

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

DOMINICAN REPUBLIC

**MULTI-PHASE LOW/MODERATE INCOME
HABITAT PROGRAM**

(DR-0141)

LOAN PROPOSAL

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BASIC SOCIOECONOMIC DATA

The basic socioeconomic data for Dominican Republic available on the Internet at the following address:

<http://www.iadb.org/RES/index.cfm?fuseaction=exteranllinks.countrydata>

INFORMATION AVAILABLE IN THE FILES OF RE2/FI2

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ABBREVIATIONS

BNV	National Housing Bank
CNVE	National Council for Housing
CONAU	National Council for Urban Affairs
DR	Dominican Republic
ESMP	Environmental and Social Management Plan
GODR	Government of Dominican Republic
HUD	U.S. Department of Housing and Urban Development
IDB	Inter-American Development Bank
IMF	International Monetary Fund
INVI	National Housing Institute
MES	Monitoring and Evaluation System
MIF	Multilateral Investment Fund
SISEG	IDB Operations' Monitoring System
TC	Technical Cooperation
USAID	U.S. Agency for International Development



Inter-American Development Bank
Regional Operations Support Office
Operational Information Unit

Dominican Republic

Tentative Lending Program

2004

Project Number	Project Name	IDB US\$ Millions	Status
DR0159	Sustainable and Protection of Social Reforms	200.0	APPROVED
DR0151	Financial Reform Consolidation Sector Program	100.0	APPROVED
DR0141	Housing Program	37.0	
DR0150	Social Reform Program	105.0	
Total - A : 4 Projects		442.0	
DR0156	Public Investment Project strengthening Management	5.0	
DR0154	Enhancement of Superior Education, Science and Technology	34.0	
DR0157	Fiscal Modernization Program	5.0	
DR0143	Rehabilitation Historical Center Sto Domingo	10.0	
Total - B : 4 Projects		54.0	
TOTAL 2004 : 8 Projects		496.0	

2005

Project Number	Project Name	IDB US\$ Millions	Status
DR0142	Credit Global Program	30.0	
DR0127	Municipal Governments Development	30.0	
Total - A : 2 Projects		60.0	
TOTAL - 2005 : 2 Projects		60.0	
Total Private Sector 2004 - 2005		0.0	
Total Regular Program 2004 - 2005		556.0	

* Private Sector Project



DOMINICAN REPUBLIC

IDB LOANS

APPROVED AS OF JANUARY 31, 2004

	US\$Thousand	Percent
TOTAL APPROVED	2,507,790	
DISBURSED	1,916,561	76.42 %
UNDISBURSED BALANCE	591,230	23.57 %
CANCELATIONS	602,458	24.02 %
PRINCIPAL COLLECTED	786,376	31.35 %
APPROVED BY FUND		
ORDINARY CAPITAL	1,692,214	67.47 %
FUND FOR SPECIAL OPERATIONS	728,945	29.06 %
OTHER FUNDS	86,631	3.45 %
OUTSTANDING DEBT BALANCE	1,130,185	
ORDINARY CAPITAL	700,523	61.98 %
FUND FOR SPECIAL OPERATIONS	423,121	37.43 %
OTHER FUNDS	6,540	0.57 %
APPROVED BY SECTOR		
AGRICULTURE AND FISHERY	526,309	20.98 %
INDUSTRY, TOURISM, SCIENCE AND TECHNOLOGY	136,013	5.42 %
ENERGY	352,719	14.06 %
TRANSPORTATION AND COMMUNICATIONS	236,750	9.44 %
EDUCATION	253,677	10.11 %
HEALTH AND SANITATION	148,108	5.90 %
ENVIRONMENT	0	0.00 %
URBAN DEVELOPMENT	34,210	1.36 %
SOCIAL INVESTMENT AND MICROENTERPRISE	530,860	21.16 %
REFORM AND PUBLIC SECTOR MODERNIZATION	213,905	8.52 %
EXPORT FINANCING	20,296	0.80 %
PREINVESTMENT AND OTHER	54,943	2.19 %



DOMINICAN REPUBLIC

STATUS OF LOANS IN EXECUTION

AS OF JANUARY 31, 2004

(Amount in US\$ thousands)

APPROVAL PERIOD	NUMBER OF PROYECTS	AMOUNT APPROVED*	AMOUNT DISBURSED	% DISBURSED
<u>REGULAR PROGRAM</u>				
Before 1998	3	145,200	80,313	55.31 %
1998 - 1999	7	241,960	133,442	55.15 %
2000 - 2001	2	74,300	16,987	22.86 %
2002 - 2003	7	165,800	200	0.12 %
2004	1	200,000	148,000	74.00 %
TOTAL	20	\$827,260	\$378,942	45.81 %

* Net of cancellations. Excludes export financing loans.

MULTI-PHASE LOW/MODERATE INCOME HABITAT PROGRAM

(DR-0141)

EXECUTIVE SUMMARY

Borrower: The Dominican Republic

Executing agency: National Institute of Housing (INVI) and National Housing Bank (BNV).

Amount and source:		<u>Phase I</u>	<u>Phase II</u>
IDB: (OC)	US\$	37.0	63.0
Local:	US\$	4.2	7.2
Total:	US\$	41.2	70.2
Financial terms and conditions:	Amortization Period:	20	Years
	Grace Period:	4	Years
	Disbursement Period:	4.5	Years
	Currency:	Single Currency Facility US\$ Dollars	

The interest rate, credit fee, inspection and supervision fee mentioned in this document are established pursuant to document FN-568-3 Rev. and may be changed by the Board of Executive Directors, taking into account the available background information, as well as the respective Finance Department recommendation. In no case will the credit fee exceed 0.75%, or the inspection and supervision fee exceed 1% of the loan amount.

Interest Rate:	Variable
Credit Fee	0.25%
Supervision and Inspection:	0%

Objectives: The overall objective of the proposed program is to contribute to the improvement of the habitat conditions of low/moderate-income households through re-orienting public resources and expanding credit markets towards these income groups.

Description: The Program institutes a new approach to housing policy in the country, which redirects public support to lower income households through innovative and more cost-effective types of programs and investments. For the first time the National Housing Institute (INVI) will focus on providing urban services to poor neighborhoods as well as economical core units to low/moderate-income households. The National Housing Bank (BNV) will rediscount microcredits originated by first-tier lenders and directed to housing improvements. These new programs will be complemented by the creation of housing planning and policy making instruments, including a housing programs monitoring system and a unified beneficiaries register, destined to institutionalize the new policies and monitor effectiveness

of public resources applied in the sector. This constitutes the first of a two-phase Program intended to support and consolidate these new types of investment and approaches to housing policy.

The Program has three components: (i) New housing and infrastructure programs; (ii) housing policy instruments and reform; and (iii) institutional strengthening and support for program implementation.

New housing and infrastructure programs (US\$35 millions). This investment component will support three types of shelter projects directed to low/moderate-income households: (1) integrated neighborhood upgrading; (2) housing microfinance and (3) land development for core units.

Integrated neighborhood upgrading (US\$18.6 million) will finance a minimum package of infrastructure and social services to poor neighborhoods (with households earning below US\$300 per month) selected on a national basis, which includes water, sewage solutions, drainage, street paving, lighting and environmental protection and garbage collection. Social services include early childhood development, primary health services, complementary education and technical training, sanitary and environmental education. Land tenure regularization will be a part of the projects as appropriate. Investments per family have been limited to US\$2,800, including all related costs. In the first phase, neighborhoods have been selected mainly on the basis of their income levels and infrastructure deficits. Other requirements included sizes of neighborhoods and existence of community organization, among others. In total, this sub-component will finance the upgrading of about 10 neighborhoods with a total of 7,000 families.

Housing microfinance (US\$ 8.1 million). This sub-component builds on the rich organizational base of microfinance institutions in the DR, a portion of which have diversified into housing lending. These small loans range typically from US\$500 to US\$7,500 at market-rates for short terms (typically 1 to 5 years) for various types of low-cost housing solutions, including home improvement, expansion, and construction of a new core unit on a lot already owned by the low/moderate-income family or provided by government. Approximately one-quarter of these micro loans will complement the neighborhood-upgrading component by helping construct or improve a unit on the serviced and titled lot. This microfinance component will operate on a strictly commercial basis.

BNV will rediscount microcredits of qualified first-tier microfinance institutions and Savings and Loans. BNV will qualify these first-tier lenders using a series of prudential criteria including amount and experience of the institution's existing loan portfolio, capacity to

originate and service micro-housing loans, capital adequacy, and other financial indicators. These first-tier lenders will work directly with borrowers to originate and then service these housing microcredits, and will take the credit risk on these loans. This sub-component will finance approximately 4000 microcredits.

Land Development for Core Units (US\$8.3 million). This pilot project combines existing government-owned land with urban infrastructure financed by the Program to produce developed land, which will be sold to private developers under the condition that they build on it housing units costing up to US\$10,000. The core expandable units (of a minimum built area of 40 square meters) will be sold to moderate-income households. These households will have to provide a down payment of approximately 10% of the unit's total cost and secure a mortgage loan from a bank to finance the difference between the price of the house minus the US\$2,000 discount given by INVI (equivalent to an effective subsidy). INVI will designate government-owned tracts based on urban development and environmental criteria build the infrastructure and sell these parcels to private developers. In turn, these developers will build core expandable units, with bridge financing from private banks and sell them to the targeted moderate-income households.

Housing Policy Instruments and Reform (US\$1.3 million). The housing section reform component consists of support for new policy instruments and for modernization of INVI. The new policy instruments include: (a) a *Housing Policy and Evaluation Unit* that will generate and apply a vision for housing reform and monitor and evaluate government housing programs, including this one; (b) a *Unified Beneficiary Registry* to help Government account for the families granted subsidies in this and other projects; (c) development of a *regulatory framework* for housing based on the changes instituted in this Program, including the streamlining of development regulations and processes, particularly that for new subdivisions.

Support under the Program for modernization of INVI will consist of: (a) *institutional reorganization*, based on an Action Plan to be contracted to a private-sector firm experienced in organizational reform; (b) *rationalization of INVI's loan portfolio*, and partial transfer or sale; (c) *titling of properties* that INVI has sold to households without full legal title.

Support for Program Execution (US\$2.51 million). This component includes assistance for: (i) long-term consultants to support Program implementation during its three years of execution; (ii) monitoring, evaluation and auditing; (iii) supervision of INVI-sponsored projects under the Program; and (iv) strengthening BNV's capacity of to act as a second-tier financier of housing microcredits.

Bank's country and sector strategy:

The IDB Country Paper notes that “the central challenge facing the country’s development is not the absence of social policy, but rather the severe distortions and constraints that have frustrated sector policies and limited (its) effectiveness and sustainability”. In this regard, one of the strategic vectors of IDB support is “to expand the capacity of institutions to respond to social demands.” This Program is designed to carry out this goal in the housing sector, reorienting towards social priorities this important sector and supporting its key institutions.

Coordination with other Multilateral Development Institutions:

The Program supports the strengthening of INVI and BNV so that these organizations can effectively perform their functions as, respectively, coordinator of the housing sector and the second-tier financial institution. IDB has coordinated with other donors active in the DR including USAID, HUD, and the World Bank in working in the housing sector (par. 1.32)

Environmental/Social review:

This project will have a highly positive social and environmental impact through improving living conditions of the families benefited by its three investment components. A series of studies have measured the social and environmental impact of the sample of three neighborhood-upgrading projects as well as the pilot subsidy for new units, and have contributed to the development of an Environmental and Social Management Plan (ESMP) for the Program.

The ESMP, which will be used to evaluate each INVI-sponsored project under the Program, specifies: (a) environmental eligibility criteria for all neighborhood upgrading projects and land development for core units; (b) mitigation measures and environmental management plans with its respective costs, for all sample projects including land development for core units; and (c) community participation process through out the project cycle (in conceptualization, design, execution and environmental supervision and auditing). In addition, the program has: (i) developed a mechanism in the project cycle to ensure appropriate environmental due diligence of all investment projects; and (ii) incorporated appropriate measures to ensure correct institutional environmental capacity within INVI.

Benefits: The immediate impact of the Program will be to improve the housing conditions of 14,000 low/moderate-income households as follows: (a) infrastructure and community services improved for 7,000 families in 10 informal neighborhoods; (b) 3,500 units improved, expanded or built through housing microfinance; and (c) 3,500 new progressive house units built with support of the land development for core units component.

The Program, however, will have a systemic developmental impact beyond the immediate investment in four important respects: (a) the housing microfinance component will develop the credit market for low/moderate-income households; (b) the land development for new core units will move unused portions of government land on the urban fringe into private ownership, helping to build the assets of households, increase the efficiency of urban development of INVI; (c) the Program will focus resources on improving the habitat of poor and low-income households, with health and other social benefits; (d) titling of units developed in the past by INVI (currently lack full legal title) will stimulate private property rights of the beneficiary households and build their assets.

