISP beneficiaries only have to take responsibility for securing the necessary finance to purchase the top structure. They have no responsibilities with respect to the construction of the top structure.
- Occupation is immediate as the services and a formal starter/complete structure are provided.
- It enables delivery at scale and accommodates small to large projects that can be implemented by a range of contractors.
- BNG SANS10400XA or similar specifications can be used to reduce the price of the top structure targetted at the FLISP lower-gap market.
- It is likely to appeal to lenders as the leakage and default risks are much lower than the incremental self-build options. Lenders are able to pre-approve the

¹¹ While the Provincial Government (Western Cape Government) is currently implementing a project of this nature, legislation may make it difficult for municipalities to "fund" the top structure construction costs.

housing typologies to be built by the contractor and their price. They are also able to check the top structure quality after construction. Furthermore, it will be easier for borrowers that find themselves in financial difficulty to let/sell their property to offset their loan obligations.

- The province/municipality as developer model is suited to projects where a small number of FLISP lower-gap top structures are to be built and facilitates the participation of small building contractors who have lower overheads and may provide better value for money spent.

The disadvantages of this delivery approach are:

- The purchaser, must be able to access a considerable sum of finance to be able to purchase the products likely to be offered. This may restrict the bottom end of the lower-gap market's access to this delivery option.
- Community dynamics and the reluctance to pay for a house when BNG beneficiaries are getting them free may undermine the success of these projects.
- The risks (theft, labour disputes, community dynamics etc.) carried by the building contractors are high and the returns are lower than a turnkey development. The profits on-site servicing are higher than they are on top structure construction. In top structure only projects the margin is in the region of 5%.
- In the province/municipality as developer model, the project management responsibilities and financial risks carried by the provincial government/municipality are higher than the other options. In addition, the construction period may be longer as small contractors can take up to 3 months to complete a house.

Table 6. Overview of Top Structure Delivery Models

Activity/ delivery approach	The property owner takes the lead		Contractor built starter and complete housing		
	Supported self-build	Intermediary facilitated self-build	Turnkey developer	Implementing agent	Province/municipality as the developer
Site finance	USDG funding used for site servicing	USDG funding used for site servicing	USDG funding used for site servicing	USDG funding used for site servicing	USDG funding used for site servicing
Who undertakes the site servicing?	Appointed civils contractor	Appointed civils contractor	Appointed turnkey developer	Appointed civils contractor	Appointed civils contractor

Activity/ delivery approach	The property owner takes the lead		Contractor built starter and complete housing		
	Supported self-build	Intermediary facilitated self-build	Turnkey developer	Implementing agent	Province/municipality as the developer
Top structure financing	Property owner (recipient of the FLISP serviced site subsidy) raises own top structure finance.	Property owner (recipient of the FLISP serviced site subsidy) raises own top structure finance.	Appointed turnkey developer raises the project finance and recoups costs via sale of property to qualifying lower-gap FLISP beneficiary	Appointed implementing agent/building contractor raises the project finance and recoups costs via sale of property to qualifying lower-gap FLISP beneficiary	Provincial/municipal government provides funds from own sources and pays contractors on a progressive drawdown basis. Appointed building contractors raise project finance for each construction phase. Provincial/municipal government recoups costs via sale of property to qualifying lower-gap FLISP beneficiary
Top structure construction	Property owner with/without the support of family, friends, skilled labour and/or small contractor	Property owner with support of implementing agent and small contractor	Appointed turnkey developer	Appointed implementing agent/building contractor (medium- large)	Appointed building contractors (small-medium)

8. Policy Recommendations

Regardless of the options and business models chosen, there are a number of policy amendments/enhancements that would support the proposed delivery systems, promote greater horizontal and vertical equity and facilitate the development of top structures targeted at the lower-gap market. These are:

- Providing land for FLISP lower-gap market housing at no/nominal cost; and applying the government's fee structure and VAT provisions applied to BNG projects to FLISP lower-gap properties/projects;
- Increasing the subsidy allocated to beneficiaries of the serviced site option by up to R60,000. The additional subsidy could be used to facilitate the immediate occupation of the site and get formal house construction off to a good start by, for example, funding the supply of a wet core, slab and/or party walls as per options 3-5 in Figure 1.
- The formulation of a FLISP lower-gap market housing policy which includes specifications regarding the contractor built starter housing options supported by the subsidy programme; and
- A review of the income ceiling of the lower-gap subsidy.

