Case Study Series 12

March 2018

By Davina Wood

The Role of Savings and Credit Cooperative Organizations in Kenya's Housing Finance Sector

Executive Summary

With an estimated shortage of 2 million units and 61% of the urban population living in slums (WB, 2017), Kenya is facing a huge housing crisis. The high cost of development, coupled with expensive mortgage finance, make it nearly impossible for the majority of the population to become home-owners.

Unlike the traditional banking sector, Savings and Credit Cooperative Organizations (SACCOs) and Housing Cooperatives have shown themselves to be innovative and responsive to market conditions and client needs, including housing security. They have adopted various legal forms and developed an array of valuable financial services for their clients. The World Bank estimates that up to 90% of the country's housing finance is now supplied by SACCOs and housing cooperative networks (WB, 2017). While their ability to mobilize savings and importance in the housing sector is indisputable, how SACCOs support affordable housing has not been thoroughly documented.

Kenya's SACCO industry has done tremendously well given the challenging environment in which it operates. Recurrent obstacles include cumbersome title transfer procedures and lack of infrastructure. One of the industry's largest constraints has been access to low-cost, long term capital. The government has recognized the vital role the sector plays in the housing delivery chain and is developing a financial package including liquidity facilities to support its continued growth. Recently, Kenya's State Department of Cooperatives and State Department of Housing and Urban Development committed to building one million affordable housing units by 2022. Construction will be heavily subsidized by the government and the Cooperative sector is expected to be engaged as a key stakeholder.

CONTENTS

Across Africa, practitioners are grappling with the challenge of creating an enabled housing finance environment. While these challenges may seem insurmountable, there is a growing track record of novel solutions and initiatives, pioneered by policy makers, financiers, developers and households themselves, suggesting that there are new opportunities for making the housing finance sector work for the poor in Africa. This case study is part of a broader series that CAHF has commissioned in order to support professional development and inform a broader research and dialogue process. The case studies vary, addressing themes as diverse as housing microfinance, mortgage liquidity facilities, cement block-banking, home loan guarantees for the informally employed, and infrastructure financing, highlighting experiences from countries across the continent. We hope this series contributes to more precise and successful endeavours that realise the opportunities in this market.

This case study was produced with the support of FSD Africa.

As the SACCOs and Housing Cooperatives continue to solidify their role in the housing market, their capacity and performance will be subject to greater scrutiny. A closer look indicates that the sector must institute changes, such as more rigorous credit risk systems and corporate governance, in order to remain viable over the long term and to best serve their members.

This report describes the role of SACCOs in Kenya's housing finance sector. The work of Stima SACCO and Stima Investment Cooperative Society, two heavily subscribed and active organizations, is highlighted as a technical example of the way cooperatives are providing affordable housing. The government's support of the sector and other current developments are also discussed, as is its overall health, in an effort to help potential investors assess risk and identify opportunities. Increasing SACCOs' access to capital is crucial for their ongoing growth. It is hoped that the report will shed some light on the industry and thereby facilitate affordable housing investment in Kenya.

The SACCO Model and Market

SACCOs and the broader cooperative movement are an integral part of the Kenyan economy. Although many SACCOs were originally informal community savings groups known as chamas, the government's regulatory framework now covers SACCOs, and once licensed, they are formal financial institutions[1]. Existing legislation makes a distinction between deposit-taking and non deposit-taking SACCOS. The former are prudentially regulated service providers supervised by an independent statutory agency known as SASRA. The latter are registered with a government ministry, but they are not subject to prudential oversight. These differences are further discussed in the Corporate Structures and Regulatory Environment section of the paper.

As of December 2016, the country's 175 licensed and regulated deposit-taking SACCOs had nearly 3.5 million members and combined total assets of Ksh 393 billion (US$ 3.8 billion). Membership and total assets grew by approximately 9% and 13%, respectively, from the previous year.

SASRA Data	2016	% growth	2015	% growth	2014
Number of DT SACCOs	175	-0.57%	176	-2.84%	181
Members	3,456,975	9.01%	3,145,565	4.36%	3,008,497
Financials - Kshs. Million	**2016**	**% growth**	**2015**	**% growth**	**2014**
Total Assets	393,136	12.79%	342,848 1	2.04%	301,573
Total Deposits	272,749	12.95%	237,440	13.25%	205,974
Net Loans and Advances	282,733	11.20%	251,080	8.98%	228,524
Capital Reserves	67,555	24.72%	50,856	15.28%	43,086
Core Capital	58,174	28.30%	41,712	19.63%	33,525

Source: SASRA, February 2017

This is impressive, given the multitude of legal, regulatory, and operational challenges the sector faces. It must also be seen in the context of a country whose financial landscape has been dramatically transformed by the birth of Mobile Financial Services (MFS). Since its launch in 2007, MFS adoption has significantly outpaced Bank and SACCO usage. FSD Kenya's 2016 FinAccess survey reported that 71.4% of Kenyans used MFS in 2015, 31.7% used Banks, and 13% used SACCOs. Seven years earlier, in 2009, reported MFS usage was 28.4%, Bank usage was 20.5% and SACCO usage was 9%.

The remarkable growth of MFS doesn't mean that it has poached SACCO members; many Kenyans simply added MFS to a portfolio of complementary financial services. The SACCO sector's expansion is best explained by Kenya's growing economy and consumer appetite for credit. GDP growth has been relatively strong for seven years, averaging 5.64% between 2014 and 2016, and the domestic credit market has grown steadily, surpassing pre-crisis levels and averaging 43.85% of GDP between 2014 and 2016 (World Bank, 2017). These market fundamentals are not expected to change in the mid-term. Indeed, in a country with a population of 48.46 million, 24.6% of which use either informal or no financial service provider at all, there is still significant unclaimed market share open to the SACCO sector.

How they work

SACCOs are non-profit financial cooperatives owned by their members and governed by a member-elected board of directors. SACCOS were originally formed around a common bond, such as shared industry or location. Examples include a cooperative for tea-growers based in a specific region, or a cooperative for teachers based in a specific city. These days, many SACCOs are open to the public. Individuals must complete the necessary paperwork and purchase a minimum number of non-refundable shares to become a member. They also commit to a minimum monthly savings contribution. Businesses or savings groups can also join cooperatives.