Risks: **Capacity of INVI and BNV.** INVI's experience in development strength gives the organization the capacity to execute the subsidy for new core units. During project preparation extensive resources were dedicated from the Technical Cooperation to train INVI staff in the two components under its responsibility. In addition, the Program provides long-term consultants to co-manage project execution with INVI. BNV has a relatively well-qualified staff but lacks some of the specialized financial skills and information systems necessary to fulfill its mission as a second-tier finance institution. The Program provides resources for one type of secondary finance market that for housing microfinance while a recently approved technical cooperation strengthens BNV's capacity for performing as a second-tier finance institution.

Governmental transition risk: Due to its timing the Program will span across more than one administration. Elections in 2004 will result in a new government taking charge in August who might reevaluate the basis of this operation. This Program has dealt with this transition risk in three ways. First, through the extensive preparation work that enabled the involvement of all of the relevant stakeholders among the private sector (finance and microfinance organizations, builders and developers, research institutions, architects and engineering associations), non-governmental organizations (involved with community work) and community level groups. This has generated both expectations for reforms and support for the new approach proposed by the Program. Second, INVI and BNV have committed resources to launch the three investment sub-

components (barrio upgrading, housing microfinance, and subsidy for new core units) on a pilot basis, which can be started in the last quarter of 2003 before the new government takes possession in August 2004. Thus, the operation will establish methods and begin to show results prior to the incoming Administration. Finally, the operation provides key support for its investments and reforms in steps staggered over two phases to allow for the gradual absorption of changes and the Bank's participation in its adjustment.

Sustainability of New Policies A risk related to the above is that of the continuity of the new policies and programs supported by this operation by a new incoming administration. This risk is mitigated by both the support gathered throughout the preparation process among key stakeholder in government, private sector and civil society, which assures the consensus on the continuation of new poverty-focused housing policy, and by the Program's two-phase strategy, which will enable the Bank to maintain an active dialogue with the government on sector's policy direction.

Macro-economic instability. The DR is currently experiencing considerable macro-economic instability resulting, in part, from a financial crisis. Prima facie, these difficulties might appear to reduce the participation of the private sector in parts of the operation (housing microfinance, and the subsidy for new core units; although the bulk of the Program's investment integrated neighborhood improvement-involves no credit finance). However, IDB experience in countries experiencing similar financial economic and financial difficulties shows that similar housing programs tend to work rather well in such circumstances, because they programs become one of the few options for business available to developers and financial institutions that normally ignore low/moderate-income markets. A recent update of market housing microfinance and the subsidy for new core units verifies that effective demand still far exceeds the Program's potential supply.

Special contractual clause:

Special conditions for first disbursement:

- a. Official enactment of the Program's Operating Regulations
- b. Agreement between the Borrower and INVI for program execution.

Other Special conditions:

- a. Prior disbursement of resources for the upgrading of a particular neighborhood (as part of the integrated neighborhood upgrading sub-component), entry into effect of a participation agreement between INVI and the corresponding municipality.
- b. Official enactment of the Credit Regulations and designation of a core professional team at BNV to operate the microcredit sub-

component are conditions for disbursement of this sub-component.

c. Prior disbursement of resources to any participating financial institution (microcredit sub-component), entry into effect of the participation agreement between the particular financial institution and BNV indicating terms and conditions for credit.

d. The hiring of the Environmental Specialist is a condition for first disbursement of the *New Housing and Infrastructure Component*.

**Poverty-targeting
and social sector
classification:**

This operation qualifies as promoting social equity because the bulk of the investment component finances slum upgrading, in accordance with the Eight Replenishment Document (AB-1704). The Program qualifies as poverty targeted since over 50% of the beneficiary families are below the poverty line for the Dominican Republic (par. 4.14).

**Exceptions to
Bank policy:**

None.

Procurement:

International competitive bidding will apply for: (i) construction contracts for works over US\$1,500,000; (ii) goods and related services valued over US\$250,000; and (iii) consulting services valued at more than US\$200,000. Procurement of goods, works and consulting services below these thresholds will be carried out in accordance with Bank procedures. The selection of consulting firms may be based on the price and quality method, provided that the weight allocated to price as a criterion does not exceed 20% of the total ranking.

I. FRAME OF REFERENCE

A. Socioeconomic framework

- 1.1 The Dominican Republic's economy experienced strong growth over the last decade, even though Hurricane Georges hit the economy hard in 1998. Although the country has long been viewed primarily as an exporter of sugar, coffee, and tobacco, in recent years the service sector has overtaken agriculture as the economy's largest employer, due to growth in tourism and free trade zones. The country suffers from marked income inequality; the poorest half of the population receives less than one-fifth of GNP, while the richest 10% enjoy nearly 40% of national income.
- 1.2 After a strong economic performance during 1992-2000, the Dominican Republic economy is currently facing a serious crisis. The country experienced a series of external shocks, starting in 2001, including a rise in oil prices and the September 11 events with the ensuing reduction in tourism. Additionally, the country faced a bigger shock in 2003 with the failure of a large private bank following revelations of fraud. The banking problems contributed to pressures on the peso and to a sharp rise in public sector debt. Economic activity has weakened and inflation was close to 40 percent in 2003, in annual terms, reflecting the weaker exchange rate. The authorities have launched a comprehensive program to strengthen the banking system, which included audits of most banks, reinforcing the legal framework for bank resolution, and strengthening prudential regulation and bank supervision. With a drop in consumer confidence and investment, economic activity was estimated to decline by 3 percent in 2003, after rising by 4 percent in 2002.
- 1.3 The combined Public Sector Debt has increased to around 52 percent of GDP, from around 26 percent in 2002, raising concerns about debt sustainability. To address these concerns, the authorities have taken a number of measures to contain the deterioration in the public finances, including expenditure cuts and increase in revenues a tax on checks, an imports surcharge, and other temporary measures. Further measures and reforms are envisaged for the coming months in order to contain the public sector deficit at 1.5 percent of GDP in 2004. Exports and tourism have recovered so far in 2003, and imports have fallen as a result of the downturn in the domestic demand and the sharp real depreciation of the peso. The external current account has shifted into a surplus of about 1 percent of GDP in the first half of 2003, from a deficit of 4 percent in 2002. The financial account has weakened sharply, despite the placement of a US\$600 million sovereign bond in early 2003; foreign direct investment has declined and there have been capital outflows. Net international reserves fell by about US\$65 million in the first half of 2003 bringing gross international reserves to around US\$500 million at end-June, or less than 1 month of imports. In 2004, private consumption and investment will remain depressed by the decline in real incomes and the financial crisis. On the assumption of a broad-based world recovery, tourism and free-zone exports will again buck the downward trend, offsetting the depressed state of domestic

demand. Credit will remain expensive and scarce and private investment will be crowded out by the government's large borrowing requirement. In 2005, the economy will return to positive growth on the assumption that the incoming government takes the necessary measures, particularly in respect of management of the public finances, to restore confidence, creating the conditions for a reduction in interest rates.

B. The sector

- 1.4 **Overview.** The housing sector in the DR presents some marked contrasts. Housing construction costs and median purchase prices¹ (around US\$9,000) are quite low relative to median household income (around US\$7,000). Hence, the ratio of median sales price to median household income is only slightly above 1, and is far better than that of virtually all other countries in the hemisphere.² Urban land is in reasonably ample supply in the suburban areas of the largest cities. In particular, the Government owns large amounts of former sugar land on the fringes of the main urban areas, especially Santo Domingo. The country's private-sector developers and Savings and Loan industry are strong.
- 1.5 Yet Government and the private sector have produced and financed housing almost exclusively for the highest income households – the 8th decile and above. For example, less than 20% of the housing solutions produced by the National Housing Institute (INVI) reach low-income households. Developers generally do not build for and Savings and Loans do not extend mortgage loans for low or moderate-income households (families earning below US\$800/month). The great bulk of the population remains left out, and informality is very high. Sixty-seven percent of households lack full legal tenure, including the overwhelming bulk of low/moderate-income families. Over two-thirds of housing production occurs outside building and planning regulations. Land invasions account for over 40% of settlement in urban areas, and informal settlement overall for 75%.
- 1.6 Low/moderate-income habitat problems in the DR come as much from the lack of urban infrastructure as from the shortage of houses or their poor structures. Studies (Angel, 2001; FONDOVIP, 2002) show that 32% of units lack adequate urban services, including safe water and sanitation services, drainage systems, access roads and street systems, garbage collection and others. This results in large tracks of under-serviced neighborhoods that concentrate the poorest segment of the urban population, mostly located in the fringes of the largest cities. For this growing segment of the urban population there are currently no housing or urbanization policies to assist them.

¹ All figures in US dollars are based on studies prepared until July 2003. Later devaluation of local currency may affect the current parity of these estimates.

² The median sales price to household income ratio is 3.1 in the U.S. (2002), and ranges from 4 to 7 in most Latin American countries.

- 1.7 Given these issues, a new approach in housing policy is required that redirects public support to both lower income households and to innovative, more cost-effective types of investment. Such policy should redirect the priorities of the National Housing Institute -INVI towards programs that assist these households in their more immediate habitat needs, such as the provision of urban infrastructure and services to poor neighborhoods, and towards low cost core housing.
- 1.8 **Housing demand and supply.** The annual urban population increase of 3.1%, represent the formation of 56,000 new households each year. The formal private sector has produced an average of about 12,000 units per annum over the last seven years, while Government has averaged 3,000 units per annum. The gap is filled by a variety of arrangements, including self-help construction, informal land occupation and construction, and overcrowding of existing homes. Typically a poor family either purchase a lot invade land and build their home gradually over 5 to 15 years. As Government and the private sector provide virtually no support to the incremental building process used by the low-moderate income majority, it often results in poor living environments. Hence, qualitative problems are just as important as new home construction in the Dominican Republic.
- 1.9 Bottlenecks in basic services in poor neighborhoods, housing finance, residential land, high standards, and institutional structure must be dealt with to meet this goal of reaching low/moderate-income households on a substantial scale.
- 1.10 **Poverty Issues:** Despite the important economic growth experienced during the 1990s, poverty in the Dominican Republic currently affects more than half of its population - an estimate that is expected to further increase as a result of the current economic crisis. According to recent estimates, 58.1 percent of the population lives in poverty while 14.6% live in extreme poverty.³ Higher levels of poverty are observed among women (16% of female-headed households live in extreme poverty) and children (over 50% of children under 4 are considered to be poor). An important number of the poor are located in rural areas, especially in provinces bordering Haiti. In general, the Dominican poor have larger families, lower level of education, less participation in the labor market, lower access to health and social services, and lower access to appropriate housing and basic services.
- 1.11 Poverty in Dominican Republic is *strongly correlated with deficient houses and lack of basic services*⁴. For instance, only 35% of the poor live in houses built with permanent materials compared to 63% of the non-poor, while 15% of the poor live in houses with mud floors. In terms of basic services, only 15% of households in the bottom decile have indoor sanitation compared to 87% in the top decile. Similarly, only 23% of the households in the bottom decile possess indoor running water versus 82% in the top decile. These figures indicate that

³ *Estrategia para la Reducción de la Pobreza en la Republica Dominicana*, Presidencia de la Republica, Gabinete Social, Oficina Nacional de Planeación, Santo Domingo, junio, 2003.

⁴ *Poverty Assessment Paper*, The World Bank, Washington, 2001.

