Editorial: Finance and shelter improvements

DIANA MITLIN

Lending to low-income households for shelter improvements, to allow them to buy or build their own homes, has had a bad press recently as the full consequences of sub-prime lending have been felt in the US financial markets and, as a result of the scale of their impact there, in the global capital markets. However, experiences across Southern towns and cities demonstrate that loan capital can provide a critical contribution to improved shelter and livelihood strategies. The papers in this volume of *Environment & Urbanization*, as in the previous volume, provide multiple examples that demonstrate two lessons from experience. The first is that financial markets can contribute to improving the well-being of low-income households. The second is that this contribution is not inevitable but is achieved through a careful reflective design process that takes account of the particular circumstances of the target group and the vulnerabilities that they face. Perhaps a further emerging lesson is that lending to the poor does not have to threaten the stability of financial markets, but can help to strengthen economies through encouraging savings and developing good lending practices.

What is the sub-prime crisis? In the United States, lenders have sought to reach those low-income households that were seen as risky by the conventional mortgage providers. They have done so by creating an expanding sub-prime market – lending at higher interest rates to those families considered to be high risk because of low incomes and/or poor credit records. In some cases, lenders have been accused of deliberately encouraging default through high-cost loans to very low-income households, but it is not clear that such abuse was widespread. In most cases, the lenders simply sought to secure their profits through the repayment of loans rather than secure the housing asset through default, as lenders benefited from the interest rate premium that they charged these low-income clients. However, as the sub-prime market has moved into crisis it is evident that there are real issues of affordability, with many loans being taken by families who now find themselves struggling to manage repayments, in part because these mortgages had a repayment structure that offered low rates for the first few years. In the US, the sub-prime lending market was virtually unknown 10 years ago, but now accounts for just over 20 per cent of US mortgages.[1] The affordability problems are demonstrated by the fact that sub-prime loans are responsible for 55 per cent of foreclosures (repossessions). In December 2007, *The Economist* estimated that sub-prime mortgage borrowers in the US might default on US$ 300 billion of loans (about one-third of current US sub-prime debt).[2] In the UK, sub-prime lending now accounts for about 8 per cent of UK mortgages, but sub-prime lenders are responsible for more than 70 per cent of all repossessions.[3]

Meanwhile, financial intermediation, which appeared to be adding to the achievement of well-being and prosperity by providing additional capital to markets, may have encouraged lenders to take excessive risks. Mechanisms such as securitization and mortgage-backed derivatives were intended to add value to the market, leading to greater financial wealth through more precise packaging of assets and the delineation and spreading of risk.[4] By December 2007 they had failed,

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1. Schifferes, Steve (2007), "Foreclosure wave sweeps America", 5 November, accessible at www.bbc.co.uk.

2. *The Economist* (2007), "Postcards from the ledge", 19 December, accessible at http://www.economist.com/opinion/displaystory.cfm?story_id=10334574.

3. Chapman, Matthew (2007), "Sub-prime borrowers face repossession", BBC Panorama, 8 October, accessible at www.bbc.co.uk

4. Securitization is the packaging of a flow of future income into a capital asset (a security) for trading. In relation to mortgage finance,

the complexity of these financial mechanisms adding to the nervousness of markets as those responsible for operating the complex structures find other financial institutions and themselves confused about just who is solvent and who is not. In the face of such uncertainty, individual institutions are choosing to do nothing and have avoided lending. Such systemic failures among lending and investment institutions have been added to by rating agencies, who have followed their clients' interests rather than their professional expertise in valuing organizational risk. *The Economist* summarizes the current position thus:

> "Risk was supposed to be bought by those best able to afford it, but often ended up with those seduced by yields they did not understand. Mathematical brilliance was supposed to model risk with precision, but the models evaporated along with the liquidity that they had failed to quantify. Rating agencies were supposed to serve the market, but their first loyalty seems to have been to the issuers who were paying their fees."(5)

The scale of the disaster is such that governments have felt forced to intervene to prevent a global recession. In December 2007, central banks agreed to provide US$ 500 billion of loan finance to ensure that banks had the liquidity they needed and to prevent the reluctance of financial companies to lend to one another from catalyzing a global recession. However, there remained considerable fears that huge losses were still to be declared by the financial sector and that their shares would subsequently fall in value. Just one month later, in January, the Federal Reserve substantively cut US interest rates to signal to markets that it would do whatever it takes to boost expenditure and prevent recession.