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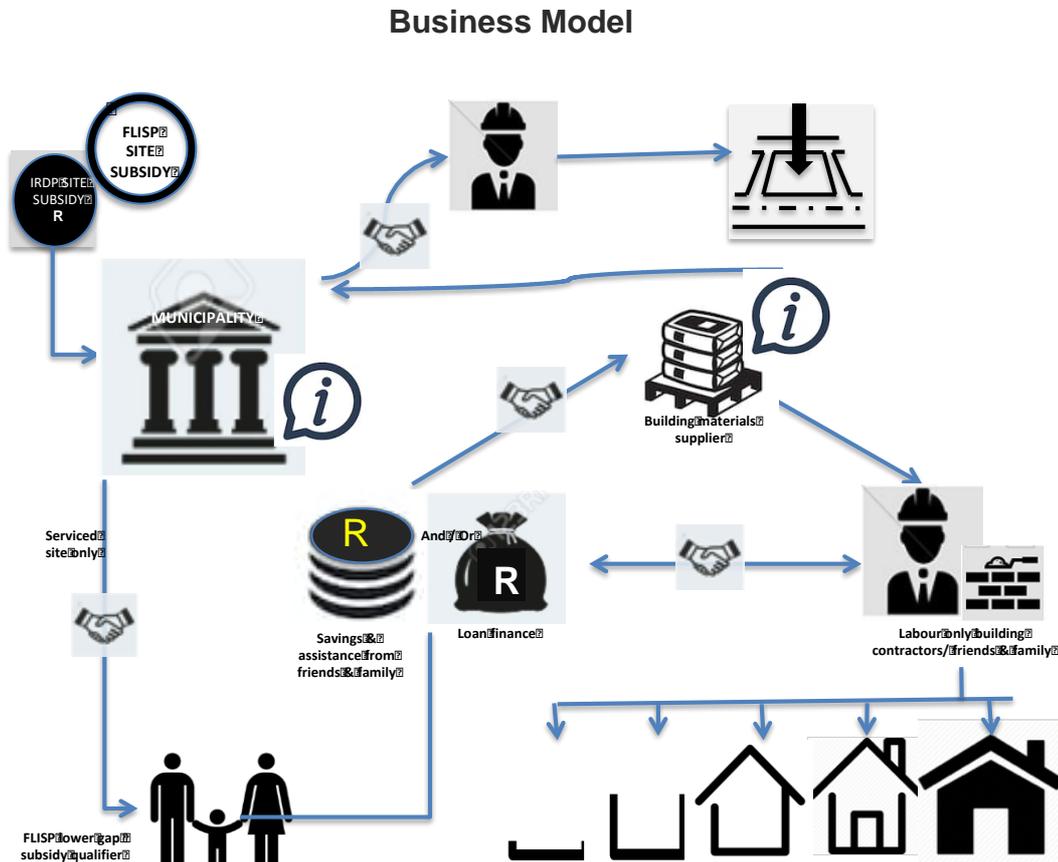
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Annexure 1: Proposed Housing Delivery Options