[1] Chama means "group" or "body" in Kiswahili. Chamas grew in popularity in Kenya in the late 1980s and 1990s and remain an important provider of informal financial services. An estimated 41.4% of the population uses informal savings groups like chamas, Accumulating Savings and Credit Associations (ASCAs) and Rotating Savings and Credit Associations (ROSCAs) (FSD, FinAccess Report 2016).

At a minimum, SACCOs offer savings accounts and loans. Non-withdrawable accounts include the share capital the member is required to purchase, and savings that are used as collateral on deposit-based loans. Withdrawable accounts operate like current accounts, with services like chequing and salary processing. Approximately 63% of deposit-taking SACCOs, and certainly all the larger ones, are now connected to an ATM network. The Cooperative Bank of Kenya, a commercial bank whose majority ownership is controlled by a group of cooperatives, provides an ATM service and a mobile banking platform to 108 SACCOs (SASRA, 2017). Deposit-based loans are usually sized at three to four times the amount of the member's savings held at the SACCO. Repayment terms on deposit-based loans typically range between 12 and 72 months. Interest rates are fixed and in recent years have ranged between 12 and 16%, depending on the type and length of the loan. Salary-based loans are also often available to members whose salaries are processed through the SACCO.

The SACCO model encourages savings and introduces many people into the formal financial system. What makes the model unique is that loans are secured by the members' deposits, and oftentimes by guarantees from other members too. This guarantee structure leans on the community-oriented nature of the SACCO, provides an additional layer of risk assessment, and increases the likelihood of debt recovery.

Who they service

Except for MFS, which has been adopted by every socio-economic class in Kenya, the formality of financial service providers in Kenya is correlated with the user's income level. The higher the income, the higher the usage of formal financial services such as Banks and deposit-taking SACCOs. This makes sense given that a SACCO member must have savings if it wishes to utilize the SACCO to its fullest extent. Young people without savings and the poor are therefore under-represented in SACCOs. The typical client profile of one of Kenya's larger SACCOs is middle-aged, middle income or moving into middle income, has a tertiary education and is formally employed. Diaspora clients are also a part of the SACCO client profile. Aware that sustainable growth will require the infusion of new capital, SACCOs have been targeting youth in recent years.

SACCOs are present throughout the country, with more elevated usage in urban areas than rural (15.5% versus 11.5%). Central Kenya is the most serviced region; 25% of the population belongs to a SACCO. Similar to banks, SACCO members are more likely to use services monthly rather than daily like MFS. The average monthly usage rate is 67.5% (FSD, 2016).

2016 saw the emergence of SACCOs appointing third party agents to provide transactional services, namely cash withdrawals, deposits and transfers. A group of 90 SACCO agents conducted over Ksh 300 million ($2.9 million USD) of transactions in 2016 for twelve deposit-taking SACCOs. SACCO agents are an important new delivery channel as they allow SACCOs to reach members in more remote areas without having to open branches.

The number of SACCOs in Kenya has decreased slightly in recent years as consolidation has occurred. In 2015, the eight largest SACCOs (measured by total deposits) were reported to control 39.8% of the deposit-taking SACCO market (SASRA). There are approximately 100 SACCOs with total assets below Ksh 1 billion ($9.6 million USD). Overall membership growth is expected to continue unhampered thanks to a rising middle class.

Why Join? Cheap credit

The ability to access credit is what motivates many people to join SACCOs. Second only behind mobile bank account loans from the likes of KCB M-Pesa, MCo-op Cash and M-Shawri, SACCO loans account for 5% of all formal credit instruments in Kenya (FSD, 2016). Thanks to their non-profit status, SACCOS are often able to make loans at comparatively lower rates then banks. Prior to the interest rate cap put in place by the government in September 2016, the SACCO sector's weighted average interest rate was 12% while commercial banks' was 18.3% (SASRA, December 2015 rates)[2]. Some SACCOs lowered their rates once the cap was instituted, but the overall impact on the market is unclear as new data on average rates for 2016 is still not available. In addition to their prohibitive rates, the general market perception is that banks charge more fees, adding to the overall cost of borrowing.

SACCO loans are also easier to access, with much less paperwork and a faster turn-around time than banks. The processing period for a loan disbursement from a SACCO can be as short as one to two days, compared to as long as six weeks at a commercial bank (Kayira, 2017).

Higher returns

SACCOs pay higher interest rates on savings than Banks. The average rate paid on savings and deposits by deposit-taking SACCOs was 9.70% in 2016, compared to 6.37% paid by Banks (SASRA, 2017). The difference was significantly larger in 2015, at 8.08% to 1.58% (SASRA, 2016). In addition, SACCOs pay dividends to all members. An average 7.10% dividend was paid by deposit-taking SACCOs in 2016, up from 5.04% the year prior (SASRA, 2017). Some of the larger SACCOS distribute much higher dividend payments. In 2015, for example, Stima SACCO posted a dividend payment of 23%. Finally, the simple, democratic model employed by SACCOs is likely appealing to many customers.

2 The interest rate cap prohibits lending more than 4% above the 91-day T-bill rate (8.134% as of 25/09/17). Many SACCOs have implicitly complied with the cap, even though it doesn't apply to them, in an effort to remain competitive. The effectiveness of the cap has been widely contested and it is expected to be removed within the next year, after the 2017 presidential elections.

SACCOs and Housing Finance

The lack of affordable housing in Kenya is extreme. Compared to most other African countries – many of whom have no formal housing finance options at all- Kenya's mortgage market is large, and operates within a relatively mature and deep financial system. But compared to developed countries, it is tiny. There are a mere 25,000 registered mortgages in the country and mortgage debt accounts for just 3.15% of GDP (WB, 2017).

The problem is two-fold: housing is both inaccessible due to elevated purchase prices and the high cost of finance, and unavailable because it is not an appealing investment proposition. Most Kenyans cannot afford a bank issued mortgage because interest rates are so steep. In fact, the cost of borrowing is so prohibitive that it is rumored most mortgages are held by bank employees, who receive preferential rates. Basic market dynamics also cause the lack of supply. Real estate development is an expensive undertaking in Kenya, which makes building affordable housing stock unattractive for most investors. Institutional grade real estate is a better understood asset class with significantly higher returns. Cytonn Investments, a Nairobi-based private equity fund, reports average returns of 25% per annum on its real estate portfolio, which consists of high end residential or commercial projects. It is unlikely that an affordable housing development would be as lucrative under prevailing market conditions.