What is clear is that the costs of speculative profit-oriented behaviour by sub-prime lenders are potentially high; and that many of these costs are being paid by citizens, through government budgets. However, the conclusion should not be that lending to low-income families is high in risk or mistaken. Rather, the lesson is that poorly regulated financial markets will take potentially expensive risks for speculative private benefits. As noted above, there are many examples showing that financial markets are relevant to low-income households, and that improved access to financial services offers benefits to both borrowers and lenders. In the last issue of *Environment & Urbanization*, we included a wide range of papers illustrating some of the approaches that have been used. Because of the scale of interest and activity in this area, we are continuing with the theme in this present issue.

As illustrated in this and the preceding volume of *Environment & Urbanization* and in many other publications, access to financial services is important to low-income households, helping them to increase their development options and reduce future vulnerabilities. Core financial services are savings and loans. Many of the papers emphasize the importance of savings, both for its immediate benefits and as a preparation for borrowing. Savings is often a first, and sometimes the only, service that is required. The practice of putting away resources for the future is a common individual and household activity, to minimize future risk and allow for the accumulation of resources. Savings reduce vulnerabilities by providing resources that can be used in emergencies; they also help households to spread income across productive and less productive periods. Savings is also a preparation for borrowing in several ways: they help accumulate required deposits; they enable households to see what they can afford to set aside for loan repayments; and they build up solidarity between members of a collective finance scheme. Loans help households to accumulate assets, paying for goods at the same time as they benefit from the services that they secure through owner-ship. Institutions that help individuals and households to save offer them the option of accumulating their own cash rather than taking

this involves the packaging of mortgages for sale. Selling individual mortgages incurs high transaction costs and is seen as risky, hence the on-sale of mortgages is only feasible once they are brought together into bundles. Mortgage companies sell such bundles on financial markets to obtain further finance for new mortgage borrowers. In this context, the availability of mortgage finance is linked to the ease with which packages of mortgages can be sold to investment companies and other financial institutions, which are purchasing the mortgages to benefit from the stream of repayment income. Derivatives are tradable securities whose value "derives" from the actual or expected price of some asset, in this case the mortgage bond/loan; many are concerned with assets that earn future income. Hence, the sale of mortgage-backed derivatives involves the sale of the (future) value of the mortgages. Derivatives have been viewed as allowing for better risk management, as investors can buy assets that will bring them future income, perhaps offsetting more risky present investments.

5. See reference 2.

on the risk of borrowing; moreover, regular savings can also help households prepare for loan repayments.

Despite the evident benefits of and interest in such financial services, low-income households in the North and South have struggled to find modern institutions that are responsive to their need to save and borrow. The recent growth in lending to low-income households is unusual. In many low-income areas, there are no banks. Where there are banks, at best they are not interested; at worst they are anti-poor, refusing entry to those without smart clothes, formal employment or other high-income/high-status indicators. As Solo describes in her study of the "unbanked" population in Colombia and Mexico:

> "In both the Colombian and Mexican surveys, the primary reasons given for not using banks or formal sector institutions were insufficient resources, high charges and mistrust of, or discomfort with, banking institutions."

She stresses that people want access to bank accounts and that multiple consequences arise from a lack of access, including difficulties in saving, and problems and/or additional costs in making payments and sending and receiving money. A further and widely recognized problem is that the costs of borrowing in informal loan markets are generally much higher than from formal financial institutions.

A further problem is that the market in finance, as in other goods, responds to scale; the best deals are available to those with the most money. Small levels of savings may attract only low returns, while small loans may have high administration costs attached to them. Solo also describes some of the ways in which new technologies are helping to reduce the relatively high transaction costs associated with small quantities of money.