Option 1: The Property Owner Takes the Lead

1. Supported Self-build



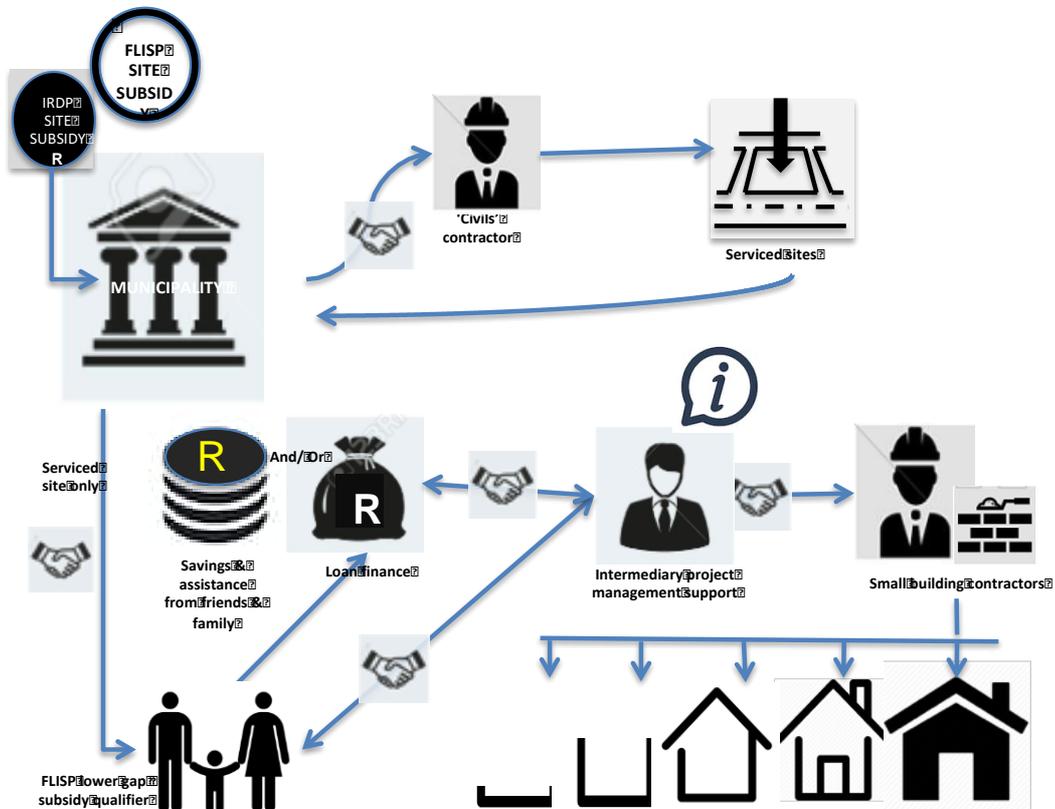
Project initiation	The municipality issues a tender for servicing sites targeted at the FLISP lower-gap market or a range of markets. When the sites are completed the municipality transfers the sites into the qualifying FLISP beneficiaries' names.
Project implementation	<p>The new property owner may select to build a temporary structure on the property and then over time build a formal house. The speed at which the house is built will depend on her/his savings and ability to secure a loan. The property owner usually purchases the building materials. House construction is undertaken by family and friends, a labour only contractor and/or skilled labour. The property owner may ask family and friends to help them manage the contractor and skilled labour.</p> <p>Additional support is provided by the municipality and/or building materials supply outlets.</p> <p>The municipality could, for example, set up one or more housing support centres. The staff in the support centre could:</p>

	<ul style="list-style-type: none"> • Provide standard house plans and bills of quantity for sites of different dimensions; • Comment on plans and advise on the positioning of the house; • Advise how to optimise the construction of the house given their budget constraints; • Assist with the electronic submission of plans on, for example, the City of Cape Town’s DAMS portal; • Supply a list of contractors accredited by the municipality; • Provide advice on building contracts and contractor payment; • Facilitate departure applications; and/or • Provide advice on NHBRC registration. <p>Other facilitative state interventions could include:</p> <ul style="list-style-type: none"> • Discounting the plan approval fees & NHBRC registration fees; • Speeding up the plan approval process; • Building inspectors providing on-site building advice; • The preparation of an incremental self-building handbook that breaks up the construction process into steps that are linked to the loan amounts the market can potentially access; and/or • Setting up contractor/builder/skilled labour skills development and mentoring programmes to mitigate the risks of poor construction. <p>Alternatively/additionally, building materials suppliers could be encouraged to provide the following services:</p> <ul style="list-style-type: none"> • Provide standard house plans and bills of quantity for sites of different dimensions; • Assist with the estimation of materials required for plans prepared by others; • Advise how to optimise the construction of the house given their budget constraints; • Provide advice on building contracts and contractor payment; • Provide advice on where to apply for credit; and/or • Provide advice on NHBRC registration.
<p>Financing of the project</p>	<p>Project financing: The USDG covers the site servicing costs. The IRDP subsidy rules determine the draw downs of the site servicing costs and hence the amount of project finance the civils contractor has to raise to cover the civils work.</p> <p>End user financing: The new property owner is responsible for raising the end user finance. Savings and donations from friends and family usually play a large part in the financing of the house. Where loan finance is secured it is most likely to be rotating small personal finance loans and/or housing/building material linked loans. A small proportion of the households may be able to secure a personal loan from the bank, an employer or via a pension backed guarantee.</p>