In the past decade, SACCOs have recognized the housing crisis facing many of their members and begun to offer an alternative, more accessible, path to homeownership. SACCOs not only offer cheaper financing options, but they also stimulate investment by providing a platform for sellers and buyers. Some Housing Cooperatives have even developed their own housing projects specifically for their members.

It is difficult to quantify the exact extent to which SACCOs are now involved in the market. FSD Kenya reports that 45.9% of housing and land purchases are now financed by SACCOs, while the World Bank estimates that up to 90% of housing finance is provided by SACCOs (FSD, 2016 and World Bank, 2017). The discrepancy in the two figures could be because most SACCOs do not include a breakdown of their debt profile in the financial statements they publish. Moreover, even if the information were available, it is hard to say whether it would be reliable, as evidence suggests that many loans booked as personal loans are ultimately being used to pay for land and house purchases. What is abundantly clear, however, is that SACCOs are one of- if not the most- important providers of housing finance in a country with an urgent and growing need for it.

Corporate Structures and Regulatory Environment

Cooperatives can take different legal forms in Kenya, depending on their objectives and purposes. The Central Bank of Kenya (CBK) began to formally distinguish between Back Office Service Activity (BOSA) or non deposit-taking SACCOs and Front Office Service Activity (FOSA) or deposit-taking SACCOs in 2008, when the SACCO Societies Act was passed. BOSAs take non-withdrawable deposits as a source of capital for lending to members. A member can use its non-withdrawable deposits as collateral for a loan, and the deposits will only be refunded if the member leaves the SACCO. Deposits at FOSAs, however, can be both un-withdrawable and withdrawable. Un-withdrawable deposits serve as collateral, and withdrawable deposits operate as demand deposits. As such, FOSAs tend to offer a more traditional product line like chequing and ATM services. Neither FOSAs nor BOSAs are registered clearing agents with CBK.

Two different authorities regulate the two types; BOSAs are regulated by The Ministry of Industry, Trade and Cooperatives, and FOSAs are regulated by the SACCO Societies Regulatory Authority (SASRA), which was also created in 2008.

SASRA is a fairly high touch authority. Its regulatory role includes licensing SACCOs and new branches, as well as approving new products. It also provides advisory and dispute resolution services to SACCOs, and it promotes the sector by championing its interests legislatively. Conversations with several SACCOs revealed that their relationship with SASRA was, for the most part, positive.

One of SASRA's most important duties is the imposition of capital requirements on FOSAs. Core capital includes member's shares, retained earnings, statutory reserves, and restricted grants and donations. Institutional capital is core capital less the member's share capital. Minimum capital ratios are as follows:

- Core capital of not less than 10% of total assets;
- Core capital of not less than 8% of its total deposit liabilities; and
- Institutional capital of not less than 8% of its total assets.

Compliance with liquidity requirements is not always met. SASRA revoked or refused to renew the licenses of eight FOSA SACCOs in 2014 and 2015. As of January 2017, 164 FOSA SACCOS had licenses to operate, twelve had restricted licenses for the period ending June 30th, 2017, one was under statutory management by SASRA, and one had its license revoked (SASRA, 2017).

FOSAs are not permitted to purchase or invest in land themselves because real estate is not considered part of the SACCO model's core business, but they can and do frequently act like agents, whereby they connect buyers and sellers. They also extend loans that are used to finance the land or house. FOSAS grow their membership base (both parties must be a member of the SACCO), share capital, and loan portfolio by encouraging such transactions. They do not charge commissions for the services rendered, but they do pass the cost of appraisals and other due diligence on to the clients. If a SACCO wants to offer real estate investment opportunities to its members, it must form a separate Housing Cooperative.

Housing Cooperatives

Housing Cooperatives are regulated by The Ministry of Industry, Trade and Cooperatives, not by SASRA, because they don't take deposits. Most invest in land as well as more conservative assets such as shares at the Cooperative Bank. Like SACCOs, the responsibility to pay their members dividends guides how much risk they assume. Some SACCOs, such as Stima, Safaricom, and Chai, work with a dual entity model, consisting of a FOSA and a Housing Cooperative that interact frequently with each other. Urithi Premier SACCO is a BOSA and its real estate arm, Urithi Housing Cooperative, is a Cooperative.

The National Cooperative Housing Union (NACHU)

The National Cooperative Housing Union (NACHU), a non-profit housing finance and technical service provider for housing cooperatives in Kenya, is a well-known player in the industry. As an umbrella organization representing housing cooperative throughout Kenya, NACHU performs advocacy work and provides technical support services, community mobilization programs, and loans to its member cooperatives. It also develops community housing projects as well as commercial real estate projects to supplement income. Over the last 4 years, NACHU has been able to complete 14 affordable housing estates comprising 1,573 units with an average price of Ksh 950,000 ($9,200 USD) per unit.

NACHU provides access to finance to both Housing Cooperatives and individual members. In 2016, 545 housing co-operatives of the 934 affiliated to NACHU were participating in NACHU Housing Scheme, representing 12,312 active individuals participating in housing saving and loan program. 84% were low-income earners and 16% modest-income (Cooperative Housing International, 2017). The non-profit reported Ksh 974 million ($9.4 million USD) in outstanding loans to Cooperatives on its 2016 financial statements. NACHU's activity in terms of savings mobilization is notable; members deposits were reported at Ksh 540 million ($ 5.2 million USD) in 2016. More than half of the savers are women.

Housing Products

As briefly mentioned earlier, SACCOs rarely extend formal mortgage products due to inherent constraints in their capital structure. SACCOs are often short on cash because membership demand for credit, coupled with the need to meet capital requirements instituted by SASRA, is often higher than member deposits. This is a tricky problem to solve. Raising equity from non-members is not an option under the co-operative model. Expanding the membership base may increase capital, but it also puts further strain on the demand for credit. And unlike Banks, SACCOs do not have access to the national payment system, meaning that deposits are their only source of liquidity.

SACCOs are therefore often forced to take loans from Cooperative Bank or other commercial banks, as exhibited by the sector's 108% debt to member deposit ratio (SASRA, 2017). Unfortunately, the spread between the rate on a commercial bank loan and the rate that the SACCOs on-lend is minimal, eating into their profit margins. As of July 2017, for example, the Cooperative Bank was making loans to Stima Investment Cooperative (Stima SACCOs sister Housing Cooperative) at a rate of 14%. Moreover, bank loans are not only expensive but short-term, creating a tenor mismatch with longer term credit products. SACCOs simply cannot tie up capital at low rates for long periods of time, making a standard mortgage product uneconomical.