In the last two decades, however, institutional innovation has been more significant than technological innovation. First microcredit and then microfinance agencies have emerged to reduce the costs faced by the poor as a result of the reluctance of formal financial institutions to service low-income households. Following initiatives such as the Grameen Bank, a range of NGOs and specialist agencies have developed increasingly complex programmes to provide financial services to low-income households. Since they have demonstrated the potential of this market, commercial companies have been increasingly interested in replicating their efforts.[6] While the expansion of microfinance has increased access to enterprise loans, lenders have struggled to deal with shelter-related lending, partly because longer loan periods are required, even for an incremental housing process. More recently, there has been interest in expanding into housing, as a number of initiatives have demonstrated that it is possible to enter this market successfully with a particular concentration of households with relatively secure tenure seeking finance for upgrading.[7]

Contributions to this issue consider ways in which finance (often, but not exclusively, loan finance) has helped families and communities improve their shelter and/or livelihoods and create new development options for them. In a context in which poverty is frequently defined by lack of income, it is almost self-evident to say that finance is a critical means to reduce poverty and improve inclusion. Small loans, as already noted, may be used to build up enterprises;[8] as important, it has been recognized that housing investment may help to increase tenure security as informal neighbourhoods consolidate and more closely resemble formal areas.[9] Savings[10] may be a preferred source of investment funds for water and sanitation by some low-income women. The potential for local income to support individual well-being and collective improvements is highlighted by an analysis of the financial model of Orangi Pilot Project and associated programmes.[11] Small quantities of

6. See Escobar, A and S R Merrill (2004), "Housing microfinance: the state of the practice", in F Daphnis and B Ferguson (editors), *Housing Microfinance: A Guide to Practice*, Kumarian Press Ltd, Bloomfield, pages 33–68 for a discussion of such interest in the case of Latin America. More recently, ICICI bank in India has also been actively exploring how to enter this market.

7. See reference 6, Daphnis and Ferguson (editors) (2004); also Cain, Allan (2007), "Housing microfinance in post-conflict Angola. Overcoming socioeconomic exclusion through land tenure and access to credit", *Environment & Urbanization* Vol 19, No 2, October, pages 361–390; and Mills, Sophie (2007), "The Kuyasa Fund: housing microcredit in South Africa", *Environment & Urbanization* Vol 19, No 2, October, pages 457–470.

8. See Brook, Hillyer and Bhuvaneshwari in this volume.

9. See Hasan in this volume.

10. As discussed in Muller, Anna and Diana Mitlin (2007), "Securing inclusion: strategies for community empowerment and state redistribution", *Environment & Urbanization* Vol 19, No 2, October, pages 425–440.

11. See Hasan in this volume.

external capital have provided technical assistance to households organized into lane committees, technical assistance (of a different kind) to state agencies and, in some cases, very small capital funds to communities. The approach has drawn in hundred of thousands of households to invest in improved infrastructure (at less than US$ 50 per household), generally financed through savings and income.

What is notable about these papers is that finance is considered as much more than simple monetary transfers. The authors, from varying perspectives, consider how access to finance (in various forms) can lead to behavioural changes among individuals and families, to new community capacities, and to attitudinal changes among formal agencies. These factors change individual and collective actions and result in new outcomes within low-income settlements; also, new kinds of relations are established with local government and other agencies, catalyzing and strengthening a process of pro-poor change. Equally notable is that, irrespective of the present crisis in global financial and stock markets, this set of papers is broadly optimistic about what can be done to address shelter poverty and/or improve livelihoods.

The programmes reported in this issue of *Environment & Urbanization* range from income generation in India to building materials banks in Argentina; they include initiatives that have addressed the needs of a few hundred households and those that have reached across nations. Some key points emerge regarding the delivery of financial services to low-income groups to address inadequate shelter and/or livelihoods. In drawing out these emerging lessons, I am not trying to simplify a complex set of interventions or to make over-reaching generalizations. I am arguing that the conclusion to draw from the sub-prime lending crisis is not that low-income households cannot afford shelter loans, or that the financial system cannot afford the risks of lending to the poor but, rather, that carefully considered programme design that involves the perspectives of beneficiaries is critical if lending is to be in the interests of low-income households and hence built into a stable economic system that offers development opportunities to all. As argued in the introduction to the last issue, beneficiary (savings), public and private finance can all contribute to improved outcomes. Risks and vulnerabilities need to be carefully considered and taken into account in the design. In this process, no-one has more at stake than the low-income households themselves, and their need is for finance that assists them to address household needs and that supports the stability and growth of the economies in which they are located.