Beneficiary selection - FLISP serviced site subsidy	Because the site is transferred at the end of the site servicing stage qualifying beneficiaries can be selected on the basis the municipality's allocation policy and/or the allocation criteria for the the project.
Transfer of the property - FLISP serviced site qualifiers	The property is transferred into the qualifying FLISP beneficiaries' names when the servicing of the sites is completed and the General Plan is registered.
Pros	<ul style="list-style-type: none"> • The property owner is not put under pressure to secure medium to long term finance. • Where the affordability exists, a formal structure could be developed within a reasonable time period. • There is scope to provide technical advice in key areas. • The property owner and/or family and friends can play a role in the construction of the house. This can lead to a considerable saving as labour costs constitute $\pm 40\%$ of the cost of building a house. • The property owner is likely to be happier with the end product and be better placed to extend and maintain the property in the long term. • If the construction process is well managed and not too drawn out the property owner may get better value for money spent.
Cons	<ul style="list-style-type: none"> • The occupation of the site may be delayed as the service connections are only provided to the edge of the property. • A large proportion of the property owners drawn from the top of the municipalities' housing waiting list are likely to be above 60 years of age and may find it too challenging (physically and financially) to construct a formal house. • To safe guard formal property owners investment and avoid NIMBYism the land parcel identified for serviced site only projects has to be carefully selected. The implication is that most projects will be located on the periphery of cities and towns. • The property owners financial circumstances may result in the construction period ranging from 3 months to 20+ years. • Construction without qualified technical design and oversight and low skilled labour is at higher risk of structural instability and poor durability. • Uninformed budgeting may result in projects that are left incomplete or result in the property owner over paying. • Materials stored for some time on-site may be damaged or stolen. • The municipality and/or building material suppliers may not be prepared to cover the costs of supplying the support outlined above.

2. Intermediary Facilitated Self-build

Business Model



Project initiation

The municipality issues a tender for servicing sites targeted at the FLISP lower-gap market or a range of markets. When the sites are completed the municipality transfers the sites into the qualifying FLISP lower-gap market beneficiaries' names.

Project implementation

The new property owner may select to build a temporary structure on the property and then over time build a formal house. The speed at which the house is built will depend on her/his affordability. The property owner appoints an intermediary organisation e.g. a not for profit organisations such as Fix Forward or the Development Action Group to help her/him to manage the house construction process. A building materials supply outlet of HMF could also potentially play this role. The intermediary organisation "acts as the glue" between the key role players. They could:

