STAKEHOLDER ENGAGEMENT ON THE FORMATION OF THE KENYA MORTGAGE REFINANCE COMPANY (KMRC)

SPEECH BY THE MR. HENRY ROTICH, EGH,CABINET SECRETARY FOR THE NATIONAL TREASURY AND MINISTRY OFPLANNING

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Banks Chief Executives present;
SACCOS Chairmen and Chief Executives;
KBA CEO, Dr. Habil Olaka;
Chief Executives of Financial Sector regulators
Distinguished Guests;
Ladies and Gentlemen.

GOOD MORNING,

1. It is a great pleasure to have you here today to deliberate on this all important issue on affordable housing finance which remains one of our key priorities. As you are aware, the Government has outlined four key priorities (The BIG 4 agenda) for implementation over the next five years. This includes raising the share of manufacturing sector to 15% of GDP; ensuring all citizens enjoy food security and nutrition; achieving universal health coverage and delivering at least 500,000 affordable housing units in major cities around the country by 2022.

2. The National Treasury is supporting the affordable housing agenda by facilitating the creation of a mortgage liquidity facility in Kenya -the Kenya Mortgage Refinance Company (KMRC).

3. As you are aware, affordability is a major constraint to the growth of the housing and mortgage markets and a key challenge to access decent housing. With a GDP per capita of US$2,925 per annum as of 2016, few Kenyans can afford homes built by formal developers resulting in mortgage lending being accessible to only a minority of the population. According to calculations in the World Bank Report **Improving Access to Affordable Housing in Kenya**: *A Strategic Framework,* approximately 40% of urban households and 7% of rural households would be able to afford a mortgage on a Kes. 1.7mn house, which is approximately the price of the least expensive formally built property. The Centre for Affordable Housing Finance (CAHF) has done similar work using private survey data which found a much lower level of affordability of 10.2% of urban households. The average bank mortgage of Kes. 9.1mn would only be available to a very small percentage of people. It is no surprise that only about 26.1% of Kenyans in urban areas were residing in their own dwellings according to a 2015/16 survey by KNBS.

4. **Ladies and Gentlemen,** Kenya is facing high rates of urbanization and population growth. Although only 32% of the population lives in cities today, the figure is expected to grow to 50% by 2050 according to UN Population Division (2014). Rapid urbanization has resulted in a large informal housing and slum dwellings; nearly 61% of urban households live in very poor-quality housing (slums according to the Millennium Development Goals definition). Provision of adequate housing for the low-income groups is a perpetual problem in cities. Kenya, with a population of over

46 million people, faces a critical shortage of housing units. According to conservative estimates, there is already a backlog of 2 million housing units, and the backlog increases by 150,000 units every year due to several factors including the limited availability of mortgage finance and developer finance.

5. Although small at present, Kenya has a dynamic mortgage industry, which is growing rapidly and becoming increasingly competitive. In relation to the Kenyan economy, mortgage debt represented 3.15% of GDP, based on CBK data as of 31st December 2015. However, housing finance in Kenya remains below its potential because of a number of constraints. The 2016 Residential Mortgage Market Survey conducted by the CBK revealed that high cost of houses, high interest rates on mortgages, high incidental cost of mortgages, low levels of income, difficulties with property registration and titling and lack of access to long term finance are the major inhibiting factors to the growth of the Kenyan mortgage market. Furthermore, there is little standardization of loan underwriting, documentation or servicing procedures.

6. A 2014 report of the National Treasury/CBK committee also identified a number of blockages in housing supply and the transaction process. These include lack of availability of land for affordable housing projects, high construction costs, preference for larger housing units and limited availability of financing for developers. The land registration process is cumbersome and costly particularly for multi-unit developments and results in properties being bought on mortgage priced at as much as 10% or more to cover the developer's cost of carry during the registration period.

7. However, it is gratifying to note that several policy initiatives are currently underway to address these issues. In particular, the Ministry of Lands is undertaking reforms including re-engineering of the land registration processes, digitization and computerization of land records to ease land transactions, establishment of a computerized titling center in a bid to fast-track the issuance of title deeds; and an ongoing evaluation of the Sectional Properties Act in order to facilitate issuance of titles in multi tract developments.

8. At the same time, the National Treasury is reviewing the interest rate capping law and will consider replacing it with a comprehensive legal framework to address shortcomings in the credit market. This will include promoting a fair and competitive market place for access to consumer credit, encouraging full disclosure and transparency, real financial consumer protection through effective enforcement and establishment of national norms and standards relating to consumer credit among others.

9. **Ladies and Gentlemen**, Cooperatives have been a major driver of economic growth in Kenya. In the urban areas, Savings and Credit Cooperative Organizations (SACCOs) have assisted people raise funds to get into commerce, construct housing and raise deposit to buy houses. The SACCOs continue to play an important role in realization of housing and in mobilizing funds for purchase of land to put up housing besides raising capital for housing development.