The importance of housing microfinance – small-scale lending for housing improvements – is evident in several of the contributions here (as in the last issue). Stein and Vance summarize financial innovations in a number of Central American countries, including Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua. Almansi and Tammarazio offer a detailed historical analysis of a fund that emerged from a housing materials bank established in a low-income settlement on the periphery of Buenos Aires (Argentina). The authors stress the importance of finance in assisting residents to improve their dwellings, and discuss the success of the initial activities in drawing in state monies at a time when housing microfinance became a recognized approach in Argentina. While these papers discuss specialist shelter-related programmes, in other cases lending for housing has emerged from enterprise-oriented microfinance activities. Brook, Hillyer and Bhuvaneshwari present an assessment of a microfinance intervention in six villages in peri-urban India and discuss how the programme was established and what benefits have accrued. Stavrakakis with McLeod and Francis discuss another example from India, of a network of self-help savings and loan groups that has structured itself to use capital effectively and link to the formal financial sector to raise additional capital. The authors explain how additional guarantees were required to enable larger loans for housing and infrastructure from banks, although the scale of financial activity enabled the groups to negotiate good terms from the banks for core financial services.

Stein and Vance, in their reflections on previous housing programmes in the area, highlight the mixed results from private sector involvement in housing programmes. In El Salvador, the housing policy resulted in an increase in the production of cheap, affordable and completed small housing units known as *urbanizaciones*, constructed by private builders in areas relatively far from the centre of main cities in El Salvador. These settlements became extremely violent

places, plagued with crime and juvenile gangs. One hypothesis is that this occurred:

> "…because the housing units, backed with mortgage state finance, were purchased by formal sector workers and, in most cases, both parents had to leave their children unattended during working hours. By contrast, unserviced plots of land that were sub-divided by private owners (*lotificadores*), and sold either for cash or rental with a sales option to formal and informal sector workers who built their own housing units, consolidated more rapidly and became more secure neighbourhoods. In this case, no state funds were available and the private land developer loaned money to the families for land and building materials."

As is the case with sub-prime lending, this quote illustrates that the capacity of the private sector to act in the broader public interest is limited. There is no reason why profit-seeking behaviour should address wider social needs, although, as also indicated by Stein and Vance's analysis, this may be the outcome. Private sector contributions to shelter improvement need to be managed (either regulated and/or negotiated) if they are to make a positive contribution to supporting low-income settlements and low-income shelter.

This is further evident through support for incrementally built housing, where a simple structure is improved by small multiple investments over a period of time. As Greene and Rojas explain, incremental housing, long recognized but inadequately supported, has a critical contribution to make as its financing requirements are a close fit with the financial constraints of low-income households. Once more, the position of the private sector is likely to be varied; suppliers of building materials will benefit from the increased demand for materials but, as suggested by Stein and Vance, the larger-scale construction companies may resist support for incremental housing and argue that addressing shelter needs requires "*…new housing solutions rather than improvements*." Hasan, reflecting on the experience with bulk infrastructure investments in Karachi, also highlights the difficulties of working with commercial engineering firms that design expensive complex systems that involve unnecessary expense and that do not fit well with community investments. However, the project works with a range of local, generally informal, commercial companies.

The experiences with microfinance discussed here, as with Allan Cain's account of new programming initiatives in Angola,[12] highlight the positive relationship between livelihood-related investments and shelter improvements. Struggling with multiple demands on scarce incomes and conscious of present and future vulnerabilities, households face difficult choices between potential income gains (microenterprise-related borrowing), expenditure savings (through investments in improved services), investments in capacities and relations (marriage-related expenditure, education) and investments in assets (housing). As is widely recognized by professionals working closely with low-income households and by microfinance agencies themselves, household heads reallocate money from one area to another as needs, experiences and perceptions change. Brook, Hillyer and Bhuvaneshwari report on the diversity of uses to which small loans were allocated in the case of the microfinance programme that they researched. Such information shows that reducing risks and managing opportunities at the household level requires flexibility; programmes that offer only limited borrowing opportunities need to recognize that the lack of loan opportunities may add to budgeting difficulties as, for example, obligations in relation to housing loan repayments increase without improvements to incomes.

What is also evident is that there are very real limits to the improvements that can be achieved if the state does not contribute finance and, in some cases, amend policies to make them more favourable to shelter improvement. In addition to a positive policy orientation and regulatory capacity,[13] there is a role for poverty reduction funding. One notable aspect of this collection of papers is the frequency with which state financial contributions are mentioned. Almansi and Tammarazio discuss Argentine government programmes to increase the availability of capital for housing microfinance, support regularization of tenure and the extension of public infrastructure, and enable the unemployed to undertake community work. Stavrakakis with McLeod and Francis report on the significance of the National Bank for Agriculture and Rural

12. See reference 7, Cain (2007).

13. See Greene and Rojas in this volume.

Development (NABARD) programme in India, which promotes links between rural self-help groups and commercial banks. Stein and Vance (in the context of Central America) discuss national and local government contributions to urban upgrading. Jones discusses a social protection programme to enhance the incomes of the most vulnerable households in Peru, while Muller assesses the policy of the South African government to provide free basic water to its population. The issue, in these contexts, appears to be as much related to how government finance is allocated as to whether or not it is available.