As a result, most members finance their housing with short or medium-term project loans, on average ranging from four to six years. These loans are sometimes secured by a charge on property, but often are unsecured. Interestingly enough, medium term loans work well with incremental build, a common feature of the Kenyan housing landscape. Property development in is frequently done in stages, with land acquisition, service installation, and rooms being built sequentially. Whether the short-term tenor of SACCO housing finance is actually a burden or a fitting model might therefore merit further discussion. Similarly, the risk of entering into long term credit agreements with members could also influence a SACCO's degree of willingness to issue standard mortgage products. Long term financial planning necessitates job security and overall economic stability, which many Kenyans cannot reasonably guarantee for the long term.

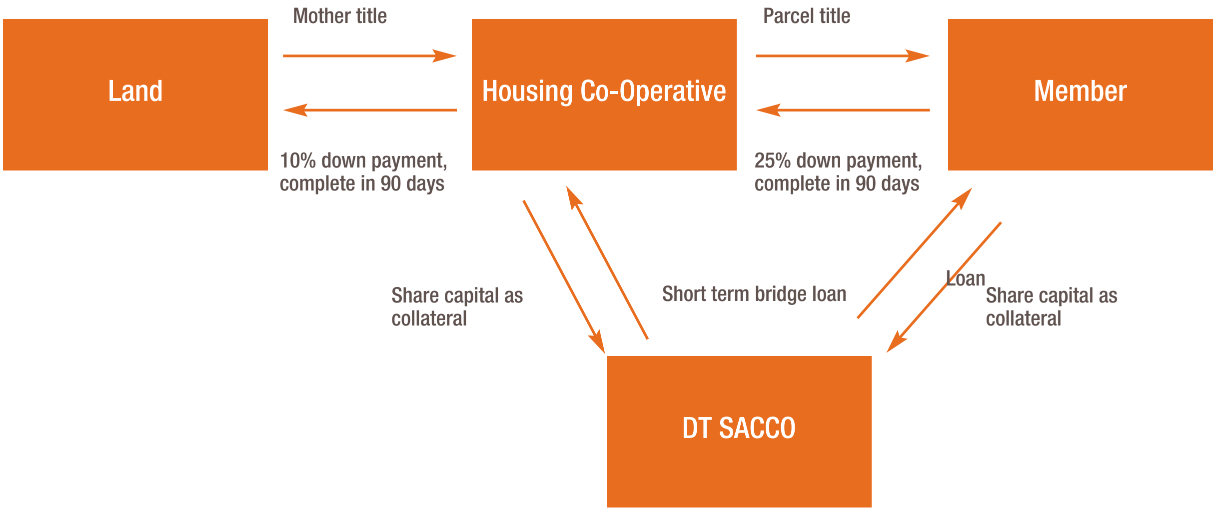
The SACCO-supported Delivery Chain

SACCOs in Kenya frequently provide loans that members use to finance housing, while Housing Cooperatives sell land to their members and sometimes act as full-fledged developers. When a Housing Cooperative is involved, the order of events is usually as follows:

1.) The Housing Cooperative will be approached by someone looking to sell a larger land parcel for a housing development project, or it will identify land itself. Sometimes SACCOs will connect a seller with a Housing Cooperative.
2.) The Housing Cooperative performs standard due diligence including title work.
3.) Once an investment decision has been made, the Housing Cooperative makes an initial deposit of approximately 10% and agrees to complete the purchase in 90 days. Housing Cooperatives shore up the funds needed for this deposit by seeking loans from their partner SACCOs or from banks.

4.) The Housing Cooperative then secures legal rights to the entire land parcel. This is known as the 'mother title'. Land in Kenya can be under a leasehold or a freehold tenure, depending on the location and use.
5.) The Housing Cooperative then markets parcels of the land to its members. Plot sizes are typically ¼ or 1/8 of an acre (1,010 or 505 square meters, respectively).
6.) Members must put down an initial deposit of approximately 25% on the land and agree to pay the balance within 90 days. Most members finance the balance by obtaining a loan from the partner SACCO or from a bank recommended by the Housing Cooperative. The Housing Cooperative holds the mother title and will not transfer the parcel's title until it has been fully paid. The title will be either freehold or leasehold, depending on the mother title's basis.

The SACCO Supported Housing Delivery Chain



In cases where Housing Cooperatives also construct homes, the member must usually put down a 10% deposit and will have three to six months to clear the balance, either with a mortgage or cash. If the house is still off-plan or in construction, then the member may be offered the option to pay in installments of up to 24 months. Development is often done incrementally according to the amount of capital raised by the Cooperative and by the financial assistance available to its members. Housing Cooperatives rarely develop residential projects entirely on their own, but rather enter into JV agreements with local developers who have construction experience.

Benefits of the Model

The benefits of this model are many. Acquiring large tracts of land versus individual plots results in cost savings that the Housing Cooperatives pass on to their members, making homeownership more affordable. It also opens up the possibility of speculative investing. It is not unheard of for Kenyans in the diaspora or chamas to purchase land through SACCOs or Cooperatives as investment opportunities. As one agent representing many end-users, the SACCO is also able to get more traction with the government when it comes to the provision of basic infrastructure services such as water, sewer, and electricity. In addition, one of the largest obstacles to acquiring real estate in Kenya is gaining clear title to land. Title issues are both costly and time-consuming, and immensely important in a country with land tenure issues and a risk of land grabbing. Housing Cooperatives, however, have the technical knowledge to manage arduous title processes, and they can foot the bill. Members also feel that they can trust the Cooperative as their interests are aligned.

Challenges

The weak points in the model are mainly rooted in access to capital. First of all, the Housing Cooperative must have enough cash on hand to make the initial deposit. Sometimes a Housing Cooperative will have to seek a loan from its partner SACCO, or it will obtain a short-term (expensive) loan from a commercial bank to bridge the initial payment.