- Assist with securing end user finance and improving the property owner's credit score (if required);
- Assist with the drafting of building plans and bill of quantities;
- Assist with plan submission and approval by the municipality;
- Check the quality of materials supplied;
- Appoint and pay the contractor;
- Assist with NHBRC registration; and/or
- Monitor the quality of construction

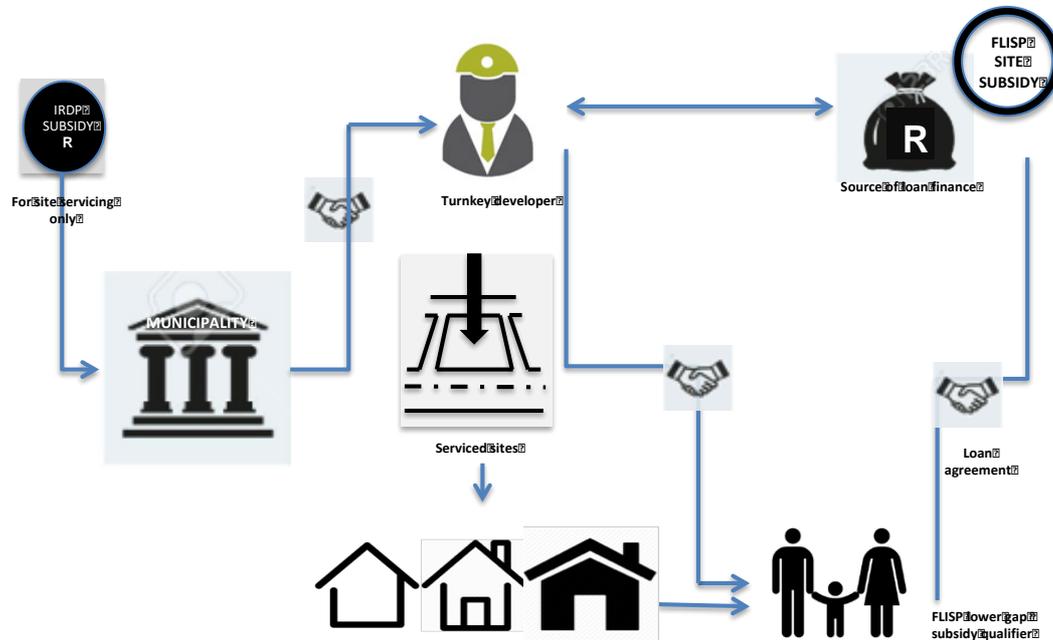
	<p>The intermediary may/may not charge a cost recovery fee for its services. Other facilitative state interventions could include:</p> <ul style="list-style-type: none"> • Discounting the plan approval fees & NHBC registration fees; • Speeding up the plan approval process; • Setting up contractor/builder/skilled labour skills development and mentoring programmes to mitigate the risks of poor construction. • Helping put in place an affordable fee structure for intermediary organisations supporting self-builders.. The use of the intermediary should ideally be a condition of loan approval and her/his fee should be built into the loan amount/interest charge. In addition the building materials suppliers could pay a commission to the intermediary
Financing of the project	<p>Project financing: The USDG covers the site servicing costs. The IRDP subsidy rules determine the draw downs of the site servicing costs and hence the amount of project finance the civils contractor has to raise to cover the civils work</p> <p>End user financing: The new property owner is responsible for raising the end user finance. Savings and contributions from friends and family usually play a large part in the end user financing in this model. Where loans are applied for they are most likely to be rotating small personal finance loans or housing/building material linked loans. A small proportion of the households may be able to secure a personal loan from the bank, an employer or via a pension backed guarantee.</p>
Beneficiary selection - FLISP serviced site subsidy	<p>Because the site is transferred at the end of the site servicing stage qualifying beneficiaries can be selected on the basis of the municipality's allocation policy and/or the allocation criteria for the the project.</p>
Transfer of the property - FLISP serviced site qualifiers	<p>The property is transferred into the qualifying FLISP beneficiaries' names when the servicing of the sites is completed and the General Plan is registered.</p>
Pros	<ul style="list-style-type: none"> • Substantial technical support is provided to the property owner during the house construction process. • Where the affordability exists, a formal structure could be developed within a reasonable time period. • It may be easier for the property owner to secure loan finance as the intermediary helps reduce the risks of leakage and poor quality construction. • The property owner and/or family and friends can play a role in the construction of the house. This can lead to a considerable saving as labour costs constitute $\pm 40\%$ of the cost of building a house. • The quality of the house construction is likely to be good. • BNG SANS10400XA or similar specifications can be used to help reduce the price of the product. • The property owner is likely to be happier with the end product. • The model facilitates the participation of small building contractors and skilled labour who have relatively low overheads. The house may,