State funding for these activities is related primarily to poverty reduction objectives. As Muller elaborates, the free basic water policy was developed to achieve multiple goals, but one was the desire to find a strategy that enabled all households to benefit from water supplies. He suggests that there has been some success but highlights the need for local government as well as national government to develop the necessary capacities and priorities. His conclusions illustrate some of the real dilemmas that governments face once they have committed themselves to a process of social inclusion and poverty reduction; what is an acceptable outcome in terms of reaching low-income households, and how can finance be used to greatest effect? The priority given to inclusion is also highlighted in the contribution by Brook, Hillyer and Bhuvaneshwari in their analysis of the impacts of a microfinance intervention. The authors suggest that the results of the intervention are somewhat inconclusive; low-income families are, in general, neither under- nor over-represented as members and users of the financial services. However, this might be considered a positive result in the light of other evaluations of microfinance interventions that suggest that they tend to service the financial needs of higher-income households among the poor.[14] Moreover the authors report that:

> "In an independent impact study[15] of the project discussed here, it was found that between 2001 (before project) and 2005, mean household saving of poor SHG members increased by 647 per cent (from Rs 305 to Rs 2,278), while for non-poor, the increase was 126 per cent (from Rs 4,229 to Rs 9,547)."

At least some households have made the most of their new opportunities to accumulate money by significantly increasing their savings.

Inclusion is also sought through the Peruvian social protection programme described by Jones, which requires participation in health and education programmes if the households' funding is to continue. In this case, the finance is provided as a supplementary income to women in targeted households. Successes have been noted in respect of increased child participation in school, better nutrition, changed gender relations within the household, and demonstrated popular support. However, there are some indications that the programme is divisive, resulting in a new form of exclusion:

> "…(the) targeting process has had a less positive impact on community dynamics. In a context of general poverty, when some families are included and others not and there is insufficient clarity about the reasons for this, the introduction of the programme has generated feelings of sadness, resentment and anger among some community members."

The paper by Patel and Arputham discusses another aspect of inclusion. In this case, the focus is related to the rights of those living in low-income settlements with ambiguous legal and/or illegal status to be involved in plans for the future development of the city, and to have the quality of their homes and neighbourhoods prioritized within redevelopment programmes. A sole focus on household well-being may overlook the issues of neighbourhood quality highlighted earlier in the quote from Stein and Vance. In the case of Dharavi (India), this well-located site is home to tens of thousands of households and businesses. Redevelopment is highly profitable due to its location, but how should the benefits of redevelopment be shared? Articulating an alternative vision for the city of Mumbai to that proposed by the state and would-be developers, Patel and Arputham argue that lower profits should be accepted in return for a lower-density development. They suggest that a preferred option would

14. See Malhotra, M (2003), "Financing her home, one wall at a time", *Environment & Urbanization* Vol 15, No 2, October, pages 217–228 for a discussion of the income group being reached by housing microfinance initiatives.

15. ITAD (2005), Final Technical Report, NRSP Impact Assessment Case Studies – PU Suite 1, PD 138, Report to DFID, London, 123 pages.

be *"…ground-plus-three (four-storey) or ground-plus-four (five-storey) buildings instead of high rises."* *"…**We feel that enabling huge profits for the developers and huge revenues for the government of India should not be the main purpose of the project**."* (original emphasis)

After a period of lobbying and campaigning, some movement has recently occurred in the government's stance, and a period of information gathering is now ongoing with the expectation that as the plans develop they will take greater account of the perspectives and aspirations of residents and have accurate information, including details of the numbers of people and businesses occupying the land at present.

