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Relying on Oneself: Assets of the Poor

Marianne Fay and Caterina Ruggeri Laderchi

To an individual, anything is wealth which, though useless in itself, enables him to claim from others a part of their stock of things useful or pleasant.

John Stuart Mill (1848)

Assets: "Rights or claims related to property, concrete or abstract. These rights or claims are enforced by custom, convention or law."

Michael Sherraden (1992)

Assets are at the core of households' strategies to survive, meet future needs, improve their lot, and reduce exposure to or minimize the consequences of shocks. Many classifications of assets are possible. One commonly used typology divides them into natural assets (such as freely available natural resources); human assets (such as education and skills); financial assets; physical assets (housing, equipment, consumer durables); and social assets (interpersonal ties with individuals and groups that can be called upon to help). The institutional, cultural, and economic context in which a household lives and the types of risks to which it is exposed affect the relative desirability and usefulness of specific types of assets.

This chapter and the following two examine the assets of the urban poor, the characteristics of these assets, and the role they play in the livelihoods of the poor. This chapter focuses on physical and financial assets. Chapter 7 examines social capital, and chapter 8 looks at the role of social safety nets (public programs to help households mitigate risk and the effect of poverty). Human capital, which conditions poor urban households' access to jobs and the quality of the jobs they can access, is

Marianne Fay is a Lead Economist and Caterina Ruggeri Laderchi an Economist at the World Bank. The authors are grateful to Sonia Hammam and Paavo Monkkonen for comments and suggestions.

discussed in chapter 3. Since natural assets are less important in the urban economy than in the rural one—common property resources are rare, and households are integrated into the monetary economy—they are not directly discussed here.[1] Physical and financial assets together constitute material wealth. In economic terms they represent purchasing power stored for future use: by putting money in a savings account, for example, households forgo current consumption, storing their wealth in a form in which they can access it later. This process of transferring purchasing power over time is subject to risks. These include the risk of being unable to sell the asset for its original value (risk of depreciation), the risk that the expected increase in the value of the asset is not realized (uncertain returns), and the risk that the claim to the resources stored in the asset cannot be realized (lack of enforceability). Liquidating an asset usually involves transaction costs, particularly when the market is thin or illiquid.

Despite these possible drawbacks, financial and physical assets represent the first source of security for households in weathering shocks and financing predicted future expenditures related to life-cycle events. The 2001 U.S. Survey of Consumer Finances finds that the two main reasons for savings are for retirement and for liquidity reasons, such as the sudden need for cash or to cope with unemployment or illness. Other types of assets require a more complex process of transformation to yield purchasing power. For example, to draw on human capital, one needs to first find an employer and then to perform the necessary labor. Human capital thus provides less flexibility than other types of capital.

Households also accumulate physical and financial assets (henceforth referred to as "assets" unless otherwise specified) for reasons other than consumption smoothing and security.[2] They save in order to improve consumption over time (through the accrual of capital gains); acquire a higher social status (either by displaying some sign of "wealth" or by contributing to networks of reciprocity); provide resources for one's children; and accumulate in order to finance future entrepreneurial activities or the future purchase of costly items. As poor households are likely to be constrained in their access to credit for either business or consumption, this last motive can play an important role in their accumulation strategies.

This chapter examines how the poor accumulate assets and the use they make of them. It then reviews the types of assets available to the urban poor and analyzes whether these are in fact good assets. The third section addresses the three key policy questions: how to increase the ability of the poor to save; how to improve the quality of the assets they hold, in terms of liquidity, riskiness, and rate of return; and how to broaden the range of assets available to them.