	<p>therefore, provide better value for money spent than houses delivered by large and medium contractors.</p> <ul style="list-style-type: none"> • The model is suited to projects where a small number of FLISP lower-gap top structures are to be built.
Cons	<ul style="list-style-type: none"> • The occupation of the site may be delayed as the service connections are only provided to the edge of the property. • A large proportion of the property owners drawn from the top of the municipalities' housing waiting list are likely to be above 60 years of age and may find it too challenging (physically and financially) to construct their own home. • The property owner may not be prepared to pay a fee for the services of the Intermediary. • The intermediary's fee may be too high for this market to sustain. For example, Fix Forward charges 15% of the contract sum. Thuthukani estimated that three site inspections during house construction would cost R1,000 per house. The possibility of the fee being reduced by the intermediary supporting a group of self-builders in an area needs to be investigated further. • The property owner may not be able to secure sufficient loan finance for an optimal stage of construction. • The property owners financial circumstances may result in the construction period ranging from 3 months to 20+ years. • To avoid NIMBYism between the owners of formal properties and those with informal structures the land parcel identified for serviced site only projects would have to be carefully selected. Unfortunately, the land is most likely to be located on the periphery of cities and towns.

Option 2: Contractor Builds Starter and Complete Housing

2.1. Turnkey

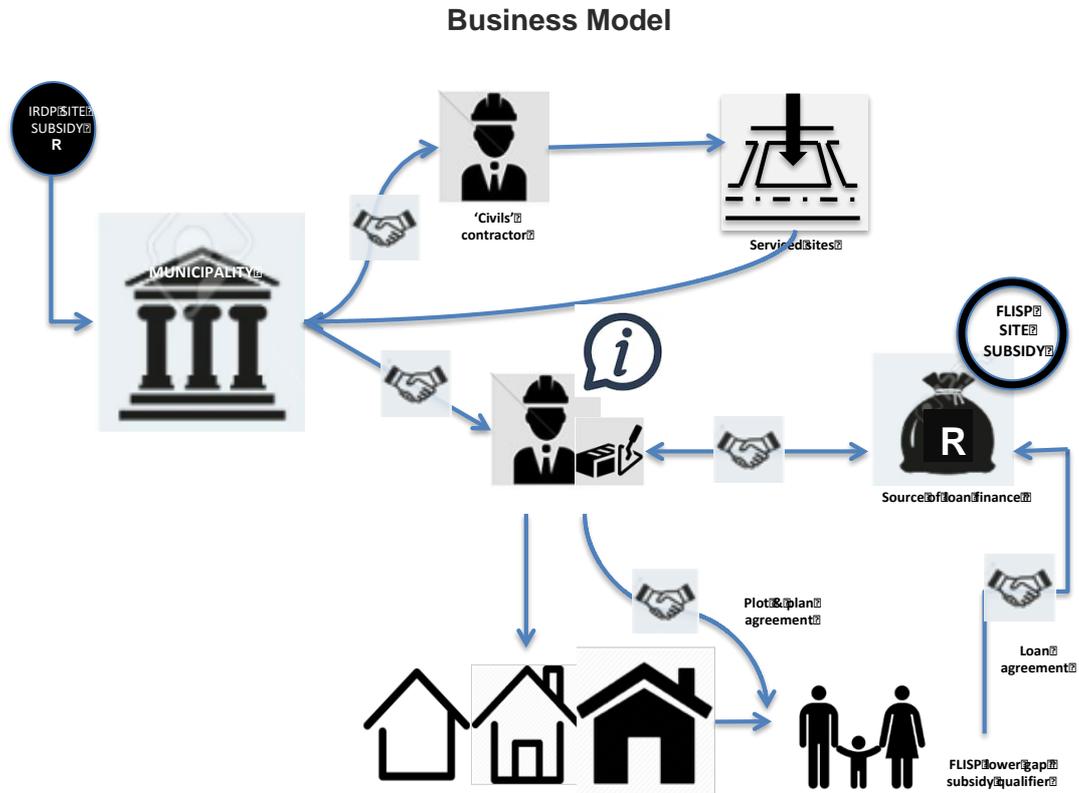
Business Model



Project initiation	The municipality issues a proposal call for a housing development on a turnkey basis. The proposal call specifies the percentage of the development that should be targetted at different markets e.g. BNG, FLISP (lower and upper gap market) and market. It also requests that a range of top structure options (including starter housing) and their associated costs be supplied. The municipality awards the tender and enters into a Land Availability and Development Agreement with the successful bidder.
Project implementation	The appointed turnkey developer takes all the responsibilities and risks associated with the project. S/he services the sites, builds the houses, markets the FLISP and market housing and transfers (with the assistance of a conveyancer), the properties into the qualifying beneficiaries' names.
Financing of the project serviced site subsidy	Project financing: The USDG covers the site servicing costs. The IRDP subsidy rules determine the draw downs of the site servicing costs and hence the amount of project finance the developer has to raise to cover the civils work. The developer will have to bridge finance the top structure costs. End user financing: The purchasers are responsible for raising the end user finance they need.
Beneficiary selection - FLISP serviced site subsidy	Prior to house construction qualifying purchaser must secure sufficient finance via loan finance and/or savings and finance from other sources (e.g. family, friends and employers), to purchase the housing product that

	meets his/her affordability. The turnkey developer will enter into a plot and plan agreement with the beneficiary when the finance is secured.
Transfer of the property - FLISP serviced site qualifiers	The property is transferred into the purchaser's name upon the full purchase price minus the FLISP subsidy being paid.
Pros	<ul style="list-style-type: none"> • Qualifying FLISP beneficiaries only have to take responsibility for securing the finance necessary to purchase the top structure. They have no responsibilities with respect to the construction of the top structure • Occupation is immediate as the services and a formal starter/complete structure are provided; • It enables delivery at scale; • It reduces the demands on the municipality; • The returns for the developer are more attractive than the other business models; • BNG SANS10400XA specifications or similar can be used to reduce the price of the top structure targetted at the FLISP lower-gap market. • It is likely to appeal to financial institutions as the leakage and default risks are much lower than the incremental self-build options. They are able to pre-approve the housing typology and price and check its quality after construction. Furthermore, it will be easier for borrowers that find themselves in financial difficulty to let/sell their property to offset their loan obligations; and • It facilitates cross subsidisation within the project.
Cons	<ul style="list-style-type: none"> • The purchaser, must be able to access a considerable sum of finance to be able to purchase the products likely to be offered. This may restrict the bottom end of the lower-gap market's access to this delivery option. • Community dynamics and the reluctance to pay for a house when BNG beneficiaries are getting them free may undermine the success of these projects. • The risks (theft, labour disputes, community dynamics etc) are high • Only large scale developers are likely to have an appetite for this type of project and have the ability to raise the necessary project finance; • The project must be a minimum of 500 units, the larger the project the better as economies of scale will help reduce the top structure costs; and • The project should ideally contain a mix of incomes and land uses.