Second of all, there must be enough member interest for the Cooperative to raise the funds it needs to complete the purchase. Finding price points that work can take some trial and error, and rarely do interested members have enough cash on hand to purchase the property outright. This is where the related SACCO once again often comes into play. While a Housing Cooperative cannot provide financing on the land, they can have exclusive financing arrangements with their FOSA SACCO counterpart. Sister SACCOs and Housing Cooperatives frequently source business for each other. Housing Cooperatives will also market their projects to other, unrelated SACCOs. Urithi Housing Cooperative, for example, frequently works with Unaitas SACCO to source buyers.
Whether or how long it takes for a member to obtain financing is essential as it directly impacts the success of a project. Economies of scale cannot be fully realized if resources aren't pooled in an adequate and coordinated manner, and construction delays are often caused by members' inability to honor payment terms.

Another frequently cited challenge for Housing Cooperatives is the development cost, which makes it very difficult for them to build homes that are affordable to low-income households. At $63,241 USD, the average cost to build a basic, generic house in Kenya is higher than in any other African country (CAHF, 2017). The cost of land, infrastructure, and sales tax in particular put a strain on project budgets.

New Initiatives

Cooperatives continue to develop new products tailored to their members' needs. Stima Investment, for example, is looking into launching a project development company that would build homes for members at cost, and potentially rent and manage the properties post-construction. Diaspora members have expressed interest in such an arrangement because it would allow them to build and own a home in Kenya, but they would not have the headache of managing the property. It would also provide a cash flow until they are ready to occupy it. Unlike Stima Investment's developments to date, the homes would be built to the individual member's specifications. Property management fees could also provide an additional earned revenue stream to the Cooperative.

SACCOs are also working together to develop strategies aimed at increasing access to housing by pooling their capital. In July 2017, a group of 35 SACCOs announced the Africa Tenancy Purchase Initiative. The scheme reportedly employs an interest free rent-to-buy model, where members pay an upfront deposit of 10% and the balance in monthly rent installments over a 20-year period. Some of the SACCOs involved include Kimisitu, Safaricom, Habitat Housing Cooperative, and Nation Housing. The proposed pipeline consists of five projects, all high-rise apartment blocks within Nairobi metropolis, containing approximately 6,000 units (Daily Nation, 2017).

Stima SACCO and Stima Investment Cooperative Society Limited

The below section provides a detailed account of Stima SACCO (Stima) and Stima Investment Cooperative Society Limited's (SIC) product offering and housing projects. It is meant to help interested parties understand the model SACCOs and Housing Cooperatives are currently employing.

Stima was founded in 1974 as a SACCO for employees of the East African Power and Light Company. It is now open to the public and has over 80,000 members. It is a deposit-taking or FOSA SACCO, offering savings and credit facilities. As of December 2016, the SACCO reported total assets of Ksh 24,482 million ($236 million USD), making it the second largest SACCO in Kenya (SASRA, 2017).

SIC provides real estate investment opportunities to its members. It also invests member capital in Cooperative Bank shares, or fixed deposits in other banks. It was founded in 2005 and now has about 13,000 members. Many members belong to both organizations. Together the two organizations have significant brand equity and are well known for their high returns to members, scope of services and product offerings, and project portfolio.

Stima SACCO (Stima)

To become a member of Stima, an individual must purchase at least one share of Ksh 100 (less than one USD) and must agree to make monthly non-withdrawable deposits of at least Ksh 1,000 ($9.64 USD). Loan products such as development loans do not specify a use of funds and may be used towards housing. A selection of Stima deposit-based loan products are highlighted below:

Loan Type	Max Amount	Annual Interest Rate	Processing Period	Repayment Period (months)	Other Requirements
Normal Development	3x deposits	12%	14 days	48	Min savings 1% of loan, up to Ksh 5,000
Super Development	4x deposits	14%	14 days	60	Min savings 1% of loan, up to Ksh 5,000. Salary must be processed through Stima.
Emergency	3x deposits	12%	8 hours	12	
Premium	4x deposits	14%	14 days	72	Min deposits Ksh 1 million, Min savings 1% of loan, up to Ksh 5,000
Corporate	4x deposits	15%	14 days	60	
Group	3x deposits	15%	14 days	36	
Makeover	3x deposits	16%	One day	15	Max loan amount Ksh 100,000
Salary Advance	Ksh 100,000	3% per month	One day		Sized at up to 50% of net salary. Salary must be processed through Stima.
Fosa Advance	Ksh 200,000	18%	One day		Salary must be processed through Stima.
Fosa Flex	Ksh 1,000,000	16%	One day		Salary must be processed through Stima. Additional min deposits of Ksh 1,000 required
Mwangaza	Ksh 2,500,000	14%	14 days		Salary must be processed through Stima. Monthly savings of 1% of loan amount up to Ksh 10,000.

Stima was one of the first SACCOs to launch its own mobile banking app. The app became available in May 2015 and is called M-Pawa. It allows users to transfer funds from one account to another, as well as to other members' accounts. It also allows members to apply for short term advances. The loans are collateralized by members' savings at the SACCO. Loans may be as small as Ksh 500 ($4.82 USD) but may not exceed Ksh 120,000 ($1,157 USD). The longest term available is six months, with payments due monthly. Interest rates are fixed and vary depending on the term:

Term	Rate
One month	7%
Two to three months	5%
Four months	4.5%
Five to six months	4%

For a period of time Stima also offered Land Purchase and Construction Loans. The program was launched in partnership with USAID and Habitat for Humanity and was piloted in 2016 in select markets. It was met with immense interest, so much so that complaints were issued by members unable to access the product because they were located outside the serviced area. Stima discontinued the program in January 2017, mainly because the relatively long-term loans of up to 12 years created a liquidity challenge for the organization. The product had also yet to approved by SASRA and its availability was always envisioned as short-term until full approval was obtained[3].

All loans had to be secured or guaranteed; eligible collateral included deposits and property titles. A sampling of the loan product line is included below:

Loan Type	Amount (Range in Ksh)	Annual Interest Rate	Repayment Period (months)	Other Requirements
Home Improvement	10,000- 200,000 (US$ 96.40 - $1928). Sized using x 5 deposit multiplier.	16	18	Cost estimate.
Land Purchase	200,000- 1,000,000 (US$1928 - $9640). Sized using x 5 deposit multiplier.	16	48	Title Deed. Member must bank with SACCO.
Progressive Construction	200,000- 1,000,000 (US$1928 - $9640). Sized using x 5 deposit multiplier.	16	60	Min savings of Ksh 1,000 or pegged to higher outstanding loans. Cost estimate & architectural sketches. Member must bank with SACCO.
Whole House Construction I	100,000- 2,500,000 (US$96.40 - $24 100). Sized using x 5 deposit multiplier.	16	72	Min savings of Ksh 5,000 over and above other loans. Approved architectural plans, bill of quantities. Member must bank with SACCO.
Whole House Construction II	2,500,000- 5,000,000 (US$24 100 - $48 200). Sized using x 4 deposit multiplier.	18	120	Min savings of Ksh 5,000 over and above other loans. Approved architectural plans, bill of quantities. Member must bank with SACCO.
Whole House Construction III	5,000,000- 7,500,000 (US$48 200 - $72 300). Sized using x 4 deposit multiplier.	18	144	Min savings of Ksh 5,000 over and above other loans. Approved architectural plans, bill of quantities. Member must bank with SACCO.