Good Times and Bad: How the Urban Poor Accumulate and Use Assets

The bulk of the literature on the savings and coping behavior of the poor is based on rural studies. Little research has been conducted specifically on the saving behavior of the urban poor and on the type of assets they accumulate. This is all the more unfortunate given that saving patterns and instruments of the urban poor are likely to differ from those of the rural poor, for a variety of reasons:

- The high (if not total) integration of the urban poor into the market economy is likely to result in accumulation patterns in which financial assets are a priority. The availability of cash can limit access to key resources (such as food or health care). In urban areas it plays a primary role in dealing with shocks. In contrast, in rural settings there is greater reliance on natural resources and in some cases traditional institutions (such as healers) as service providers.
- The causes of vulnerability are different in urban and rural settings, requiring different types of assets and coping strategies. The urban poor are more affected by what Glewwe and Hall (1998) call "market-induced vulnerability" rather than weather variability. This tends to result in idiosyncratic shocks (such as a household member losing her job) rather than covariant shocks (such as a large set of households suffering because of a bad crop). Poor urban households seem to engage in risk management strategies based on diversifying income sources.
- The savings instruments of the poor face different challenges in urban and rural areas. Informal arrangements (either savings or insurance based), for example, are less susceptible to covariant risk, due to the diversification of activities in urban areas, but they face greater problems in terms of enforcement, due to the higher mobility of individuals (Morduch 1999).

Acquiring Assets: The Savings of the Poor

The poor clearly save—how else would they cope with the occasional need for lump sums of money? Indeed, savings are likely to represent the most important way in which poor people today can accumulate assets (other ways of accumulating assets include inheritance, marriage, or redistribution by some third party, generally the state).

The difficulty comes in measuring their savings, since the poor are usually excluded from formal financial markets. As a result, they save by accumulating anything from consumption goods (such as food) to semidurables (such as clothing) to durable goods (such as furniture, equipment, and housing), as well as cash or contributions to informal institutions or networks of reciprocal obligations.[3] It is therefore difficult to identify how and whether poor people are saving, given that the assets they hold have both consumption and investment value (box 6.1). More generally, the measurement of savings through household survey data is complicated and plagued by concerns over measurement error (McKay 2000).[4]

There is little quantitative evidence on the savings of the poor in Latin America and the Caribbean, and what there is may not capture the complex means by which the poor save. Szekely (1998) suggests that the bottom 30 percent of Mexicans are unable to save at all. This notion is hard to reconcile with the fact that homeownership among poor Mexican households is more than 65 percent (World Bank 2005).

Both demand and supply factors affect the extent to which poor people can save. On the demand side, scarce resources and the need to satisfy immediate survival needs limit the extent of savings. Poor households, however, function in a highly volatile environment, which is likely to provide a strong incentive for saving to build up buffers against consumption shocks (Morduch 1999). This motivation is all the more powerful if access to credit and insurance markets is limited or costly. Furthermore, poor people's reported risk aversion, arising from the potentially disastrous consequences of not being able to face adverse

Box 6.1 How the Poor Save and Draw on Their Assets: Illustrations from *The Children of Sánchez*

The Children of Sánchez, by Oscar Lewis, is an account of the life of a poor family in Mexico City. Although the book, a classic of anthropology, was published in 1961, excerpts from it sound remarkably contemporary:

"I spent the whole night in a sea of confusion and tears, wondering how to get the money. I would sell or pawn my clothes or borrow from a loan shark no matter how high the interest was."

—Consuelo

"I hated to sell the watch, because it was only one week old. The week before I had received 400 pesos from a *tanda* [rotating savings pool] I had joined with other neighbors, and I used the money to buy myself a watch and a jacket.

To get off to a good start…Baltasar offered to pawn his new radio and pay five months rent in advance, so that we would have a place to live.

We did not have a single *centavo* in the house, and Baltasar had no money to work with, so we sold the pig my father had given us, before it was fully grown."

—Marta

shocks when living conditions are already so precarious, should provide a further incentive to save.

The evidence on this issue is conflicting. A few studies (see Lawrance 1991 and literature quoted therein) have sought to test differences between rich and poor in terms of their "time preference" (interpreted as the willingness to forgo current consumption in favor of future consumption). They find that all else equal, poor people are less "patient" than the rich and therefore less willing to forgo consumption and save. This conclusion may be due to the fact that these studies do not disentangle poor people's preferences from all the other factors that may distinguish them from the nonpoor, notably the immediacy of their needs.