- housing needs and lack of basic infrastructure are a useful proxy for poverty conditions and can be useful as a targeting tool.
- 1.12 Lack of access to physical assets – such as land and houses – further exacerbates conditions of vulnerability among the Dominican poor. The availability of housing for the Dominican poor is deeply restricted by the lack of affordable options. Current housing options offered by the formal sector - both public and private - are far beyond the reach of lower income urban households: only the top two income deciles of the population can afford the lowest-cost housing options offered by the private sector, while the cheapest options offered by the public sector (even if they include a subsidy) are only affordable by the highest three income deciles (Angel, 2000).
- 1.13 **Poor Informal Neighborhoods.** An estimated 2.3 million (FONDOVIP, 2002) of the DR's 8 million people currently live in poor under-served neighborhoods. These neighborhoods have been growing steadily over the last decade. Poverty is pervasive and indices of health and social problems are high. For example, overcrowding affects 38% of Dominican families and one-third lack at least one basic service, and indices are higher in these poorer areas. These poor neighborhoods are dense by Latin American standards⁵, and many households (21% of the total in the country; Angel; 2000) live in tenements. By and large, these areas lack adequate sanitation, drainage, accessibility and social or community facilities. Despite their prevalence there are virtually no programs at significant scale to address the need of poor informal neighborhoods.
- 1.14 **Mortgage finance.** The Savings and Loan System which started in 1962 makes the overwhelming bulk of mortgage loans. Eighteen Savings and Loans extend 90% of all mortgage loans at variable interest rates for terms of 20 to 30 years, and have low arrears rates - on average, under 2.5%. Although growing, the housing credit portfolio in the DR is still small in comparative terms. As of 2000, for example, outstanding mortgage credit of US\$635 million accounted for 13% of all credit, compared to 20% in Latin America as a whole. The number of mortgage loans increased from 3,700 in 1993 to over 9,000 in 2000. Nevertheless, the total number of mortgage loans outstanding (39,926 in 2000) covered only 2% of households. The average mortgage amount - around US\$30,000 - is affordable only to the top fifth of the income distribution.
- 1.15 Macro-financial problems and rising inflation – now at 30% per annum - and high deposit rates of close to 30% have resulted in mortgage lending rates of 25% to 36% per year. The prospects for reducing the high interest rates that have cut demand for traditional mortgage finance depend on medium-term fiscal and macro-economic stabilization. In addition, Savings and Loans and other housing lenders (commercial banks) require formal employment, good credit, and full

⁵ Overall population density in the DR is 9,500 people per square kilometer compared to an average of 5,700 in Latin American and the Caribbean as a whole (Angel, 2000).

legal title to qualify households for loans. In contrast, most low/moderate-income households fail to meet many of these underwriting criteria, and depend on low-cost housing solutions that require funding for the steps in the incremental building process. As the experience of similar IDB housing programs in other countries experiencing high interest rates and financial instability has demonstrated, the investment components of this Program offer attractive options for households, developers, and financial institutions when difficult macroeconomic conditions reduce demand for traditional mortgage finance and residential development.

- 1.16 **Housing microfinance.** Housing microfinance (HMF) small loans, at market rates, for short terms for low-cost housing solutions can help solve many of the problems of traditional mortgage finance. The DR is fortunate to have a large pool of financial institutions capable of meeting this demand (Lasa, 2003). These institutions include: (a) the top five microfinance NGOs (loan portfolio of US\$26 million in 2002); (b) the top two private MFI development banks (loan portfolio of US\$75 million); (c) 13 rural savings and credit cooperatives (loan portfolio of US\$109 million); and (d) a portion of the Home Savings and Loan Associations (loan portfolio US\$1.15 billion to reiterate that 2002), and two foundation established for these S and Ls to undertake HMF. The first three sets of institutions the microfinance NGOs, the development banks, and the rural Savings and Loans already conduct microfinance as their main business, and already lend modest amounts for housing. Of this total, eight institutions – two private development banks, one microfinance NGO, and four rural Savings and Credit Cooperatives with a loan portfolio of US\$210 million - are interested and capable of undertaking HMF on a much large scale, and will represent the first set of loan originators under the Program. Analysis projects that these institutions have the capacity to originate US\$10 million in 5,000 HMF loans (averaging US\$2,000) in the first 3 years of operation and US\$10 million in 5,000 HMF loans per annum latter on. It is important to reiterate that, the population segment to be attended is such that actually is not benefited from the regular banking credit.
- 1.17 The National Housing Bank BNV, the official second-tier finance institution of Government under the Monetary Code has launched a pilot second-tier facility for housing microfinance and extended liquidity for a small number 50 credits. In summary, the DR's strong micro lending infrastructure and these incipient efforts at building liquidity facility represents an important strength on which to build.
- 1.18 **Availability of land.** Government both national and local owns large amounts of land near urban areas in the Dominican Republic. The main Government housing agencies INVI and BNV have received substantial amounts of land from the State Sugar Council, which owns some 1,762 square kilometers within urban growth rings of cities. The amount of land currently managed by INVI has a value of roughly US\$55 million. Many municipalities also own significant amounts of land. This publicly owned land represents by far the largest Government resource for social housing in the Dominican Republic. Given the fiscal problems of

Government, in general, and of these housing institutions, in particular, public land will continue to be the main resource for social housing for the foreseeable future. Up until now, the land owned by INVI and BNV has gone mainly for middle and upper middle-income housing development, while the allocation method has been less than transparent. Channeling this land transparently for low/moderate-income households for core expandable units and other low-cost housing solutions holds key importance.

- 1.19 **Property rights and informality.** Roughly 75% of housing development occurs informally, outside the development approval process. Invasions are the principal means of low-income settlement. About 40% of the total population of the National District lives on invaded land. Although many households (60% in the National District; 75% in the country as a whole) say they own their home, most (67%) lack full legal title, including 90% of low-income households. The Program for Land Modernization (DR-0118) supported by IDB has worked with the agency of the Supreme Court in charge of the registry, cadastre, and other land measuring and recording functions to improve its operations with the objective of cutting times and lowering costs. In principle, the next step should be massive land titling. Nevertheless, the problems will not be solved easily. The charges and times for titling continue to be problematic, often costing US\$500 to US\$800 per family and involving a complex, lengthy process beyond the capacity and endurance of most low-income households. In addition, until recently, an anachronistic law has required INVI to transfer of units and lots it has built without accompanying full legal title, under the philosophy that these units represent a “family good” and should not be commercialized. This law has changed and INVI is now engaged in providing title to families living in projects it has developed in the past.
- 1.20 **Development norms, standards and processes.** Inappropriate development and building standards raise housing costs substantially in the DR. Most countries in Latin America and the Caribbean have adopted the concept of the core expandable unit of 25 to 40 square meters⁶ as a pillar of their social housing efforts and commercial private-sector production. Neither Government nor the private sector, however, produces such core expandable units in the Dominican Republic. The smallest units produced at significant scale exceed 60 square meters and most entry-level units are a minimum of 80 square meters. Infrastructure standards are also demanding, and the development approval process lengthy and cumbersome. Partly as a result, the least expensive commercially built house sells for US\$16,000, and is affordable only to households in the top 30% of the income distribution. Therefore, lower standards,

⁶ These small units are programmed for expansion horizontally or vertically to two to three times this size. The low cost of providing such a starter units translates into much greater production with a given amount of funding, and stretches infrastructure, other services, and land, thereby reducing costs further.

speedier processing and progressive housing solutions are key to reaching moderate-income households.

C. The country's sector strategy

1.21 The housing sector has suffered from institutional fragmentation and, until recently, limited policy direction. The main institutions in the sector and their principal activities are as follows:

1.22 **National Institute of Housing (INVI).** The President has designated INVI as the coordinator of the housing sector and the entity mainly in charge of executing the Government's housing policy. INVI's annual budget now US\$35 million is increasingly difficult to maintain. The greatest cash burden is INVI's program of completing on-going housing projects started by previous administrations. INVI contracts the building to the private sector and then originates a mortgage to sell the resulting units at below-market interest rates (10% fixed). INVI performs this construction management function competently. However, the institution's financial roles of origination and servicing loans are faulty, and household repayment on these mortgages to INVI is poor. A presidential decree requires INVI to sell or transfer its loan portfolio's administration. The institution has begun to clean up the problems in its loan portfolio, and has recently transferred the servicing of a quarter of its portfolio \$10 million to the Reserve Bank.

1.23 Despite the many drawbacks of INVI's direct production program, it represents virtually the only source of new formally developed housing for moderate-income households in the Dominican Republic. Substantial sums have also been spent on the existing housing projects now being completed under the direct new construction program. As a result, INVI's direct production activities can be phased down only as better approaches replace it and once the existing projects now being built have been completed. Another INVI program that involves providing land to stimulate private-sector development has much greater potential and - once reformed - can eventually replace INVI's direct production program by the end of the second phase. In essence, INVI sells raw parcels at rates below market to developers, who then build and sell units⁷ to middle-class families that receive purchase loans at market rates from private-sector financial institutions. Once reformed, a similar method could be used to produce core expandable units affordable to low/moderate-income households if joined with a modest expenditure to finance infrastructure on these parcels. This approach has great advantages over direct construction and finance of new units. Foremost, it costs INVI only one-fifth the amount per unit of its direct production program by leveraging the resources of the private sector. However, changes are needed to reduce the size of units, strengthen safeguards in beneficiary selection, and codify methods. This first phase of the proposed Program supports INVI to make these changes on a pilot scale, in order to expand to full scale in the second phase.

⁷ With price ceilings to reflect the subsidy received

- 1.24 **National Housing Bank (BNV).** BNV started in 1962 in order to finance construction and purchase of housing, particularly through acting as a second-tier liquidity facility to the Savings and Loan industry. Over its history, however, the main functions of the organization have been to operate a mortgage insurance program (called "FHA") which is now legally required for all institutional housing loans and as a developer of land received from Government to sell to builders for middle-income housing. BNV has also recently started a small pilot project to rediscount housing microfinance credits originated by first-tier lenders with its own funds. The Monetary Code law approved in late 2002 stipulates that BNV abandon the function of developer and focus on its primary role as a second-tier liquidity facility, not only for housing but also for other sectors. A TCL operation, recently approved, is currently in process to support BNV in this role as a second-tier financial institution.
- 1.25 **Advances in Policy Reform.** As the activities of the main housing organizations show, the Government's approach to housing until recently has consisted mainly of building and financing units directly. These units have largely gone to the middle-class rather than low-income or poor families. The Government has taken the fundamental decision to target low-income households and to transition towards facilitating and leveraging the resources of the private sector. Concrete policy and institutional initiatives have accompanied this decision. Presidential decrees have created the "Social Cabinet" (Gabinete Social) and the "National Council for Affordable Housing" ("Consejo Nacional de la Vivienda Económica" - "CNVE"). The Social Cabinet has made housing a pillar of its goal to reduce poverty by half by 2015. CNVE coordinates actions and programs aimed at private-sector development of low-cost housing solutions affordable to the majority. A recent Presidential Decree (#372-02) has re-affirmed INVI's role as the coordinator of the housing sector, emphasized serving low-income households, specifically authorized the institute to operate the relevant investment components of this Program, and defined Government's role in housing as one of "facilitator." In addition, the approval of the Monetary Code in 2002 mandated elimination of BNV's land development activities and re-affirmed its key function as a second-tier finance agency for housing as well as other sectors. In summary, the Government has made important progress in reforming the housing sector.
- 1.26 **Broad-Based Consultation.** INVI is implementing a Technical Cooperation financed by the Japanese Special Fund to develop a housing policy framework and to design a program aimed at low/moderate-income households. The process of consultation for this policy framework has included a two-day housing workshop sponsored by the Bank with key public and private-sector leaders in 2001, consultations with approximately forty groups of public (central and local) and private sector agents, non-governmental and community stakeholders in the housing sector, and a logical framework workshop.

D. The Bank's sector strategy

- 1.27 The IDB Country Paper stresses that the central challenge facing the country's development is not the absence of social policy, but "rather the severe distortions and constraints...that have frustrated sector policies and limited (its) effectiveness and sustainability". In this regard, one of the strategic vectors of IDB support is "to expand the capacity of institutions to respond to social demands." This Program carries out this goal in the housing sector reorienting it towards the efforts for poverty reduction in the country and advancing social priorities and supporting its key institutions.
- 1.28 IDB's experience in housing over the last decade spans a variety of program types, including slum upgrading, subsidy programs, and second-tier credit finance programs. A number of key lessons have emerged from this experience. First, a reasonable division of labor in the housing sector requires central governments to undertake funding and regulatory roles, the private sector and non-profits should be involved in direct provision of solutions and community organization to execute specific programs, and municipalities can play a key role in land development and services provision for poor neighborhoods. Second, as most households cannot afford to purchase a complete commercially built unit in the Region, low/moderate-income housing programs should support a progressive building process. This support combines public subsidies, credit, and a beneficiaries' savings in varying degrees to deliver solutions appropriate to each income level. The poorest households, which cannot afford credit even microcredit, should be supported through the provision of basic services. Most low and moderate-income households (earning from US\$120 to US\$800 per month), however, can afford a small loan for the next step in the incremental building of their unit, such as improvement, expansion, or construction of a core unit on a lot they own. While the effective demand for these small housing credits is enormous, supply tends to be limited by the capacity of finance and microfinance institutions to offer such loans. Thus, liquidity can galvanize the development of a significant housing microfinance market.
- 1.29 Third, even moderate-income households (earning US\$400 to US\$800 per month) frequently have no access to formal-sector finance which is the case of the DR. The recommendation for this strata is to provide a modest subsidy to allow these households to bridge the affordability gap, while working with the private-sector stimulate a market for low cost core units. These units should be "progressive" (i.e. designed for subsequent expansion) to allow the household to improve and increase their size as income and family needs require. The Bank has often used "direct demand subsidy programs" to provide the necessary funding for moderate-income households. However, these programs must be sustainable overtime. In the DR, although fiscal resources are currently lacking, the Government possesses substantial amounts of developable land in urban areas that can be used to "subsidize" the cost of core houses for low-income households.