10. I understand the Kenyan SACCO sector is the largest in Africa and is globally ranked at the 11th position according to the World Organization of Credit Unions (WOCCU) 2014. The Deposit Taking Sacco (DTS) sub-sector experienced strong growth between 2014 and 2016. The total asset base

increased by 30.5% and this was funded primarily by members' deposits, which grew by 32.3% to Kes. 272.6bn from Kes. 206.0bn. Gross loans increased by 30.2% to Kes. 297.6bn from Kes. 228.5 bn. The income statement for the sector showed overall improved performance in total income, driven mainly by income from loans.

11. This growth momentum continues to underscore the importance of Deposit Taking SACCOs as alternative financial service providers. The 2016 SASRA report indicates that notwithstanding the introduction of the interest rates capping law to the Banking sector during the last quarter of 2016, there has been no noticeable ripple effect of the same to the Deposit Taking SACCOs, in the growth of their loan assets or deposits. Towards this end, the government published and tabled before Parliament the Sacco Societies (Amendment) Bill, 2016, which contained some key reforms aimed at building confidence in the DT-SACCO segment, as well as strengthening the governance and management systems among DT-SACCOs to ensure integrity and propriety in persons serving in key positions among DT-SACCOs. Some of the key reforms proposed in the Bill include: Provision of a criteria for determining suitability for persons serving or seeking to serve in key positions of DT-SACCOs; Inclusion of DT-SACCOs in to the mandatory reporting framework of credit information sharing – including full-file reporting through the established CRBs; Legal protection of the identities of DT-SACCOs, to distinguish SACCO Societies that undertake deposit-taking business, and those that do not.

12. **Ladies and Gentlemen**, the purpose of establishing KMRC is to offer the housing finance market in Kenya a credible, professional and high quality large scale medium- to long-term refinance. This type of institution has proven to be an important factor in the launching, growth and success of mortgage finance markets in other emerging countries.

KMRC would serve as a secure source of long term funding at attractive rates while ensuring sound lending habits amongst PMLs resulting in greater availability of fixed rate mortgages, and longer available loan terms. This would improve mortgage affordability, increase the number of qualifying borrowers and result in the expansion of the primary mortgage market and home ownership in Kenya while deepening the capital markets.

13. KMRC will be set up as a limited liability company incorporated under the Companies Act. It will be a newly created, non-bank financial institution that is restricted to providing long-term funding and capital market access to mortgage lenders and issuing bonds to investors. As a wholesale secondary market institution, it will neither take deposits nor lend directly to individual borrowers. The company will be subject to regulation and supervision of the Central Bank of Kenya (CBK) with CMA providing oversight over its bond issuance operations.

14. The primary objective of KMRC is to operate as a private sector driven company with the public purpose of developing the primary and secondary mortgage markets by providing secure, long-term funding to the mortgage lenders, thereby increasing the availability and affordability of mortgage loans to Kenyans. Based on international experience, such facilities are owned by the banks or institutions which use it for refinancing. Including SACCOs in the solution would broaden the reach of housing finance to borrowers with low and informal incomes and therefore the potential increase in the number of loans originated and borrowers reached could be quite large. Additionally, KMRC operations would contribute to the improvement of lending practices in Kenya and incentivize standardization of terms and conditions among lenders.

15. We expect that on inception the KMRC will be financially stable with strong positive cash flows enabling it to meet its business obligations. It is however pertinent to note that the KMRC is primarily a vehicle for market development; therefore, investors need to take a long-term view to investments made in the KMRC. There is also the social impact of investing in the KMRC in view of the many social benefits associated with increased housing production, finance, and home-ownership, including job creation, improving the asset base, and providing formal sector homeowners a legal stake in their community.

16. The National Treasury is committed to provide strong support to KMRC during its early years in order to assist the Company achieve long-term sustainability. The KMRC will have equity capital contributions from the GOK and some international financial institutions that have already committed to support GoK on this initiative. In this regard, we encouraged you to subscribe to the Company's equity capital in order to benefit from KMRC's services including access to affordable long-term funding at fixed price, as in mortgage refinance companies in other countries.

17. **As I conclude, Ladies and Gentlemen,** the National Treasury has prepared an information document which provides greater detail on the establishment of KMRC. The document contains some of the key milestones and tentative timelines on when some key activities will be completed including expression of interest and commitments by potential shareholders. As we target to have the company fully incorporated by end of April, we are also engaging a consultant to develop a detailed business plan which will enable potential shareholders to do appraisals in order to make informed investment decisions. We sincerely hope you

will join hands with us in order to complement Government's efforts in realizing our objective to support provision of affordable housing in our country.

18. **Finally**, I want to thank KBA and SASRA for partnering with the National Treasury in coordinating this meeting. I also wish to commend all of you for joining us on this important occasion. I look forward to your support and financial commitment towards this initiative.

Thank You/Asante!

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