This last contribution returns to our starting theme. There is no reason to believe that the market will act in the interests of the poor; market outcomes favour the interests of those with capital who are in a position of power. In addition to the impact on individual households, its consequences for districts can be disastrous; the BBC reported on 5 November 2007 on some of those consequences, when it explained that:

> "Cleveland, Ohio …is the sub-prime capital of the United States. One in 10 homes in the city is now vacant and whole neighbourhoods have been blighted by foreclosed, vandalized and boarded-up homes."[16]

In this case, the impact of the financial sector's lending policies has had negative impacts on residential neighbourhoods, in addition to causing difficulties for individual households, due to the intensity of lending practices and associated vulnerabilities.

The power of the financial market institutions has been demonstrated by government actions in recent months; the financial market is considered to be too important to abandon to market forces. Governments are acting now to increase stability in the financial system and minimize economic consequences. In Dharavi, local residents are also vulnerable to the investment decisions of private capital seeking, in this case, to develop a new city on the site of a low-income settlement, Asia's so-called largest slum. As the authors demonstrate, it is through being organized and making alliances that the citizens can hold government to account for its management of the situation, including the potential benefits to developers. Collective action is a route towards identifying, understanding, analyzing and acting to create development options that are not available to individuals acting alone.

16. See reference 1.

What remains extraordinary is the democratic deficit in respect of the financial sector. Despite the significance of the financial sector, recent events highlight that financial institutions have been allowed to make choices with negative consequences for households, neighbourhoods and economies, and regulatory agencies have failed to check their activities and hold them to account. As demonstrated here and in many other publications, while practice is far from perfect, there is a body of knowledge about successful lending to low-income households, both generally and to improve shelter. What is notable is that it was not taken into account. The following concluding paragraphs argue that some programmes have managed to extend financial services in ways that are, in aggregate, beneficial to low-income households and that offer systemic benefits.

These programmes clearly demonstrate that it is possible to lend to low-income households. It may not be possible to reach every household, and it is unlikely that everyone has benefited, but numerous households have used savings facilities and some have taken loans, repaid these loans and continued borrowing. Broadly speaking, the experiences emerging from the papers included in this issue and the previous issue are ones of measured success.

As the microcredit sector discovered in its transition to microfinance – that lending alone rarely helps those with low incomes, and what does not help the households does not work for the lender due to subsequent defaults. This simple conclusion seems to have been ignored in the case of sub-prime lending, when risk assessment almost seems to have been reduced to the interest rate premium rather than a more measured consideration of whether or not the loan was likely to be repaid successfully. By making sure that the provision of financial services, including lending practices, works for the households that take up these services, the programmes described here offer individual and collective benefits. For households, these programmes contribute by offering savings facilities and small loans. For the financial sector, the experiences offer new strategies for potentially viable commercial lending. There are indications

of increasing commercial interest, suggesting that although profits per household may be small, the potential scale of the market offers some attractive investments for formal financial institutions. For the general economy, the programmes contribute by increasing savings and ensuring that savings capital is more easily circulated, thus increasing the availability of loan capital. Lending mechanisms are designed to reduce the risk of non-payment by households and, in so doing, reduce the risk of large-scale default. Neither is this easy, and there are potential problems particularly if general economic conditions fall sharply; for example, Almansi and Tammarazio discuss the consequences of the Argentine economic crisis of 2000 for fund management. However, focusing on reducing household default risk has obvious benefits for the financial markets, rather than the more complex management of increased risk, which appears to have been the sub-prime strategy.

The multiple economic benefits of supporting the development of low-income settlements have long been recognized. In addition to the direct benefits to households, investments in local infrastructure and upgrading of households help to strengthen local economic development, drawing more customers into the area and ensuring that local incomes circulate within the neighbourhood economy through increased local buying and selling. The interest in supporting this work, shown by both the state and the private sector, is a testament to its ability both to address social development goals and to do so in ways that work for the financial markets (at least in some cases).

Both community level savings and loans and sub-prime lending are complex, but there are significant differences in the type of complexities. The complexity that relates to savings and loans activities as they have developed within the community sector of the South lies in the diversity of investments and in the negotiated relationships between different sectors (local and national government, formal and informal market providers, civil society organizations such as residents' associations and NGOs). In the sub-prime market, complexity is embedded within a more narrowly defined sector, with vertical (e.g. retail to wholesale banking) rather than horizontal relationships, and complex tools and mechanisms. The sub-prime market is clearly in crisis and the remainder of the financial sector is struggling to cope with the fall-out. State measures to reduce insecurity and anxiety seem to be bent on maintaining the existing model (albeit with a slightly higher level of financial exclusion), without any more substantive consideration about whether or not it is really effective in addressing shelter needs. The alternative model of community-based savings and loans is growing in confidence and credibility but remains too small and too specialized with, in many cases, a lack of capital. Professionals, agencies and other institutions make choices about which sectors to invest in and which options to explore. What seems to be important is to encourage debate and awareness about the choices that are open to states and citizens in terms of extending financial services and building investment capacity; we hope that this issue of *Environment & Urbanization* will contribute to this process.