3 Information obtained from a conversation with STIMA SACCO employee at STIMA SACCO headquarters on June 23, 2017.

Stima Investment Cooperative Society Limited (SIC)

To become a member of SIC, an individual must pay an entrance fee of Ksh 5,000 ($48 USD) and buy a minimum of 300 shares at Ksh 200 ($1.93 USD) each, which is payable within 15 months. The Cooperative has developed several projects since its inception, selling both plots of land as well as houses.

The price of currently available plots ranges from Ksh 396,00 ($3,827 USD) for 1/8 of an acre to Ksh 1.2 million ($11,600 USD) for ¼ of an acre. SIC states that its average price point is Ksh 500,000 ($4,833 USD) for 1/8 of an acre, but that it has sold plots at as low as Ksh 200,00 ($1,933 USD). A selection of current plots of land for sale are highlighted below:

Project name/ Location	Size (acre)	Member Pricing (Ksh)	Member Pricing (USD)
Konza, about 80km south of Nairobi	1/8	396,000	$3,827
Rongai, about 20km south of Nairobi	¼	980,000	$9,473
Ukunda, south coast of Kenya, about 30km south of Mombasa	¼	540,000	$5,220
Malindi, central coast	¼	1,200,000	$11,600
Malindi, central coast	1/8	650,000	$6,283
Naivasha, about 90km north west of Nairobi	1/8	950,000	$9,183

The time it takes to go through the full purchase and parceling to sale can vary from project to project. Demand depends on the price and location. Plots in more affluent areas and/or near to Nairobi demand a premium, and plots priced above Ksh 800,000 ($7,733 USD) tend to move more slowly. Plots at Konza, which are on the lower end of the spectrum, have been available for members for three years and it is 80% sold. SIC has also struggled with several projects. It pulled out of a couple when there wasn't sufficient member interest or when due diligence issues arose.

Members benefit from an exclusive financing arrangement with Stima SACCO for plot financing. Terms include a fixed 9% rate and 24-month repayment period, without a guarantor. SIC keeps the title until the plot has been fully paid off.

Projects with houses for sale have also proved to be popular with SIC's membership base. Stima Village and Stima Plains are two gated communities that SIC has developed. Stima Village is located in south east Nairobi, 3.5 kms off the Mombasa road (a major highway linking Nairobi with Mombasa), and consists of 152 three or four-bedroom townhouses priced at Ksh 10.5 million ($101,000 USD) and Ksh 11.5 million ($111,000 USD), respectively. The three-bedroom units are 141 square meters and the four-bedroom units are 141 square meters, with a price per square meter of Ksh 84,677 ($788 USD) and Ksh 81,560 ($820 USD) each. Terms include a 10% cash deposit. In 2017, the price of the cheapest, newly built house by a formal developer in Kenya was $30,000 USD (CAHF, 2017), indicating that SIC's houses are clearly targeted at the middle class, which is in line with the profile of its membership base.

Stima Plains is a more recent undertaking, built on the lessons learned from the Stima Village development. Stima Plains is located about 65km east of Nairobi and it has a more varied unit mix, including two-bedroom apartments, three-bedroom duplexes/bungalows, and three-bedroom townhouses. The master plan includes a total of 327 homes. Amenities include a commercial center and a nursery. SIC is marketing the units as affordable, targeting a lower income market than Stima Village.

See below for pricing.

STIMA Plains	2 bedroom apartment	3 bedroom duplex/bungalow	3 bedroom townhouse
Price Ksh	4,000,000	5,940,000	6,780,000
Price USD	38,572	57,280	65,381
Square Meters	57	83	88
Ksh/ sq meter	70,175.44	71,566.27	77,045.45
USD/ sq meter	678	691	744

SIC offers an installment payment plan to members, with a 20% down payment, 30% further payment after 9 months, and the remaining 50% on completion. Buyers with financing from Stima or other lenders are required to put down a 20% deposit to reserve the unit. The project has been met with great interest and SIC states that it is confident it will be a success once completed. As of July 2017, ten homes had been constructed.

Government Support

The Kenyan government has repeatedly stated its intent to address the country's affordable housing crisis. The below section discusses its current support of the housing sector in general, as well as support of the cooperative sector's ability to finance and provide housing.

Recent Reforms

The Kenyan government has recently instituted several policy reforms in support of the housing market. For example, in 2016, it removed two construction levies charged by the National Construction Authority and National Environment Management Authority. The Treasury also recently reduced the corporate tax paid by developers who construct more than 400 low-cost units annually, offering a 50% tax waiver. The average sales tax per house is approximately $8,700 in Kenya, the highest on the continent (CAHF 2017). These tax reforms are therefore very important and will have a real impact on construction costs.

More specific to the SACCO sector, CBK has incorporated FOSA SACCOs into Kenya's credit information sharing platform, granting them access to Kenya's three credit reference bureaus. This should allow them to improve their risk analysis and underwriting procedures. Industry-wide adoption has yet to take place and will surely take some time, but several SACCOS have started using the system. SACCOs themselves could also contribute a wealth of valuable credit information.

Commitment to Deliver One Million Units by 2022

In September 2017, the Kenyan government committed to delivering a remarkable one million affordable housing units by 2022 through partnerships with financial institutions, private developers, manufacturers of building materials and housing cooperatives. The commitment is part of Kenya Vision 2030, a broad economic development plan launched in 2008.

A presentation prepared by the State Department of Cooperatives and the State Department of Housing and Urban Development was circulated after the public announcement. It details current challenges, including inadequate legal and regulatory framework, and lays out its delivery strategy. The strategy addresses legislation, land, infrastructure, construction, and funding. Inter-governmental collaboration, unlocking unused land, the provision of social (schools, health facilities etc.) and physical infrastructure (roads, utilities, etc.), and a focus on reducing the price of construction are key components of the program.