2.2 Implementing Agent

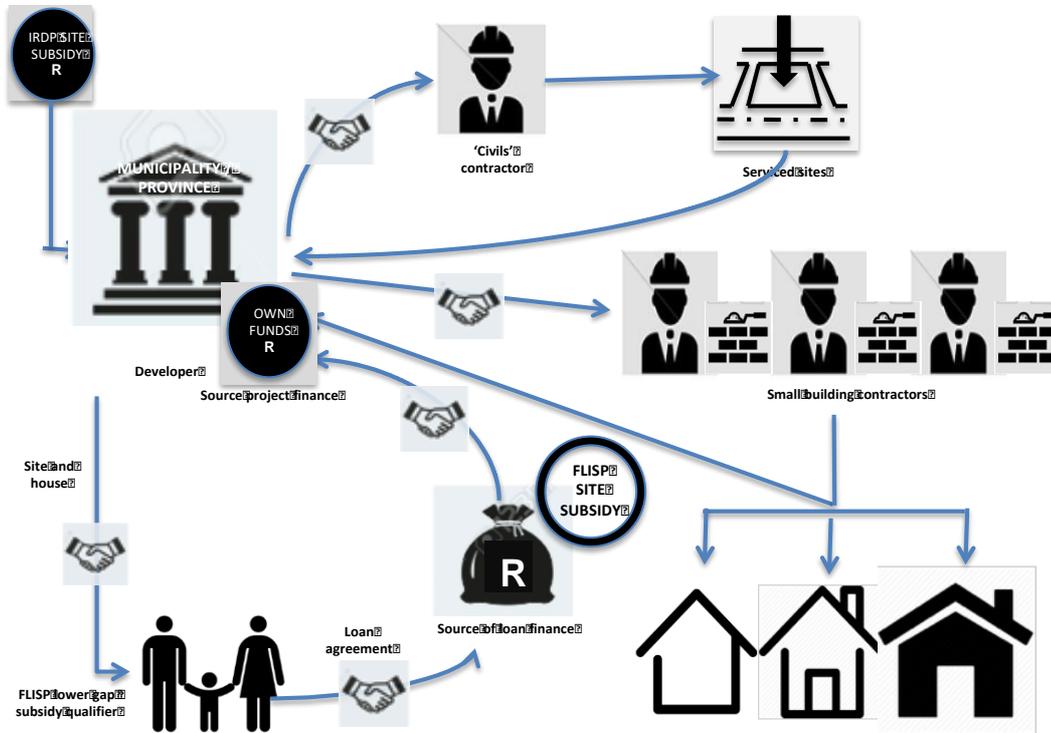


Project initiation	The municipality issues a tender for servicing sites. When the sites are completed the municipality issues a proposal call for the construction of top structures. It specifies the percentage of the development that should be targetted at the FLISP lower-gap market or different markets and requests cost estimates for a range of top structure options including starter housing. The starter house option must make provision for the incremental expansion of the house over time. The municipality awards the tender and enters into a Land Availability Agreement and Development Contract with the successful bidder.
Project implementation	The civils contractor takes all the risks associated with site servicing. The appointed top structure implementing agent takes all the responsibilities and risks associated with top structure construction, markets the houses and transfers (with the assistance of a conveyancer) the properties into the purchasers' names.
Financing of the project serviced site subsidy	<p>Project financing: The USDG covers the site servicing costs. The IRDP subsidy rules determine the draw downs of the site servicing costs and hence the amount of project finance the civils contractor has to raise to cover the civils work. The building contractor has to raise the top structure project finance.</p> <p>End user financing: The purchaser is responsible for raising the end user finance needed.</p>

Beneficiary selection - FLISP serviced site subsidy	Prior to house construction qualifying purchasers must secure sufficient finance via loan finance and/or savings and finance from other sources (e.g. family, friends and employers), to purchase the housing product that meets their affordability. The contractor will enter into a plot and plan agreement with the beneficiary when the finance is secured.
Transfer of the property - FLISP serviced site qualifiers	The property is transferred into the purchaser's name upon the full purchase price minus the FLISP subsidy being paid.
Pros	<ul style="list-style-type: none"> • Qualifying FLISP beneficiaries only have to take responsibility for securing the finance necessary to purchase the top structure. They have no responsibilities with respect to the construction of the top structure; • Occupation is immediate as the services and a formal starter/complete structure are provided; • It enables delivery at scale and accommodates projects > 200 units that can be implemented by a range of contractors. • BNG SANS10400XA or similar specifications can be used to reduce the price of the top structure targeted at the FLISP lower-gap market. • It is likely to appeal to financial institutions as the leakage and default risks are much lower than the incremental self-build options. They are able to pre-approve the housing typology and price and check its quality after construction. Furthermore, it will be easier for borrowers that find themselves in financial difficulty to let/sell their property to offset their loan obligations
Cons	<ul style="list-style-type: none"> • The purchaser, must be able to access a considerable sum of finance to be able to purchase the products likely to be offered. This may restrict the bottom end of the lower-gap market's access to this delivery option. • Community dynamics and the reluctance to pay for a house when BNG beneficiaries are getting them free may undermine the success of these projects. • The risks (theft, labour disputes, community dynamics etc) carried by the building contractors are high and the returns are lower than a turnkey development. The profits on-site servicing are higher than they are on top structure construction. In top structure only projects the margin is in the region of 5%. • The project must be a minimum of 200 units, the larger the project the better as economies of scale will help reduce the top structure cost