E. The program strategy

- 1.30 The Program introduces three key reforms consonant with the new direction of Government housing policy and the Bank's strategy in the sector. First, the Program re-orientes Government habitat programs and policy to focus on the low/moderate-income majority for the first time, particularly on basic services to poor urban neighborhoods. The Program's three investment lines support the incremental building process used by these households: (1) a neighborhood upgrading program provides basic infrastructure and accompanying social services to poor communities; (2) a housing microfinance component channels liquidity on a commercial basis through BNV for qualified first-tier institutions to originate credits to low/moderate-income households for improving, expanding, and building a core unit; and (3) a new development component ("subsidy for core units") joins government-owned land and a modest subsidy for basic infrastructure with a private-sector loan for the house so that moderate-income households can buy a progressive core unit.
- 1.31 Second, the multiphase program as a whole supports a change in Governmental policy of moving from direct production and finance of housing to facilitating the private sector. In this regard, the first phase supports INVI in beginning this process by: (a) cleaning and selling or transferring its portfolio of loans; (b) providing title to the households that received INVI units in the past that were considered a "family good" but that lacked full legal title; and (c) phasing down its direct production program, and re-programming resources to private-sector construction and finance of new core units (the subsidy for core units). In addition, the Program joined with a TCL operation, recently approved, strengthens BNV to perform its role as a second-tier finance institution as mandated by the Monetary Code.
- 1.32 Third, the Program supports the strengthening of INVI and BNV so that these organizations can effectively perform their functions as, respectively, coordinator of the housing sector and the second-tier financial institution. IDB has coordinated with other donors active in the DR including USAID, HUD, and the World Bank in working in the housing sector.

II. THE PROGRAM

A. Objectives

- 2.1 The overall objective of the proposed program is to improve the habitat conditions of low/moderate-income households through deepening credit and property markets, and re-orienting public resources towards these income groups.

B. Program Description

- 2.2 The Program implements a new approach to housing policy in the country that redirects public support to lower income households, employing innovative and more cost-effective types of investments. For the first time the National Housing Institute (INVI) will focus on providing urban services to poor neighborhoods as well as core units to moderate-income households. The National Housing Bank (BNV) will

Box II-1 Key objectives of program components:

- increase quality of life of target population as a result of the neighborhood upgrading projects
- beneficiaries' homes improved with micro-loans that complement the neighborhood upgrading component and by helping construct or improve homes on the serviced lots;
- increase access to housing for the low/middle income target population through the new instrument for financing core units
- better targeting of housing policy with the implementaton of the new *Unified Registry System* which helps the Government to account for the families who are granted housing benefits.

rediscount microcredits originated by first-tier lenders and directed to housing improvements for low/moderate-income households. These innovations will be complemented by the creation of housing planning and policy making mechanisms, including a national beneficiaries register, destined to institutionalize the new policies and monitor effectiveness of public resources applied in the sector. This constitutes the first of a two-phase Program intended to consolidate these new types of investment and approaches to housing policy. The two-phase approach is justified by the time required for the implementation of the new programs and the consolidation of the new policy instruments. Each phase and its components have been designed to reflect the institutional capacity of the executing agencies and the time required to generate the instruments and consolidate the policy changes introduced by the Program.

- 2.3 The Program has three components: (i) new housing and infrastructure programs; (ii) policy reforms and instruments, and (iii) institutional strengthening and support for program implementation. Given the recent significant variation in the relative prices, some of the underlying assumption and parameters, used to define and describe the components that follow will need to be revisited, to ensure that the housing program continues to benefit low moderate income households.

1. New housing and infrastructure programs (US\$35 millions)

2.4 This component will support three types of shelter programs directed to low/moderate-income groups: (a) integrated neighborhood upgrading; (b) housing microfinance, and (c) land development for core units.

2.5 **Integrated neighborhood upgrading** (US\$18.6 million) will finance a minimum package of infrastructure and social services to predominantly poor neighborhoods ⁸selected on a national basis. The package of infrastructure includes water, sewage solutions, drainage, street paving, lighting and environmental protection and mitigation and garbage collection. Social services include early childhood development, primary health services, complementary education and technical training, sanitary and environmental education. Assistance for land tenure regularization will be a part of the projects as appropriate.

<p>Box II-2: Main Selection and Eligibility Criteria for Neighborhood Upgrading Projects</p> <ul style="list-style-type: none">a. More than 70% of the plots in the neighborhood are inhabited;b. More than 50% of the neighborhood population are below the poverty line and presents Unmet Basic Needs for water, sewerage and social capital;c. Neighborhood is not located on lands classified as historical sites, archeological reserves or vulnerable to environmental risk or floods;d. Neighborhood has an established community organization or one in the process of formation.e. The neighborhood should not have less than 400 and not to exceed 1.200 families.
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2.6 Investments have been limited to US\$2.800 per family, including all related project costs, which includes pre-investment, community development, infrastructure works and environmental protection, and social services facilities, in addition to partial operation costs (for up to one and a half years). In this first phase of the program, neighborhoods have been selected on the basis of their income levels and infrastructure deficits, and have complied with other technical criteria, which included the possibility of connection to service networks (mainly water and electricity), feasibility of land regularization, the existence of a community organization among others (see box II-2). A list of eligible neighborhoods is included in the program's operating regulations manual. In total, this sub-component will finance the upgrading of about 10 neighborhoods with approximately 7.000 families.

2.7 **Housing Microfinance** (US\$8.1 million). The housing microfinance component builds on the rich organizational infrastructure of microfinance institutions in the DR, a portion of which have diversified into housing lending. The component will finance small loans ranging from US\$500 to US\$7,500 for short terms (typically 1 to 5 years) for various types of low-cost housing solutions and improvements. The component's Credit Regulations specify the eligible beneficiaries (poor

⁸ Neighborhoods with households earning below \$300 per month.

salaried people and microentrepreneurs), the destination of the loans (home improvement, expansion, construction of a core unit on a lot already owned by the family and titling expenses), eligible intermediaries (specialized micro lending institutions, savings and loans others, which are subjected to the Banking Superintendency supervision), their required financial ratios⁹, financial conditions of the loans (1 to 5 years, market based interest rates, which will be typically higher than the prevailing rates for commercial loans, reflecting their higher risks and service cost), among other aspects. Approximately one-quarter of these micro loans will be targeted to families in the residing in the areas included in the neighborhood-upgrading¹⁰ component thus helping them to improve their homes. The remaining loans will be open to qualified families, regardless of their location. BNV will operate as a second tier agent, rediscounting loans provided by specialized financial intermediaries and supervising the credit line operation. It is estimated that about 4,000 families will benefit from this component.

- 2.8 **Land Development for Core Units** (US\$8.3 million). This pilot project combines existing government-owned land with urban infrastructure financed by the Program to produce developed land, which will be sold to private developers under the condition that they build on it housing units costing up to US\$10,000. The core expandable units (of a minimum built area of 40 square meters) will be sold to moderate-income households. These households will have to provide a down payment of approximately 10% of the unit's total cost and secure a mortgage loan from a bank to finance the difference between the price of the house minus the US\$2,000 discount given by INVI (equivalent to an effective subsidy). INVI will designate government-owned tracts based on urban development, environmental criteria and technical specifications, build the infrastructure, divide them into at least 5 large parcels (to stimulate competition among developers), and sell these parcels to private developers. In turn, these developers will build core expandable units, with bridge financing from private banks, and sell them to the targeted moderate-income households. Developers will be also allowed to produce larger houses on a limited basis (10%), which will cost more and will be sold for slightly higher income families without the subsidy. The repayment of the amount equivalent to the subsidy from the former type of houses will be used by INVI to finance the development of land for more core expandable units. Out of the subcomponent's investment resources (US\$6.1 million) up to US\$300 thousand will be earmarked for environmental mitigation activities determined by the program's environmental review system.

⁹ The main ratios are: (i) risk-loans/assets < 9%, (ii) unproductive assets/equity: at maximum 100%; (iii) profitability: net income/equity >0; (iv) liquidity: current assets/current liabilities, at least 100%; (v) portfolio >30 days in arrears/total portfolio: no higher than 8%. Indicators for non-financial institutions are the same except for a higher risk-loans/asset < 20% and adm. costs/average portfolio balance of less than 25%.

¹⁰ The amount necessary to meet the effective demand of US\$2.5 to US\$3.0 million initially estimated for housing microfinance in the barrios to be upgraded under the Program.

- 2.9 The new beneficiary registry system will be used to track project beneficiaries, while the Program's management information system will ensure a close monitoring of project implementation in all its phases. The component cost allows the development of at least 3,500 core expandable units in two projects. Once tested in the pilot project this line of investment will be expanded substantially in the second phase of the Program to take advantage of the abundant land near urban areas owned by Government.

2. Housing Policy Instruments and Reform (US\$1.3 million).

- 2.10 This component will support the development and consolidation of new policy instruments and regulations, and the modernization of the main institution in the sector (INVI).

- 2.11 **Housing policy and regulatory instruments (US\$600,000).** This sub-component consists of 3 activities: (1) *housing policy and evaluation unit* (\$400,000). The Program will help establish an evaluation and policy unit that will assess the effectiveness of all habitat programs funded by the Government and housing activities by the private sector. This unit's mission is to generate a broad vision of housing sector activities in order to improve their quality, rationalize their expenditures, and re-orient government them to focus on low/moderate-income households. The housing policy unit will create an information system to monitor the execution of INVI's housing projects and housing production and investment overall, producing periodic reports on their status, compare their performance, and assess their costs and effectiveness in obtaining their stated goals. The Program will finance project evaluations and the production of the policy assessment reports, which will lay the basis for future governmental policies in general and INVI activities in particular. This powerful tool will give the institution the informational basis to function as the apex institution in the sector. (2) *Unified Beneficiary Registry* (US\$100,000). A second element in the sector reform is the creation of a central registry of beneficiaries of housing programs and recipients of housing subsidies. This registry will help the Government to account for the families granted subsidies and other publicly funded housing benefits, and reduces the danger of abuses in the system. INVI will be in charge of this registry; (3) *Development of regulatory framework* (US\$100,000). Based on the work begun in the Technical Cooperation and the Presidential Decree 372-02, INVI will develop a proposal for housing regulations by the end of the first phase of the Program. It will also study existing land development and rent regulations, among others, to propose measures to reduce the cost of new construction and land subdivision standards and to streamline development approval. The Program will provide support for creating new low-cost subdivision codes and processes, holding forums with the key stakeholders to discuss and agree on these changes (municipalities and developers), and disseminate them. When applicable, this sub-component shall finance the development of appropriate regulations concerning environmental considerations applicable to the housing sector.

2.12 **Modernization of INVI (US\$700,000).** Support will be provided for the institutional changes necessary for INVI to improve its operations and operate the new investments lines of this Program: (1) *Institutional Reorganization Action Plan (US\$200,000)*. The change in INVI's manner of operation will require changes in staff composition to strengthen the capacity of the organization to regulate, analyze, and operate programs that delegate execution to the private sector. In this regard, the Program will support an organizational evaluation by a consulting firm, which will develop a strategic action plan aimed at streamlining INVI's structure, refocusing its operations, and modernizing its systems; (2) *Rationalization of INVI's loan portfolio (US\$100,000)*. A Presidential Decree has ordered INVI to transfer its portfolio to the Reserve Bank, while a number of private sector institutions have shown interest in buying INVI's loans. However, the documentation and status of many of these loans is chaotic. INVI has begun ordering these records and has begun transferring the servicing of this portfolio to the Reserve Bank. The Program will support the completion of this activity; and (3) *Titling of INVI projects (US\$400,000)*. INVI has begun acquiring full legal title on properties that the organization has sold in order to transfer this title to the purchasing families. The Program will support completion of this process. In addition, concurrent with the completion of the Land Modernization Program, INVI will assess further action in property registry reform and titling in order to develop an action plan. This action plan will provide the informational base for the design of the property rights component of this Program's second phase.

3. Support for Program Execution (US\$2.51 million)

2.13 **Program Management Support (US\$700,000).** This sub-component finances managerial, technical and logistical support for INVI to implement the program. Includes both support for the implementation of information systems and the contracting of the following consultants: i) one (1) International Coordinator (three years); ii) a local counterpart coordinator (4 years); iii) a local procurement expert; iv) two local finance and accounting experts; v) an international or local environmental expert for the duration of the program (4 years) and; vi) short term consultants in progressive housing, slum upgrading and other particular areas as needed. Includes also resources (US\$30 thousand) for computer equipment and software applications for the coordination unit. The unit's functions and activities are described in Chapter III.