The one million units will be built in Kenya's largest cities, as detailed below:

Location	Land Size (acres)	Housing Units
Nairobi	3,000	450,000
Mombasa	1,200	180,000
Kisumu	1,000	150,000
Nakuru	800	120,000
Eldoret	800	120,000
TOTAL	**6,800**	**1,020,000**

The plan envisions a 65:35 ratio of housing to infrastructure on each site, and a ratio of one-bedroom to two-bedroom and three-bedroom units of 30:60:10. The sizes of the one-bedroom, two-bedroom and three-bedroom will be 30sqm, 50 sqm and 60 sqm, respectively. The project budget, which totals over Ksh 2.5 trillion ($24.8 billion USD), assumes a cost of construction per square meter of Ksh 35,000 ($338 USD). A 55-acre plot of land in Mavoko (south east of Nairobi) has been identified and will be the site of a pilot development comprising 8,223 units. Attached renderings depict high rise, high density, multifamily structures.

It isn't clear whether the government will provide the land, but as per the presentation, it will ensure the homes are affordable by covering the cost of infrastructure, using the sale proceeds of some units (three-bedroom and commercial) to subsidize smaller units, and employing a cost reduction strategy to maintain affordability. Sample mortgage terms are proposed as well. These include repayment periods of 20 to 25 years, interest rates of 3, 5, and 10%, and an assumption that no more than 30% of household income should be attributed to housing. The average mortgage rate in Kenya was 18.9% as of January, 2018, indicating that the government's target rates might not be realistic without substantial subsidy (Cytonn and www.costofcredit.co.ke).

Presumably it is expected that the Cooperative sector will market and finance the homes, as the presentation does note that the National Social Security Fund (NSSF), other pension funds, and Cooperatives are meant to serve as funding sources. The plan is clearly ambitious and early stage, but also extremely important as it sets expectations for the government's direct involvement in the provision of affordable housing. The Cooperative sector's prominent role in the delivery will necessitate its ongoing proper functioning and a high degree of professionalism.

Market Based Solutions

The CBK has reportedly been developing several market-based solutions aimed at relieving capital constraints and increasing the SACCO sector's housing finance capabilities. Several of these are discussed below. It has also reiterated its willingness to offer deposit insurance. The SACCO Societies Act of 2008 established a Deposit Guarantee Fund, which was intended to provide protection of members' deposits up to Ksh 100,000/member ($964 USD). There is no definitive timeline in place for these instruments but it is likely that together they will form part of the financial package backing the plan discussed above.

Addressing Liquidity Issues

SACCOs currently do not have access to Kenya's National Payment System and Clearing House because CBK doesn't have direct control over the sector and has been doubtful of its capacity. In addition, SASRA is a relatively new regulator; it must prove itself to be a competent and effective authority that oversees a healthy group of financial institutions.

The sector will hopefully eventually be fully integrated into the National Payments System, but in the meantime, the establishment of a wholesale bank collectively owned by SACCOs and overseen by CBK is being explored. Such a bank would represent SACCOs within Kenya's payment system, acting as a conduit to the inter-bank market. SACCOs would thus be better equipped to meet short term obligations and capital requirements, and they could access technology services that would greatly expand their reach and product offering. The SACCO owned bank would also facilitate inter-SACCO lending, providing another source of liquidity.

Another proposal being explored is the creation of a mortgage liquidity facility (MLF) that would issue bonds to provide capital to SACCOs. A MLF would provide a direct linkage between capital markets and the mortgage market. Institutional investors with long term liabilities would buy bonds issued by the MLF, and the bond proceeds would be used to refinance SACCO mortgage portfolios. The SACCOs' mortgages would be assigned to the MLF, but the bonds would not be directly linked to the underlying mortgages, thereby minimizing risk transfer. Areas that would need ironing out for such an instrument to work include pricing of the bonds, whether a guarantee would need to be included, and whether the assignments of rights the MLF has over the SACCOs would supersede the rights of SACCO members. The World Bank has experience designing and launching successful MLFs in other African countries and been working closely with CBK to develop a MLF that meets the needs of SACCOs.

Room for Improvement

Other areas where the government's support would be instrumental are on the housing supply side. These include improving timelines for planning approvals, easing the title transfer process, and delivering basic infrastructure and services. Kenya has upgraded its land registries in recent years with the introduction of record digitization and standardized forms, however further reforms are still needed for the system to work at a reasonable speed. Capacity constraints, in terms of staffing and administrative resources, could easily be addressed, for example. Improvements in these areas would unlock the country's land supply and significantly reduce the cost of building, create more confidence in the market, increase returns and attract investment capital. Finally, credit enhancements or more fiscal incentives (e.g. further tax deductions or credits) would also help to stimulate investments in affordable housing.

A closer look at the market

A closer look at the SACCO market reveals that there are more issues at play than access to capital. Technical capacity, risk management policies, debt collection procedures and corporate governance are all areas that SACCOs need to improve.

SACCO Capacity and SASRA

Not all SACCOs currently have the technical capacity to access to the National Payments system via a SACCO-owned bank or to access a MLF. Initially probably only a handful of the larger SACCOs that have rigorous credit risk procedures in place and employ sophisticated technology would be ready to use the two new facilities.

SASRA and CBK would need to create a set of guidelines and requirements, and many SACCOs would have to transition into compliance to gain access. Fortunately, the larger SACCOs also have the largest reach- as estimated fifteen of the FOSA SACCOs control 85% of industry assets- so the inclusion of just a few initially would still have a pronounced impact.

In this sense, government interventions could benefit the industry as a whole because they would incentivize SACCOS to sharpen their business practices and create points of focus for improved performance standards. The success of such a staged process, however, would depend heavily on SASRA's involvement. Hopefully the authority will continue to foster positive relationships with SACCOs and maintain a hands-on approach to ease growing pains as the sector develops.

The Cooperative Bank and NACHU could potentially play an important role as well. The Cooperative Bank could formally represent SACCOS, and NACHU could formally represent Housing Cooperatives. Both would serve as a liaison between their constituencies, the government, and investors. Their participation could be both transactional in terms of access to the liquidity facilities, as well as educational in terms of overseeing technical training.