CITIES, RISK, DISASTERS AND CLIMATE CHANGE – A NOTE FROM THE EDITORS

The April 2007 issue of *Environment & Urbanization* on "Reducing risks to cities from disasters and climate change" generated many new paper submissions. Five papers on this theme are included in this issue and several more will feature in the October 2008 issue, including papers by Debra Roberts on institutionalizing climate change in Durban (one of the few cities in Africa to have taken adaptation seriously), and by Sheridan Bartlett on the risks facing children in urban areas from climate change and what a child-focused adaptation would involve.

Environment & Urbanization will continue to cover issues related to climate change and cities, with an emphasis on adaptation and on low- and middle-income nations, as this is a subject to which inadequate attention is given (as was recognized by the IPCC's Fourth Assessment).[17] As yet, the levels of risk that climate change is bringing or will bring to low- and middle-income

17. Wilbanks, Tom and Patricia Romero Lankao with Manzhu Bao, Frans Berkhout, Sandy Cairncross, Jean-Paul Ceron, Manmohan Kapshe, Robert Muir-Wood and Ricardo Zapata-Marti (2007), "Chapter 7: industry, settlement and society", in Martin Parry, Osvaldo Canziani, Jean Palutikof, Paul van der Linden and Clair Hanson (editors), *Climate Change 2007: Impacts, Adaptation and Vulnerability*, Contribution of Working Group II to the Fourth Assessment Report of the Intergovernmental Panel on Climate Change, Cambridge University Press, Cambridge and New York, pages 357–390.

nations, and the very serious constraints on their capacity to adapt, are not receiving the attention they deserve. In part, this is because of the naivety of the technological optimists, who see the range of new technologies that could underpin a transition to a low-carbon economy (and de-link prosperity from high greenhouse gas emissions) and assume that these will be implemented. In part, it is because many international agencies want to establish their stake in this field – and over-promote their knowledge and their capacity to support adaptation. This, in turn, is often exacerbated by politicians in high-income nations who are committed to climate change issues but fail to understand the national and local political and institutional constraints on adaptation and the very poor record of most aid agencies and development banks in building local development capacity. Capacity building may figure strongly in the annual reports of most international agencies but this does not mean that they actually have the capacity or the institutional structure to support adaptation in the particular localities that are facing the most serious risks.

As the editorial in the April 2007 issue emphasized, urban adaptive capacity depends so heavily on the competence, capacity and accountability of local governments, including their capacity to work with low-income groups in reducing risks from the direct and indirect impacts of climate change. It also depends on having in place the protective infrastructure for extreme weather and water supply constraints that serve all groups. This makes adaptation a development issue – yet most governments and international agencies still see adaptation as an environmental issue and have been slow to consider the developmental importance of climate change.

For many cities, adaptation is also a disaster preparedness issue and as such needs to call on the knowledge and experience of the "disaster preparedness" community of scholars and activists who have transformed our understanding of what causes disasters and the extent to which "natural" disasters are preventable (because the actual disaster is so much to do with inadequate planning and infrastructure and lower-income groups having no alternative but to live in high-risk areas). It is surprising that they have not had a more central role in adaptation, given how much they can contribute to understanding the possibilities and constraints on adaptation that reduces risks from disasters. In addition, climate change experts in high-income nations have tended to focus more on reducing greenhouse gas emissions, so adaptation has received less attention than it deserves, especially for the low- and many middle-income nations where adaptation is more urgent.

This issue of *Environment & Urbanization* includes papers on: climate change and human health in Asian cities by Sari Kovats and Rais Akhtar; climate change, flooding and the urban poor in Africa by Ian Douglas, Kurshid Alam, MaryAnne Maghenda, Yasmin McDonnell, Louise McLean and Jack Campbell; a climate change adaptation and mitigation agenda for Indian cities by Aromar Revi; and a case study of climate change risk for Mombasa by Cynthia Brenda Awuor, Victor Ayo Orindi and Andrew Ochieng Adwera.

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