2.14 **Monitoring, evaluation and auditing (US\$300,000).** Given its innovative nature, the Program offers opportunities for and requires a monitoring and evaluation approach that allows a comprehensive scrutiny not only of cash flows but also of operational and impact results, including environmental. As such, in addition to annual external audits, systematic monitoring and evaluation activities of the Program will be carried out by means of INVI's Monitoring and Evaluation System (MES). The MES, which will be developed and implemented as part of the Program, will allow INVI to carry out a close monitoring and evaluation of the activities of the Program, and to monitor and evaluate all government programs in the housing sector.

- 2.15 With regards to the Program, the MES comprises the following elements: a) a baseline for the Program, including the identification of control groups to carry out impact evaluations; b) an integrated information system that will allow monitoring of the execution of the Program in terms of physical outputs, costs of delivery, disbursements and intermediate and final outcomes. To this end, this system will be fully compatible with the SISEG (*Sistema de Seguimiento Gerencial de Operaciones del Banco*) being used by the Country Office in DR; and (c) a set of evaluations to assess progress and impact of the activities undertaken by the Program.
- 2.16 The MES¹¹ will provide information and finance for the production of a mid-term evaluation that will: i) evaluate progress in Program implementation to be measured by the achievement of its performance indicators, ii) assess performance of institutions involved and compliance with set norms and regulations, and iii) gather any lessons that can be used to fine tune the operation's execution scheme, as well as the design of phase II. Likewise, the final evaluation will be supported by MES to measure: i) performance of the program's execution in terms of outputs, ii) the nature and magnitude of its achieved outcomes and intermediate impacts, and to iii) gather lessons learned from this operation that will serve as input to future interventions by the Bank in the housing sector. Finally the external audit of the program will also be supported by this component. Independent consultants will carry out all evaluations and audits, in accordance to Bank guidelines and procedures. Draft Terms of Reference are available in the appendices.
- 2.17 **Supervision of projects** (US\$1,310,000). This subcomponent supports the contracting of supervision of works and other field activities developed by the two investment components (barrio upgrading and land development for core units) executed by INVI. Supervision works will be carried out by external consultants or by INVI's technical team specially assigned to the project, as deemed required. Supervision activities shall include specifically the supervision of environmental and social activities and mitigation measures proposed in the project. Supervision services will be contracted before the start of any construction work or social intervention financed by the project. Budget for supervision activities accounts for 3.8% of the Program's investment component, equal to US\$1.32 million, of which US\$800,000 will be loan's resources and the equivalent of US\$500,000 will be contributed by INVI as counterpart financing.
- 2.18 **BNV strengthening for microcredit activities** (US\$200,000). The Program will support consultancies and an information system necessary for operation of the

¹¹The design and implementation of MES are being undertaken with the support of a Technical Cooperation financed by the Spanish Trust Fund and the technical assistance of the Development Effectiveness Group of Region II. The TC will finance the elaboration of the baseline, the design and testing of the MES and training for INVI's staff and the development of impact indicators for the program. The implementation of the MES as well as the monitoring system of the program, and the evaluations will be financed by the loan.

housing microfinance component by BNV. Its core group is already initiating operations in this area but will require expert support in supervision and promotion methodologies and in the development of a dedicated follow-up system for the supervision of the first tier operators in this line of credit. Broader support for BNV's conversion to a second-tier finance entity is available under a TCL operation, with which this subcomponent will coordinate.

C. Cost and financing

2.19 Total cost for the Program's first phase are presented in the cost table bellow. Bank financing through Ordinary Capital will amount to US\$37 million and counterpart financing will be US\$4.2 million, for a total of US\$41.2 million. The distribution among components is the following:

Table II-1 COST TABLE
Multi-phase low/moderate income habitat program RD-0141
(In thousand of US\$)

Components	IDB	Local Counterpart	Total	%
1. New housing and infrastructure programs	32,100	2,900	35,000	85%
a. Integrated Neighborhood Upgrading	18,000	600	18,600	
a1. Investments in Neighborhood Upgrading	17,300	600	17,900	
a2. Environmental Protection and Mitigation	700		700	
b. Housing Microfinance	7,300	800	8,100	
c. Land Development for Core Units	6,100	2,200	8,300	
c1. Development of Core Units	5,800	2,200		
c2. Environmental mitigation	300		300	
2. Housing Policy Instruments and Reform	1,300		1,300	3.1%
a. Housing Policy and regulatory Instruments	600		600	
b. Modernization of INVI	700		700	
3. Support for Program Execution	2,000	510	2,510	6%
a. Program Management Support	700		700	
b. Monitoring, Evaluation and Auditing	300		300	
c. Supervision of Projects	800	510	1,310	
d. Strengthening of BNV	200		200	
4. Financial Costs	2,300	90	2,390	7.1%
a. Commitment Fee		90	90	
b. Interest	2,300		2,300	
c. Supervision and Inspection Fee		-	-	
TOTAL	37,000	4,200	41,200	100.00%
Percentage	90%	10%	100.0%	

2.20 The size of the IDB loan of the first phase US\$37 million has been estimated as the amount necessary for initiating a housing program of significant impact on the

sector while in line with the institutional capacity of the public and private institutions involved in its implementation. This sum is also within the limits of indebtedness allowed by the current fiscal adjustment program agreed by the IMF.

2.21 The financial conditions of the loan are the following:

Amortization Period:	20	Years
Grace Period:	4	Years
Disbursement Period:	4.5	Years
Currency:	US\$ Dollars	
	Single Currency Facility	
Interest rate	Variable	
Credit fee	0.25%	
Supervision and Inspection	0%	

2.22 It should be noted that the interest rate, credit fee, and inspection and supervision fee are established pursuant to document FN-568-3 Rev. and may be changed by the Board of Executive Directors, taking into account the available background information, as well as the respective Finance Department recommendation. In no case will the credit fee exceed 0.75%, or the inspection and supervision fee exceed 1% of the loan amount¹².

D. Program Phases and Triggers

2.23 The two-phase design is intended to allow initially INVI and BNV to learn to operate the new investment modalities and to make the necessary internal institutional adjustments and to develop and promote the sector-wide policy instruments and reforms. The second phase will consolidate and expand the programs and implement the reforms. There will be an independent evaluation at the end of the first phase. This evaluation will take place after three years of Program execution, or when 50% of Program resources have been committed, whichever come first. At the time of this evaluation, the borrower should, at a minimum, have attained key benchmarks for each major Program objective. Independent consultants will carry out the evaluation and its results and recommendations will serve to improve the design and execution of the second phase of this operation.

2.24 **Triggers for the second phase.** The executing institutions (INVI and BNV) will be required to meet a set of key benchmarks in order to qualify for the second phase. INVI will: (a) institutionalize the new housing and infrastructure programs, ensuring that 100% of beneficiaries of these programs meet household income guidelines and other selection criteria; (b) have established the housing programs beneficiary register, have enrolled in it all of INVI programs beneficiaries; (c) sell or transfer at least 75% of the organization's loan portfolio; (d) produce at least

¹² With regard to the inspection and supervision fee, in no case will the charge exceed, in a given six-month period, the amount that would result from applying 1% to the loan amount, divided by the number of six month periods included in the original disbursement period.

two annual evaluations of DR housing policies and programs; (e) initiate no more than 800 new units per year under INVI's direct new construction program during the first phase of this Program; and (f) implement key recommendations of the reorganization consulting agreed with the Bank by the mid-term evaluation, including a reduction of more than between 10% of its permanent staff. BNV will: (a) end its residential land development activities; and (b) maintain microfinance lines of credit and ensure that microfinance loans meet ceilings for loan amount and home value.

- 2.25 The second phase will expand the land development for core units and continue with the neighborhood upgrading and housing microfinance components. The second phase will also build upon the action plan for property rights developed in the Bank financed Land Modernization Program to support further improvements to the property registry to cut times and costs and increase security, reform the regulatory framework, and launch a titling program. The land division of the Supreme Court and the General Services Administration would implement this property rights component.

III. PROGRAM EXECUTION

A. The borrower and executing agency

- 3.1 The borrower is the Dominican Republic. INVI will be the Program's executing agency, responsible for its general administrative and financial control. In this role it will be the sole interlocutor with the Bank, operating the special account and keeping all the documentation required for financial and performance audits. BNV will be the co-executing agency in charge of implementing the housing microfinance component. Municipalities will be involved in the implementation of the neighborhood-upgrading component, but only as co-sponsors of projects and monitors of the execution of public works and social services. *An agreement between the borrower and INVI, specifying the their responsibilities with respect to the execution of the Program is a condition prior to first disbursement of the loan. The official enactment of the Program's Operating Regulation is a condition prior to first disbursement of the loan.*

B. Program execution and administration

- 3.2 INVI will execute the slum upgrading and subsidy for new core unit investment components, the technical assistance and institutional strengthening components, and will be responsible for program administration and control as a whole. In regard to neighborhood upgrading, INVI will be responsible for the selection of neighborhoods to be upgraded, based on the pre-selection list included in the Operational Regulations, contracting engineering designs, infrastructure investments and the social services provided by the component. Municipalities will be involved from the start presenting project profiles, participating in the selection of engineering firms, in the contracting of works and services and their supervision, so that they can get involved in the maintenance and operation of the improvements in there are of competence. NGOs will be contracted by INVI with municipal assistance in order to implement community development activities, deliver social services and provide sanitary/environmental education and assist in the supervising the implementation of the environmental specifications included in the bidding documents of the works contracted.
- 3.3 The housing reform component consists essentially of technical assistance that is generally directed to strengthen INVI as a leading institution in the housing sector. The consultants required for this component as well as those required for strengthening of BNV will be selected by each institution according to Bank procedures.
- 3.4 BNV's responsibilities involve the establishment of a line of credit for rediscounting housing microfinance loans, supervision of the use of these funds by the financial intermediaries and monitoring, controlling and reporting on the effectiveness of the component in terms of its development objectives. BNV will maintain separate accounting records with regard to the use of IDB funds but will channel its financial reports and disbursement requests through INVI's execution

unit. Provisions have been made to assure that the operational performance of one institution does not affect the other. *The signing of the cooperation agreement between INVI and BNV was a pre-condition for the presentation of the Program to IDB Board of Directors which has been fulfilled.*

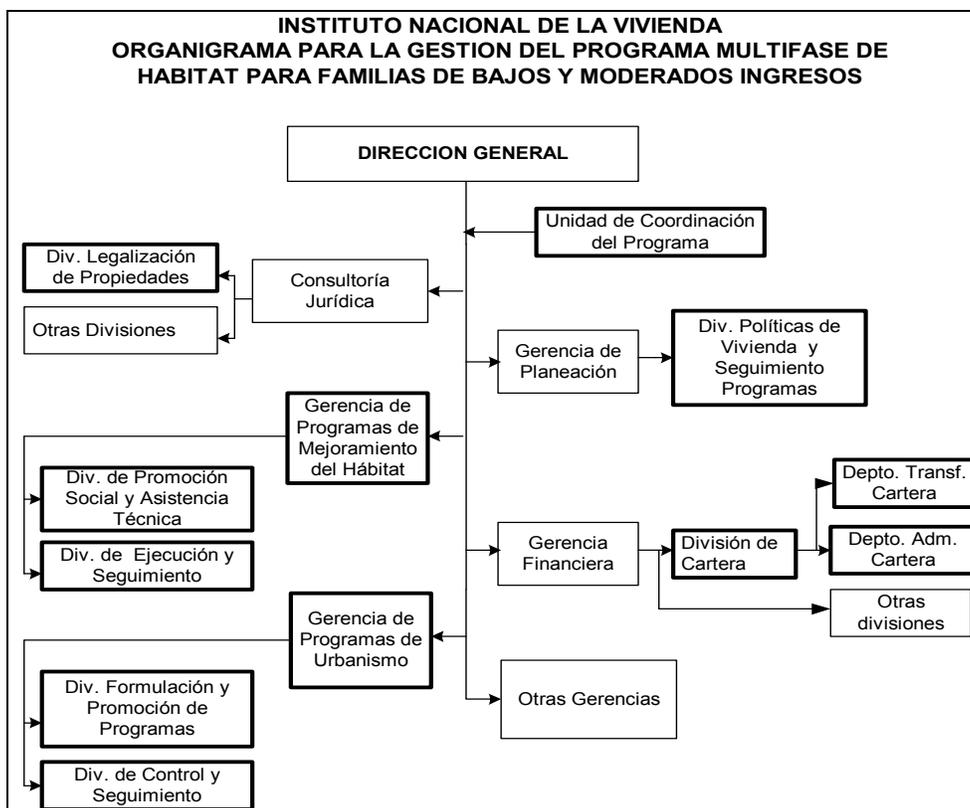
C. **INVI's Organization for Program Execution**