Financial Soundness

SASRA's published numbers indicate that licensed FOSA SACCOs are, on average, meeting statutory requirements in areas of capital adequacy, asset quality, and liquidity measures. These results, and SASRA's detailed documentation, bode well for the industry.

Financial Soundness Indicators				
Capital Adequacy	**Standard %**	**2016 %**	**2015 %**	**2014 %**
Core Capital/ Total Assets	10	14.8	12.2	11.2
Core Capital/ Total Deposits	8	21.3	17.6	16.4
Institutional Capital/ Total Assets	8	8.7	8.8	5.4
Asset Quality				
NPLs to Total Gross Loans	≤ 5	5.4	5.1	5.7
NPLS Net of Provisions to Core Capital	–	14.1	14.7	17.1
Earning Assest to Total Assets	> 80	77.6	80.5	79.5
Liquidity Measures				
Liquid Assets/ Total Deposits	≥ 15	19.3	17.2	14.6
Liquid Assets/ Total Assets	≥ 10	12.9	11.9	10.0
External Borrowing/ Total Assets	≤ 25	5.1	5.3	6.4
Total Loans/ Total Deposits	≤ 85	107.0	108.7	111.0

Source: SASRA, February 2017

The vast majority of SACCOs' assets are loans, making loan portfolio health critical. The percentage of FOSA SACCOs' NPLs to Gross Loans was 5.4% in 2016, which would be high for a traditional commercial bank[4]. Provisions for loan losses are in place, but allegations that the data provided by SACCOs is unreliable, are worrisome.

In a similar vein, there is a concern that some FOSA SACCOs do not have rigorous enough underwriting and risk management policies in place. The short-term nature of credit products means that many members roll them over at maturity, therefore their ability to pay principal sums has not been tried and tested. In addition, the industry does not have standardized documentation or portfolio monitoring systems, and anecdotal evidence suggests that control and oversight in these areas may be lacking. These issues, combined with the lack of raw data or ability to quickly see each SACCOs full financial picture, makes it difficult to conclude how healthy the industry really is. It is likely that some SACCOs would have to improve on these fronts before they would be able to raise external capital.

An analysis of a Housing Cooperative would, of course, assess different performance indicators. Housing Cooperatives need to ensure that their projects are economically viable and are delivered in a timely manner. Instituting a minimum percentage uptake on pre-sales before ground breaking, for example, is good practice to avoid stalled projects. Housing Cooperatives may undertake extensive due diligence and commit capital to land acquisitions, only to be unable to complete due to lack of member interest. Members may make the initial down payment but fail to raise the funds to clear the balance. In these situations, Housing Cooperatives must pull out of transactions, loosing time and money. Such behavior might erode investor confidence. In addition, appropriate pricing is key to the delivery model and requires an understanding of the membership base's socio-economic profile.

Corporate Governance

Many SACCOs started as grass-roots organizations and have grown to be large, formidable financial institutions. The management teams that guided these SACCOs should be praised for their commitment and capabilities. The level of expertise required for effective management, however, changes as an organization expands its operations and becomes more complex.

SACCOs need to be assessed by their leadership's performance. Decisions to invest in human capital or technical capacity, for example, should be made when needed. Resolutions surrounding dividend rates and dividend capitalization are paramount to the long-term success of Cooperatives, and boards need to demonstrate their effectiveness in this area. Boards also need to ensure that SACCOs grow their membership at sustainable rates. There is an industry-wide tendency to focus on scale in order to increase share capital, but customer service could suffer if personnel or internal capacity is not increased concurrently.

[4] As a comparison, non-performing loans as a percentage of bank loans in the US was 1.47% in 2016, and peaked post financial crisis at 5%.

Investment Considerations

The industry's ongoing need for capital has naturally prompted discussions surrounding investment opportunities. As previously mentioned, equity or mezzanine investments are difficult under a cooperative model and would require demutualization. Issuing debt, however, is not out of the question and might very well be a viable option for some SACCOs or Housing Cooperatives.

When deciding where to place money, investors would need to consider the core business of a SACCO versus that of a Housing Cooperative, as well as the different regulatory authorities and their respective effectiveness. The two types of entities would use capital for varying purposes, leading to different risk profiles. SACCOs are interested in extending more and longer-term credit, while Housing Cooperatives are looking to develop more or larger projects. In situations where a SACCO has a related Housing Cooperative, both organizations would need to be assessed individually and jointly.

While the degree of professionalism and capacity varies from organization to organization, investments would most likely require intensive oversight. One solution would be to set up a special purpose vehicle under the auspices of a JV agreement, where democratically elected SACCO members would sit on the board along with the investor. The sensitivity surrounding corporate governance issues must, of course, be kept in mind.

It is likely that initial investments in affordable housing in Kenya would be made by institutional investors who are willing to sacrifice higher returns for social impact. Increasing access to affordable homes does more than provide housing security and slum eradication; the importance of numerous other secondary benefits should not be overlooked. These include job creation, financial inclusion, neighborhood stability and security, and lower fertility rates. Moreover, SACCOs are inherently positive institutions in that they promote a savings culture and increase access to credit.

Whether SACCOs and Housing Cooperatives continue to grow into robust, profitable and well-run organizations that are able to attract a wider range of investors remains to be seen, but the outlook is positive. The industry has government buy-in, which is essential, and Kenya's broader economics makes it one of Africa's more compelling investment opportunities. The government's commitment to provide one million homes by 2022 will further solidify the Cooperative sector's role in housing finance, making it even more likely that key stakeholders will continue to foster best business practices and encourage outside investment. The sector's track-record also speaks for itself. SACCOs have evolved from non-profit organizations motivated by social missions to commercially savvy enterprises, and they have managed to remain responsive to their members' demands along the way. Their limitations must be acknowledged, but so long as investors are informed and can structure around them, they should not be a deterrence. Not only Kenya, but also other African nations with similar savings cooperatives, will benefit immensely from the sector's development.

Acronym list

ASCA	Accumulating Savings and Credit Association
BOSA	Back Office Service Activity
CAHF	The Centre for Affordable Housing Finance in Africa
FOSA	Front Office Service Activity
FSD Kenya	Financial Sector Deepening Kenya
MFS	Mobile Financial Services
NACHU	The National Cooperative Housing Union
NSSF	The National Social Security Fund
ROSCA	Accumulating Savings and Credit Associations
SASRA	Sacco Societies Regulatory Authority
WB	The World Bank