2.3 Provincial Government/Municipality as Developer

Business Model



Project initiation The Provincial government /municipality issues a tender for servicing sites. When the sites are completed the provincial government/municipality issues a proposal call for the construction of top structures to the small contractors, registered on its database. It specifies the percentage of the top structures that should be targetted at the FLISP lower-gap market or a range of markets and requests cost estimates for a range of top structure options including starter housing. The starter house option must make provision for the incremental expansion of the house over time. The municipality awards the tender and enters into a Land Availability and Development Agreement with each of the successful bidders.

Project implementation The civls work is undertaken by the appointed civls contractor. The provincial government/municipality appoints a marketing agent to sell the properties. The marketing of the houses should take place before construction starts. To facilitate the marketing of the houses each of the appointed contractors should build one or more show houses. The number of houses to be built by a particular contractor should be based on the number of “sales” of their housing product/s. Aternatively the number of top structures to be built by each contractor could be determined by their CIDB grading. The provincial

	government/municipality also appoints a conveyancer to transfer the properties into the purchasers' names.
Financing of the project	<p>Project financing: The USDG covers the site servicing costs. The IRDP subsidy rules determine the draw downs of the site servicing costs and hence the amount of project finance the civils contractor has to raise to cover the civils work</p> <p>The provincial government/municipality uses its own funds to finance the top structure construction costs. To facilitate the participation of small contractors it pays them at key milestones e.g. slab, walls, roof and completion. The implication is that the contractors only have to secure project funding for a phase of the top structure construction process.</p> <p>End user financing: The purchasers are responsible for raising the end user finance they need.</p>
Beneficiary selection - FLISP serviced site subsidy	Qualifying purchasers must secure sufficient finance via loan finance and/or savings and finance from other sources (e.g. family, friends and employers), to purchase the housing product that meets their affordability, prior to the construction of their house. The provincial government/municipality will enter into a plot and plan agreement with the qualifying purchaser when the finance is secured.
Transfer of the property - FLISP serviced site subsidy qualifier	The property is transferred into the purchaser's name upon the full purchase price minus the FLISP subsidy being paid.
Pros	<ul style="list-style-type: none"> • Qualifying FLISP beneficiaries only have to take responsibility for securing the necessary finance to purchase the top structure. They have no responsibilities with respect to the construction of the top structure. • Occupation is immediate as the services and a formal starter/complete structure are provided. • BNG SANS10400XA or similar specifications can be used to reduce the price of the top structure targeted at the FLISP lower-gap market. • It is likely to appeal to financial institutions as the leakage and default risks are much lower than the incremental self-build options. They are able to pre-approve the housing typology and price and check its quality after construction. Furthermore, it will be easier for borrowers that find themselves in financial difficulty to let/sell their property to offset their loan obligations. • The model supports the development of small contractors and is suited to projects where a small number of FLISP lower-gap top structures are to be built. It also facilitates the participation of small building contractors who have lower overheads and may provide better value for money spent.
Cons	<ul style="list-style-type: none"> • The purchaser, must be able to access a considerable sum of finance to be able to purchase the products likely to be offered. This may restrict the bottom end of the lower-gap market's access to this delivery option.

- Community dynamics and the reluctance to pay for a house when BNG beneficiaries are getting them free may undermine the success of these projects.
- The risks (theft, labour disputes, community dynamics etc) carried by the building contractors are high.
- Legislation such as the Municipal Finance Management Act may make it difficult for municipalities to use their own funds to bridge finance the top structure construction.
- The construction period may be longer as small contractors can take up to 3 months to complete a house.
- The project management responsibilities and risks carried by the provincial government /municipality are much higher than the other options.
- There are a number of hidden subsidies. This may undermine the sustainability of the model in the medium to long-term.