- 3.5 The institutional analysis concluded that INVI has the technical capacity to perform the large majority of the functions required by the Program to operate properly. Nonetheless, it still requires institutional strengthening in areas such as housing policy planning, evaluation and monitoring of social projects, portfolio management, environmental management and titling. To that end, INVI's management structure will be revised to integrate new units and strengthen existing ones, providing training to current staff and incorporating short and long term consultants. *The formal establishment within INVI's structure of the new coordinating unit and the two "gerencias" of neighborhood upgrading and urbanization was a pre-condition for presentation of the Program to the IDB Board of Directors which has been fulfilled.* The new units and their main functions are as follows:
- 3.6 **Program's Coordination Unit** will be created to supervise global performance and undertake responsibilities for the program's overall planning and management. The Unit will also provide support to the operations related to the Program carried out by other units within INVI's structure. This unit will comprise: a) a consultant with international experience who will act as a General Coordinator; b) a local consultant that will act as Assistant Coordinator (and who will take over as General Coordinator after a period of two years); c) a local consultant for two years to advice on procurement processes; d) an environmental consultant for the duration of the program; this specialist shall serve as a unit/departmental advisor in the INVI); and e) two local financial consultant format the current accounting systems to allow this information to be presented by INVI to the Bank. This unit would be responsible for hiring short-term consultants – as needed – to help in the execution of all Program components.
- 3.7 **Planning Department** (*Gerencia de Planeamiento*) this already existing department will re-orient its current functions to those related to the formulation of housing policies and strategies, inter-institutional coordination and program monitoring (at a macro level) and impact assessment. As part of its management structure, this office will include the Housing Policy and Program Monitoring Division that will be in charge of: i) promotion, discussion and writing of the final draft proposal for the National Housing Policy, ii) formulation of the INVI's annual operative plans, and iii) operation of the system for the monitoring of housing programs. This Division will be staffed by: a lawyer, an urban planner and an economist (finance).
- 3.8 **Habitat Upgrading Department** (*Gerencia de Programas de Mejoramiento de hábitat*). This is a new unit that will be responsible for the planning and execution of housing upgrading projects among others. This office would

comprise two divisions: i) Promotion and Technical Assistant Division; and ii) Execution and Monitoring Division. Both divisions would be staffed with INVI's current staff that will be supported with consultants as needed including the environmental expertise.

3.9 **Land Development Department** (*Gerencia de Programas de Urbanismo*) another new unit responsible for identifying, formulating, managing and supervising the new land development programs by INVI. This office will have two divisions: i) Project Planning and Promotion; and ii) Control and Monitoring. The former will be responsible for the identification of land parcels in conjunction with other governmental institutions (e.g., CONAU, municipalities) and the subsequent design of basic infrastructure. The latter will be responsible for contracting of companies charged with the urbanization of land parcels, allocating of parcels to private developers for the construction of core units and supervising developers to comply with contractual conditions.

3.10 **Other Units:** INVI's Legal Department (*Consultoría Jurídica*) will be enlarged with the addition of a new Property Regularization Unit. The Finance Department will establish a Portfolio Management Division with two sub-units: Portfolio Management and the Portfolio Transfer. This last will have a temporary character, operating only until legal instruments and mechanisms for transfer are defined. The following graph shows the Program execution structure within INVI's existing organization (with new units highlighted in bold frames).



D. The Project Cycle

3.11 The investment component has three types of projects, whose execution cycles are the following:

1. Neighborhood Upgrading Projects

a) Neighborhood Selection

3.12 INVI, with the cooperation of the National Office for Planning and the National Council for Urban Affairs will prepare a list of pre-selected neighborhoods eligible for the Program based on information from the Poverty Map and the criteria established in the Operating Regulations. This list will have considered all municipalities located within metropolitan areas and which concentrate more than 20% of the population living in poverty in the country.

b) Project Planning and Financing

3.13 INVI will contract consultants to prepare Neighborhood Upgrading Project Profiles, which will be developed based on the guidelines developed for such a purpose, who will work jointly with the beneficiaries municipalities. INVI will evaluate the profiles in order to verify if selected barrios meet all technical, socioeconomic, urban and environmental eligibility criteria, as established in the Program's Operation Regulations Manual.

3.14 INVI will subscribe Participation Agreements with the municipalities of neighborhoods selected for upgrading and the corresponding *Junta de Vecinos* and will proceed to contract consultants to carry out project planning. Monitoring of consultants' work will be carried out by INVI in coordination with the local municipality advised by the local *Junta de Vecinos*. Project planning will include the preparation of bidding documents and the agreement on the participation in project implementation on the part of the municipality and contributions in kind by the community. The entry into effect of these agreements in a particular neighborhood is a pre-condition for the disbursement of resources to carry out upgrading activities in that neighborhood.

3.15 During Project preparation, consultants will provide training for the *Junta de Vecinos* with regards to project management and execution, and in the administration of services to be provided as part of the project. After a period no longer than six (6) months, the project planning should be completed, approved by the community and the municipality, and presented to INVI for financing.

3.16 Public services to be financed by the Program will be operated and maintained either by utility companies at the national level or by municipal governments. These responsibilities will be established in agreements signed with utility companies (mainly sanitation and electricity) and municipalities previous to the approval of each individual neighborhood project. Regular tariffs will be charged for the provision of these services to ensure sustainability. In the case of

simplified self contained systems that are to be maintained by neighborhood groups, the community development component will provide training for the community association to enable it to adequately operate and finance the maintenance of the system. With regards to social services, operation will be responsibility of the national institutions in charge of such services (health, education, social assistance) in the terms established in the corresponding agreements. The subscription of such agreements is a condition for approval for each neighborhood-upgrading project.

c) Project Execution

- 3.17 INVI, in collaboration with the beneficiary municipality, will undertake the selection and hiring process of consultant firms that will be in charge of the implementation of community development and social participation and the construction works involved in each neighborhood project. Selection will be carried out from INVI's list of pre-qualified firms for both construction works and consulting services.
- 3.18 INVI's technical team itself by means of the Unit responsible for such a task could carry out project supervision.

2. Land Development For Core Units

a) Identification and Selection of Land Parcels

- 3.19 INVI will identify and select appropriate government-owned land parcels for development by means of a systematic analysis that includes: a) pre-selection of parcels based on the norms and priorities for development established by CONAU, the Secretariat of Environment and Natural Resources and the municipalities, b) an analysis to determine the soundness of the legal condition of pre-selected parcels (to be carried out in collaboration with the government institution in ownership of the land), and c) an analysis to determine the technical viability and economic potential of pre-selected parcels according to the criteria advanced by the operating regulations of the Program. The analysis will provide a list of parcels that fully comply with the criteria for project development established by the operating regulations of the Program. Selected land parcels will be legally transferred to INVI.

b) Urbanization of Land Parcels

- 3.20 INVI will undertake the design of urbanization projects, including the topographic survey, environmental impacts assessments or environmental analysis, land use and infrastructure design, for which it may hire specialized technical support. By means of a public bidding and a selection criteria based on best technical and economic offers INVI will contract out private firms to undertake: a) the urbanization work and b) the supervision of construction works. Contracting of private firms will be carried out following IDB procurement procedures. INVI

will be responsible for obtaining all necessary building permits and approvals, as well as for the overall supervision of works.

c) Issuing of Subsidy Vouchers

- 3.21 Towards the completion of urbanization works, INVI will proceed to issuing subsidy vouchers for individual families. Beneficiary families will be selected by INVI according to current government regulations (Presidential Decree No. 115 de 1998), which establish a point system for classifying families according to need, family size and other variables. INVI's social workers will verify the accuracy of the information provided by applicants. Vouchers will be legal documents issued by INVI to be used exclusively in the purchase of a core unit in a particular project. The number of subsidies issued will correspond to the number of lots available in such a project. The document will specify the maximum value of the core unit to purchase as well as the deadline for the use of the subsidy.

d) Sale of Urbanized Parcels

- 3.22 INVI will be responsible for the sale of urbanized parcels of land to private firms for the construction of core units. Urbanized parcels will be offered to potential developers by means of public bidding, which will be conducted by INVI according to the norms and conditions established in the operating regulations. Bidding documents will specify physical standards, environmental specifications costs and the number of the type of units to be built, as well as the rules for their promotion and sale. Bidding documents will also specify payment conditions for urbanized parcels and all legal obligations acquired by winning firms; all bidding documents will require the no-objection of the Bank. Competition will be open to private firms with experience in real estate development and awarding of land parcels will be based on the advancement of entry quotas beyond the minimum of 10% of the total cost of the urbanized land. The size of the entry quotas offered by developers will constitute the determining factor in their selection, as well as the order of priority in the choice of available land parcels.

e) Construction and Sale of Core Units

- 3.23 The private firms will carry out these activities. INVI will monitor construction and sale, ensuring their compliance with norms, criteria and conditions as established in bidding documents. Noncompliance with such regulations will lead to corresponding fines to be pursued by INVI's legal department. Private firms will promote their products among households approved by INVI to receive the subsidy. Participating households will use their subsidy together with their savings and a credit extended by financial institutions to purchase a house from those offered by the private firms. As recipient of the subsidy, participating households will be entered in INVI's beneficiary registry.

3. Housing Microfinance

- 3.24 The National Housing Bank (BNV) will implement the housing microfinance subcomponent. BNV will rediscount microcredits of qualified first-tier microfinance institutions and Savings and Loans. BNV will qualify these first-tier lenders using a series of prudential criteria including amount and experience of the institution's existing loan portfolio, capacity to originate and service micro-housing loans, capital adequacy, and other financial indicators. These first-tier lenders will work directly with borrowers to originate and then service these housing microcredits, and will take the credit risk on these loans. BNV will open a special account and submit periodically to INVI and the Bank a list of credits extended and recipient institutions for reimbursement. BNV will also present evidence that this organization has followed the procedures put forward in the Program's Credit Regulations. *The entry into effect of an agreement signed between BNV and a participating financial institution, which makes reference to the Program's Credit Regulations, is a pre-requisite for the disbursement of Program's resources to such institution.*
- 3.25 BNV has established a new unit to manage this sub-component. It is conformed initially by three core professionals who are in charge of developing the basic regulations and control systems for this new line of credit. *The official designation of this core team to operate the microcredit sub-component is a condition of first disbursement for this sub-component.*

E. Procurement of works, goods and services

- 3.26 International competitive bidding will be required for the acquisition of goods and related services when equal or exceeds US\$250.000, for works which are equal or exceed US\$1.500.000 and for consulting services which are equal or exceed US\$200.000. Acquisition of good and related services and contracting of civil financed with the project resources will be subject to Bank's procurement procedures and policies. All bidding under these limits will be done following national legislation when its provisions do not contravene the Bank's procurement and procedures policies. The selection of consulting firms may be based on the price and quality method, provided that the weight allocated to price as a criterion does not exceed 20% of the total ranking

F. Revolving Fund

- 3.27 The Project team recommends that a revolving fund of 5% be established for the program, to be managed by INVI. Furthermore, a revolving fund of 5% of the amount of the Microcredit component should be established in the name of BNV to facilitate the components execution. Both institutions will have the obligation submit semi-annual reports on the status of their respective revolving funds, within 60 (sixty) days of the end of each semester. INVI will consolidate these reports and other information, including expense justifications for presentation to the Bank.

G. Execution and disbursement schedule

- 3.28 The execution of the first phase of Program is projected to take 4 years. Annual disbursements are expected to occur according to the following schedule:

Component	Year 1	Year 2	Year 3	Year 4	Total
A. New Programs	5,500	8,500	9,000	12,000	35,000
B. Housing Sector Modernization	310	320	340	330	1,300
C. Support for Program Execution	620	630	630	630	2,510
D. Financial Costs	340	720	1,200	130	2,390
Total	6,770	10,170	11,170	13,090	41,200
%	16%	25%	27%	32%	100%

H. Monitoring and evaluation

- 3.29 The Program finances a component supporting a monitoring and evaluation system (described in paragraph 2.14), which includes the monitoring of project outputs and outcomes, follow-up of all financial and administrative operations and financing for a mid-term and a final evaluation. The mid-term evaluation will take place after thirty months (30) of Program execution or when 50% of Program resources have been committed whichever come first. At the time of this evaluation the borrower should at a minimum, have attained key benchmarks for each major Program objective. The results of this evaluation as well as any recommendations will serve to improve the design and execution of the second phase of this operation. The final evaluation will be carried out six (6) months before the final disbursement of the investment component. Independent consultants will carry out both evaluations, in accordance to Bank's guidelines.
- 3.30 INVI and BNV will collect, store and retain all necessary information, indicators and parameters, derived from the information and monitoring system, in addition to the Annual Implementation Plans, results of the mid-term review, and of the final evaluation, to enable: (i) the Bank to prepare the PCR; and (ii) the Bank's Oversight and Evaluation Office (OVE), if so wishes, to evaluate the impact of this operation in accordance to GN-2254-5.

I. Financial Control and Auditing

- 3.31 INVI, as the executing agency, will have the following obligations: i) maintain separate and specific bank accounts for managing the Bank's loan and local counterpart funds; ii) submit timely disbursement requests and the corresponding justification of expenses; iii) implement and maintain adequate systems for the management of contracts and finances, and internal controls with respect to the management of the IDB and local counterpart funds, in accordance with the Bank's requirements; iv) prepare and submit Project financial reports required by the Bank, including the consolidated financial statements of the Program and of

INVI; and v) maintain an adequate documentation filing system to support eligible expenses to be examined by the Bank and the external auditors.

- 3.32 Throughout the Program execution period, INVI will submit annual consolidated financial statements of the Program and of INVI. The external audit of the Program will be conducted by a firm of independent auditors acceptable to the Bank, hired in accordance with the Bank's requirements and based on the Terms of Reference for External Audits of Bank-financed Projects (Document AF-400). The external audit should be financial and operational in nature, requiring the submission of a semi-annual "interim" report, within sixty (60) days of the end of each first semester and annual reports on the Program's financial statements, within 120 days of the end of each fiscal year.

J. Program Supervision

- 3.33 The Bank's Country Office in the Dominican Republic will be responsible for project supervision. RE2/FI2 staff in headquarters will provide support in technical aspects as needed and accompany the mid-term and final evaluations. Given the innovative nature of the program and the specific sector issues involved in its implementation it is recommended that at least one administration mission per year be carried out during the period of project execution.

IV. VIABILITY AND RISKS

A. Socioeconomic viability

- 4.1 The three lines of investment of the project have been analyzed separately according to different methodologies: (a) cost-efficiency analysis was utilized for the slum upgrading component to determine the threshold for efficient per family investment cost to be used throughout the program; (b) the subsidy for core units component was assessed by comparing the minimum cost solutions required to achieve the lowest possible selling prices of the units with the capacity to pay of the targeted low/middle income households. This allowed to determine the size of the subsidy that will enable them to afford the core houses; and (c) the potential demand for microcredit for the housing microfinance component.

1. Neighborhood upgrading.

- 4.2 The socioeconomic feasibility of the neighborhood-upgrading component was assessed on the basis a sample of three projects, which have been developed up to the final design stage. This sample was used to define the minimum-cost alternatives for project designs and the average-cost parameters for the remaining projects to be financed by the program. The sample consisted of three neighborhoods selected on the basis of their poverty levels, infrastructure deficits and geographic location to represent the two areas where the program would operate (Santo Domingo Metropolitan Area and Santiago) and their types of urban and social problems. This exercise was also useful to test and train the executing unit in the new integrated infrastructure and social services planning methodology, IDB contracting procedures and general preparation for program implementation.
- 4.3 A summary of the sample characteristics is shown in Table IV-1. The average size of the neighborhoods was 594 families. Sanitation works comprised the bulk of the investments (35% on average), followed by streets and drainage, and complementary works, which includes works built outside the neighborhoods proper but required for the operation of their basic infrastructure (water tanks and pumps, connections to the main electricity, road or water systems etc.). Social components' costs averaged 18% of total investments.

Table IV-1: Sample Upgrading Projects - Cost Summary Table

(in US\$)

MUNI-CIPIO	BARRIO	No. Families	Sanitation	Streets & Drainage	Electricity	Complementary Works	ComM Dev & Social Project	Other(1)	Pre-Investment	TOTAL	INVEST/FAMILY
SD Este	Solares del Perla	664	766,609	394,256	225,380	34,988	298,312	2,603	60,000	1,782,147	2,684
SD Norte	Casabes de Duquesa	535	751,108	357,265	108,212	94,847	298,312	2,685	60,000	1,672,429	3,126
Santiago	S. José la Mina	583	215,732	339,463	99,621	527,225	298,312	2,430	60,000	1,542,784	2,646
	Total	1,782	1,733,449	1,090,985	433,213	657,060	894,935	7,718	180,000	4,997,359	2,804
	Promedio		577,816	363,662	144,404	219,020	298,312	2,573	60,000	1,665,786	2,815
	Porcentaje		35%	22%	9%	13%	18%	0.15%	3.60%	100.00%	

(1) Including environmental mitigation measures

4.4 Based on this sample, a cost-efficiency level of US\$2.800 per family was established (including pre-investment studies and operation of social services for the first year). This will be the maximum cost parameter to be used for the design of the remaining projects to be financed by the Program. However, given particular site characteristics, a deviation of 10% will be allowed, provided that it is justified on the basis of extraordinary site conditions. The sample study also helped to determine eligibility criteria concerning the density of the neighborhoods (70% of lots occupied) and their minimum and maximum size (400 and 1200 families respectively)

2. Land Development for Core Units

4.5 The socioeconomic viability of the Land Development for Core Units pilot project was determined through the cost-efficiency approach by identifying core-housing solutions, which could be produced and sold at prices that are affordable to the target groups. Since land is provided by the government (at no financial cost), the analysis used the cost of developing land on the periphery of Santo Domingo (the location of the pilot project) to determine a plot's size that struck a balance between minimum cost for development (i.e., economies of scale for the provision of basic infrastructure and services) and sufficient area to allow for additions to be made to the house (progressive development). Parallel to this it was also determined the cost of standard quality construction of a core unit of minimum size but capable to meet a family's basic housing needs. To this cost an average overhead margin for the private developer was added to obtain an overall cost for the core unit. The result was a minimum size plot (90 sq m) and a minimum size core unit (40 sq m). The combined solutions represent the most accessible housing option in the market in terms of its selling price (US\$8,190).

4.6 Financing the core unit is based on the combination of family savings, a credit from a commercial institution and a subsidy. Affordability for target groups was established by analyzing the saving and monthly credit repayment capacity of the

target groups based on income. As a result of this exercise, the amount of the subsidy was set at US\$2,000 (which is a discount on the final price of the house roughly equivalent to the estimated cost of the land). The subsidy covers approximately 24% of the total cost of the house, and together with a modest amount of savings (10%) makes it possible for a family in the target group to obtain a loan for which the monthly payments are affordable (representing 33% of the family monthly income) to a family that earns US\$300 a month. A summary of the cost and finance analysis for house type A is presented in Table IV-2.

Table IV-2: Cost & Finance Analysis – Unit Type A

Concept	Cost US\$	Percentage
PRODUCTION COST		
Raw land	1,440	18%
Infrastructure and Services (land dev)	1,336	16%
Unit construction	4,800	59%
Other costs (overheads)	614	07%
Total cost per unit	8,190	100%
FINANCING		
Savings (Down-payment)	818	10%
Subsidy	2,000	24%
Credit	5,372	66%
Total price per unit	8,190	100%
Monthly payment (15 years)	99	
Required monthly income	300	
Number of minimum salaries (2)	4	

(1) Plot Area 90 sq mt., unit 40 sq. mt.

(2) Equivalent to US\$ 75

3. Housing microfinance.

- 4.7 Housing microfinance (HMF) small loans, at market rates for short terms for low-cost housing solutions can help solve many of the problems of traditional mortgage finance. The DR is fortunate to have a large pool of financial institutions capable of meeting this demand (Lasa, 2003). The National Housing Bank (BNV) will implement the housing microfinance subcomponent. BNV will rediscount microcredits of qualified first-tier microfinance institutions and Savings and Loans. It is important to reiterate that the population segment to be attended is such that actually is not benefited from the regular banking credit. BNV will qualify these first-tier lenders using a series of prudential criteria including amount and experience of the institution's existing loan portfolio, capacity to originate and service micro-housing loans, capital adequacy and other financial indicators. These first-tier lenders will work directly with borrowers to originate and then service these housing microcredits, and will take the credit risk on these loans. BNV will also present evidence that this organization has followed the procedures put forward in the Program's Credit Regulations.

B. Financial viability

- 4.8 **Availability of counterpart resources.** Sufficient counterpart resources should be readily available for the Program for a number of reasons. Most of the counterpart funds are allocated to the subsidy for core unit's components. INVI will be contributing land in equal value to the subsidy for new core units for these projects, which will account for over half the required funding. In this regard, INVI also intends to begin preparing these projects with its own funds and start developing the land with its own funds (based on program regulations and Bank procedures). Similarly, BNV has decided to expand its pilot housing microfinance project by injecting US\$1 million into it once the operating regulations for this component are finalized. Therefore, the need for cash resources is small and should not constitute a problem for the institutions involved.

C. Environmental and social analysis

- 4.9 The Program will have a highly positive social and environmental impact through improving living conditions of the families in poor neighborhoods and by improving their housing conditions in general. The sample studies developed for the three neighborhood upgrading projects as well as the pilot subsidy for new units have assessed the social and environmental impact of those interventions and identified environmental risk that may be present. These studies have served to develop the Environmental and Social Management Plan (ESMP) for the Program.
- 4.10 Among others the ESMP specifies: (a) environmental eligibility criteria for project selection, which have been fully incorporated to the project approval guidelines; (b) mitigation measures, environmental management plans and its related costs; (c) environmental institutional needs; and (d) community participation in the process. The ESMP also details the execution supervision and maintenance criteria by which INVI will observe environmental and social considerations for the Program. All this information has been incorporated in the Operating Regulations Manual, and will be included in the bidding documents of the proposed infrastructure works in the Program. A specific budget for environmental mitigation measures and environmental component have been included in the cost table in order to ensure appropriate environmental compliance within the proposed works and activities.
- 4.11 During Program execution, INVI will be responsible for evaluating each proposed project based on the ESMP, and implement corresponding environmental control and monitoring mechanisms. As a condition prior to first disbursement, INVI will hire and incorporate in its staff, an environmental specialist, who will be maintain throughout the Program and will work as an advisor for all activities of the program. Among others, the following factors will be main responsibilities of the Environmental Specialist in INVI: (a) evaluate all technical-Environmental Analysis and/or EIA's related to project designs and engineering for component

- 1; the specialist will also advise in relevant issues or activities of components 2 and 3; (b) implementing measures to reduce impacts, protect the environment, and mitigate environmental disasters; (c) attention to and mitigation of negative environmental impacts; (d) assist in the analysis and monitoring of projects with the Ministry of the Environment and Natural Resources, municipalities, and other relevant environmental agencies; and (e) ensure compliance with the relocation requirements of the Bank.¹³
- 4.12 As part of INVI's general execution plan for the program, a general schedule of environmental tasks and budget will be prepared and assigned to the environmental specialist in order to ensure sustainability of the attributed responsibilities and activities throughout the execution period of the program. In addition, short term consulting could be undertaken to produce Environmental Analysis (EA) or related studies for present or future works, Environmental Impact Assessments (EIA) if required by law, environmental engineering designs, and any drafting of new environmental regulations or laws necessary to improve existing deficiencies.
- 4.13 Community participation has been key in the design and execution of projects and as such, it will be an integral part of ESMP. Consultations with community groups and other stake holders involved in the projects will continue to take place to explain impacts and mitigations measures of projects. Consultations will continue to be conducted in compliance with the Bank's practices.
- 4.14 **Social Classification:** The Program qualifies as poverty targeted since over 50% of the beneficiary families are below the poverty line for the Dominican Republic. It also qualifies as promoting social equity because the bulk of the investment component finances slum upgrading, which is a priority social sector according with the Eight Replenishment Document (AB-1704).

D. Benefits and development impact

- 4.15 The immediate impact of the Program will be to improve the housing conditions of 13,300 low/moderate-income households as follows: (a) infrastructure and community services improved for 7,000 families in 10 informal neighborhoods; (b) 3,500 units improved, expanded or built through housing microfinance; and (c) 3,500 new progressive house units built with support of the land development for core units component.
- 4.16 Historically, housing investment has often served as a counter-cyclical force to stabilize economies during recessions, as it has in several countries supported by

¹³ Relocation will be required only when necessary to allow improved accessibility within informal neighborhoods or to prevent environmental risks. They will be limited to a maximum of 5% of the total number of households within each community. Relocations will be voluntary and families will be offered solutions within or near the existing communities.

IDB housing programs.¹⁴ Thus, the economic impact of this housing investment is likely to help moderate the economic fallout from the financial difficulties currently faced by the Dominican Republic. Given the high multiplier effect of housing construction expenditures (generally estimated at 3 times the construction investment), the housing investment under the Program will inject roughly US \$120 million into the Dominican economy, and generate 12,000 jobs.

- 4.17 In addition to that, Program, will have a systemic developmental impact beyond the immediate investment in four important respects. First, the housing microfinance component will develop the credit market for housing finance of low/moderate-income households – the great bulk of the DR’s population that is now largely beyond the reach of formal-sector financial institutions. Second, the subsidy for new core units will move unused portions of government land on the urban fringe into private ownership, helping to build the assets of households, increase the efficiency of urban development, and increase the efficiency of INVI (relative to its direct new construction activities, which require five times more government expenditure per unit). Third, the Program will focus resources on improving the habitat of poor and low-income households, generating health and other social benefits. Fourth, the titling of units developed in the past by INVI (currently lack full legal title) supported by this Program’s institutional development component will stimulate private property rights of the beneficiary households and build their assets.

E. Risks

- 4.18 Capacity of INVI and BNV for new operations and policy functions. Although INVI has many employees, this staff currently focuses on the direct production of housing projects. Neighborhood upgrading and on policy formulation and monitoring are new functions for the institution. Although INVI has demonstrated in the project preparation phase that it can adapt well to new operational activities such as the design of neighborhood upgrading and parcel development, nevertheless the program has to include continuing technical support. The Technical Cooperation has trained INVI staff in the methods of barrio upgrading via the preparation of three such projects under the direction of three consultants expert in the topic. These first three slum-upgrading projects will be ready to execute on Program approval. In addition, the Program provides resources (\$700,000) for long-term consultants to co-manage project execution with INVI. In regard to BNV its relatively well-qualified staff requires less technical support. Nonetheless, the organization lacks the specialized financial skills and information systems necessary to fulfill its mission as a second-tier finance institution. The Program provides resources for one type of secondary finance market – that for housing microfinance. A MIF operation provides technical

¹⁴ For example, an evaluation of the Ecuador Housing Program sponsored by IDB found that this investment had a significant impact on the mitigating the negative impact of this country’s deep recession of 1999.

- assistance for the development of BNV's capacity as a second-tier finance institution, in general.
- 4.19 Governmental transition risk: Due to its timing the Program will span across more than one administration. Elections in 2004 will result in a new government taking charge in August who might reevaluate the basis of this operation. This Program has dealt with this transition risk in three ways. First, through the extensive preparation work that enabled the involvement of all of the relevant stakeholders among the private sector (finance and microfinance organizations, builders and developers, research institutions, architects and engineering associations), non-governmental organizations (involved with community work) and community level groups. This has generated both expectations for reforms and support for the new approach proposed by the Program. Second, INVI and BNV have committed resources to launch the three investment sub-components (barrio upgrading, housing microfinance, and subsidy for new core units) on a pilot basis, which can be started in the last quarter of 2003 - before the new government takes possession in August 2004. Thus, the operation will establish methods and begin to show results prior to the incoming Administration. Finally, the operation provides key support for its investments and reforms in steps staggered over two phases to allow for the gradual absorption of changes and the Bank's participation in its adjustment.
- 4.20 Sustainability of new policies: A risk related to the above is that of the continuity of the new policies and programs supported by this operation by a new incoming administration. This risk is mitigated by both the support gathered throughout the preparation process among key stakeholder in government, private sector and civil society, which assures the consensus on the continuation of new poverty-focused housing policy, and by the Program's two-phase strategy, which will enable the Bank to maintain an active dialogue with the government on sector's policy direction.
- 4.21 Macro-economic instability. The DR is currently experiencing considerable macro-economic instability resulting, in part, from a financial crisis. Prima facie, these difficulties might appear to reduce the participation of the private sector in parts of the operation (housing microfinance, and the subsidy for new core units). However, IDB experience in countries experiencing similar financial economic and financial difficulties (e.g. Ecuador in 1999-2000, and Paraguay during the early 1990s) shows that similar housing programs can work satisfactorily under these situations, because they become one of the few options for business available to developers and financial institutions that normally ignore low/moderate-income markets. In Ecuador, for example, 90 financial institutions and many commercial developers became involved in low-income housing lending and development for the first time in 1999-2000 because of the IDB housing program, and a core group of these organizations continue to serve this market now that times have improved.

4.22 Nonetheless, although a detailed study of supply and demand for credit under the project has already been completed, the project team has updated this analysis based on the impact of recent economic and financial events.

**LOGICAL FRAMEWORK
MULTI-PHASE LOW/MODERATE HABITAT PROGRAM (DR-0141)
PHASE I**

Narrative summary	Benchmarks	Means of verification	Assumptions
End of Phase I			
<p>Poverty levels mitigated upon improvement of living conditions and welfare of the target population.</p>	<p>Upon completion of Phase I:</p> <ol style="list-style-type: none"> 1) At least 80% of the families participating in the program have access to at least three basic services (currently only 20% have access to one basic service). 2) At least 70% of the program beneficiaries report being highly satisfied with the investments in basic services, infrastructure and housing upgrades. 3) Health indicators for the population in the neighborhoods targeted under the program improve over the baseline figures, especially the incidence of waterborne disease. 4) Target population assets increase, as measured by: <ol style="list-style-type: none"> a. property values in the upgraded neighborhoods b. the value of the homes upgraded under the microfinance component 	<ol style="list-style-type: none"> 1) ECLAC report 2) Official statistics from the Central Bank and ONAPLAN 3) Baseline survey 4) Survey upon project completion 	<ol style="list-style-type: none"> 1) The country enjoys economic and political stability. 2) The financial system is stable.

Narrative summary	Benchmarks	Means of verification	Assumptions
Purpose – Phase I			
<p>Improve the habitat quality of low/moderate-income groups by increasing the supply of credit and redirecting government resources to those target groups.</p>	<p>Upon completion of Phase I:</p> <ol style="list-style-type: none"> 1) INVI resources allocated to low/moderate-income groups represent 75% of its investment. In 2002, the figure was 20%. 2) Housing credit for low/moderate-income families increases by 10% over the baseline figure. 3) 100% of housing in the upgraded neighborhoods has sanitation infrastructure and access roads. 4) 100% of housing built by the private sector under the project meets the quality standards established by the INVI. 5) 100% of the target families under the housing component are low/moderate-income families and are registered in the Unified Beneficiary Registry. 	<ol style="list-style-type: none"> 1) Baseline survey upon program startup 2) Mid-term survey 3) Survey upon project completion 4) Monitoring and evaluation system report 	<ol style="list-style-type: none"> 1) Financial institutions participate in the INVI programs because they are attracted by the lending terms and conditions the programs offer. 2) The Unified Beneficiary Registry is used and does not have any major shortcomings.
Components – Phase I			
1) Component 1. New programs for low/moderate-income groups implemented.			
<p>1.1 Subcomponent 1. Integrated neighborhood upgrading completed.</p>	<p>Upon completion of Phase I:</p> <ol style="list-style-type: none"> 1) 10 neighborhoods upgraded, with basic infrastructure and services implemented and operational 2) 8,000 families benefit from the INVI neighborhood upgrading program 3) 1,000 children receive early childhood development 	<ol style="list-style-type: none"> 1) Baseline data 2) Monitoring and evaluation system report 3) Unified Beneficiary Registry reports 4) Semiannual progress reports 	<ol style="list-style-type: none"> 1) The communities in the target neighborhoods are interested in the project and support it. 2) The government agencies involved in the upgrading programs participate effectively and in a timely manner.

Narrative summary	Benchmarks	Means of verification	Assumptions
	<ul style="list-style-type: none"> 4) 2,000 youth receive job training 5) 2,000 women receive social services and/or job training 6) 8,000 families receive sanitation and environmental education 7) There is a community organization in each of the 11 neighborhoods representing the community and serving as its voice. 		
<p>1.2 Subcomponent 2. Housing microfinance implemented.</p>	<ul style="list-style-type: none"> 1) 3,500 housing loans approved and disbursed by year 3 (average loan: US\$2,000) 	<ul style="list-style-type: none"> 1) Unified Beneficiary Registry reports 2) Baseline data and compilation of data: records of operating organizations 3) Semiannual progress reports 	<ul style="list-style-type: none"> 1) Financial institutions participate in the INVI programs because they are attracted by the lending terms and conditions the programs offer. 2) The unemployment rate does not seriously affect family income, so families can maintain their borrowing capacity.
<p>1.3 Subcomponent 3. Subsidy vouchers for land development issued.</p>	<p>Upon completion of Phase I:</p> <ul style="list-style-type: none"> 1) 3,500 core units are constructed or under construction by the private sector. 2) All the families have been selected according to the Regulations for issuing subsidy vouchers. 3) At least 5 private developers participate in the construction of core units. Currently none do. 	<ul style="list-style-type: none"> 1) Unified Beneficiary Registry reports 2) Monitoring and evaluation system reports 3) Semiannual progress reports 	<ul style="list-style-type: none"> 1) The private sector takes on a more active role in the construction and financing of economical housing because it considers the program terms and conditions attractive. 2) The subsidy system is transparent and targeted to moderate-income families.
	<ul style="list-style-type: none"> 4) The average cost of land development (provision of infrastructure) for the housing component is maintained at +/- 10% of the cost estimated during project design. 		
<p>2) Component 2. Housing policy instruments and reform implemented.</p>			

Narrative summary	Benchmarks	Means of verification	Assumptions
<p>2.1 Subcomponent 2.1. Housing policy and legal framework developed.</p>	<ol style="list-style-type: none"> 1) A Housing Policy Unit is developed and operating in the INVI by the end of year 1. 2) The information and monitoring system for housing and new construction programs in the INVI is operational by the end of year 2. 3) The Unified Beneficiary Registry is established by the end of year 2. <p>A proposal for reform of the regulatory framework for the housing sector is prepared with input from all sector stakeholders and implemented by the end of year 3.</p>	<ol style="list-style-type: none"> 1) Reports prepared by the Housing Policy Unit 2) Monitoring and evaluation system report 3) Housing Policy Unit reports on the Unified Beneficiary Registry 	<ol style="list-style-type: none"> 1) The INVI demonstrates an institutional interest in using the information system and the Unified Beneficiary Registry and a willingness to do so.
<p>2.2 Subcomponent 2.2. INVI modernized.</p>	<p>Upon completion of Phase I:</p> <ol style="list-style-type: none"> 1) Annual reports are submitted on the efficiency and equity of government habitat programs prepared by the Housing Policy Unit. 2) An action plan to improve the institutional efficiency of the INVI is prepared and partially implemented, with efficiency indicators identified. 3) The new INVI structure is implemented with downsizing of INVI staff by at least 15%. 	<ol style="list-style-type: none"> 1) Written agreement between the INVI and the financial intermediary for transfer of the portfolio 2) INVI budget performance reports 3) Resolution to establish the Housing Policy Unit 4) Housing Policy Unit reports 5) Monitoring and evaluation system reports 	<ol style="list-style-type: none"> 1) The financial conditions in the country are such that the INVI and the private sector can conclude an agreement for transfer of the portfolio. 2) There is an interest in implementing the BNV reforms and the political will to do so.
	<ol style="list-style-type: none"> 4) The INVI transfers management of 75% of its loan portfolio to a financial intermediary. 5) The INVI reduces direct housing construction to 20% of its investment budget. In 2002 direct housing construction accounted for 74%. 		
<p>3) Component 3. Support for</p>	<ol style="list-style-type: none"> 1) The execution structure is designed and 	<ol style="list-style-type: none"> 1) Report to the IDB on 	<ol style="list-style-type: none"> 1) Executing unit staff have the

Narrative summary	Benchmarks	Means of verification	Assumptions
program execution provided.	<p>implemented according to the program by the end of the first quarter.</p> <p>2) A program evaluation and monitoring system is established, operational, and producing semiannual progress reports by the end of year 1 of program execution.</p> <p>3) The information and management system on microfinance operations in the BNV is implemented by the end of year 1.</p>	<p>establishment of the executing unit and IDB statement of nonobjection</p> <p>2) Semiannual progress reports on the project indicating activities, based on the monitoring and evaluation reports and including lessons learned</p> <p>3) Reports produced by the BNV and the microfinance information system</p>	professional profile required.

Multi-phase Low/Moderate Income Habitat Program (DR-0141)

General Procurement Announcement

Principal Procurement Processes of Project	Sources of Financing		Method of Procurement	Pre-qualification	General Procurement Notices	Status
	IDB	Local/Other			Tentative Date of Publication	
1. New Investments Component						
a. Neighborhood Upgrading Component						
- Consulting Services (Firms) Project design and community development (10 contracts @ US\$ 60,000 each)	600		IPB	Yes	April 2004/October 2004 April 2005/March 2006	
- Public Works Urban Infrastructure (Water, sewage, drainage +) (10 contracts @ average US\$ 1.8 million each)	17,400	600	IPB	No	June 2004/March 2005 August 2005/September 2006	
b. Core Housing Component						
Site Development (Water, sewage, streets, +) (3 firms @ average US\$ 1.8 million each)	5,400		IPB	No	March 2004/March 2005 March 2006	
2. Support for Program Implementation						
External Auditing	100			Yes	May 2004	