On the supply side, institutional features, such as the lack of good savings instruments and the costs associated with the available ones, constrain poor people's ability to save. In the United States it has been estimated that the difference in asset accumulation by rich and poor can be ascribed largely to differences in the ability to accumulate assets rather than to different ways of responding to incentives (Ziliak 1999). The importance of supply constraints for savings is supported by the microcredit literature highlighting poor people's ability to save when appropriate tools are provided (Johnson and Rogaly 1997). Furthermore, some of the informal institutions that poor people rely on can actually prevent accumulation: reciprocity networks can prevent enhancement of one's economic position because of network members' claims to the resources generated by "successful" members (Rosenzweig 2001).[5]

Bad Times or Opportunities: Drawing on Household Assets in Times of Need

Much can be learned about the role of assets in poor people's livelihoods by considering how they are used. The (rural-based) literature on responses to famine highlights two important ways in which households behave when they need liquidity or have to cope with adversity.

- *Tradeoffs.* Households trade off short- and long-term objectives when choosing which asset to draw on, as well as when choosing asset depletion over other coping strategies (for example, taking a child out of school to work). This is particularly evident when productive assets are involved and choices have to be made between changing consumption patterns and depleting the asset stock.
- *Sequencing.* Assets differ in terms of their liquidity, "lumpiness," and risk (Devereux 1993), as well as in the perceived irreversibility of their sale and its consequences for a household's future income streams.

> Households, therefore, do not draw on their assets randomly but rather sequence their responses based on their overall portfolio of assets and their characteristics (such as the type of productive activity they engage in and the other coping strategies they have adopted).

Poor households in Argentina and Uruguay adopted a variety of asset-based strategies in response to the economic crisis in 2002 (box 6.2). In Argentina changes in consumption patterns appear much more frequently than any of the asset-based strategies (90 percent of households in the first quintile decreased food consumption, with 98 percent of them buying cheaper food products). In Uruguay having lived off savings in the past increased the chances of relying on selling, mortgaging, or pawning assets.

The fact that households make rational decisions in choosing a coping strategy, however, does not mean that these strategies are necessarily optimal (Morduch 1999; Skoufias 2003). They may jeopardize earning prospects or have deleterious consequences on certain household members (by reducing learning as a result of decreasing spending on learning inputs, for example). Policy interventions may be needed to provide households with alternative assets or coping strategies (as discussed in the last section of this chapter). Such interventions may be all the more necessary as households may be accumulating assets whose value and returns are vulnerable to the effects of the crisis, so that their effective possibilities of coping are curtailed.

Bicycles, Houses, and Cash: The Assets of the Urban Poor

Households' well-being and security ultimately depend on the combination of assets in their portfolios. Unfortunately, the portfolio held by the poor may be suboptimal, because poor people need to limit income risks and smooth consumption and they lack access to appropriate savings instruments or credit and insurance markets (Rosenzweig 2001). Thus a household may forgo acquiring an asset with secure returns if such an item could be difficult to liquidate in case of need. The returns to an asset depend on the complementarity with other assets held (for example, between human capital and access to credit) as well as the complementarity between the private and public assets available (for example, tools and electricity). In Peru, Escobal, Saavedra, and Torero (1999) find that the cross-elasticities between one additional year of education and access to land are positive and progressive (that is, higher for the poor than for the rich).

The implication, then, is that the characteristics of a good asset depend on the particular needs of a household, the context facing it, and the available

Box 6.2 Drawing on Assets Following the 2002 Economic Crisis in Argentina and Uruguay

Following the economic crisis in 2002, households in Argentina and Uruguay were asked about the coping strategies they adopted. The results of the specialized surveys are summarized below.

Argentina

- The crisis resulted in a significant increase in the use of asset-based coping strategies: the percentage of households selling or pawning belongings rose by a factor of four (to 2.8 percent). Alternatives included informal borrowing from family or friends (11 percent of households); relying on store credit (7 percent); drawing on savings (5 percent of households, representing 12 percent of those who reported having savings); and borrowing from banks (2 percent).
- The use of coping strategies varied by income level. Among those in the bottom quintile, 6 percent sold assets (1 percent in the top quintile), 3 percent drew on their savings (8 percent in the fourth quintile), and 15 percent relied on store credit (1 percent in the top quintile). Interestingly the second quintile relied most heavily on borrowing from banks (3.6 percent), while just 2.0 percent of the top quintile borrowed.
- Multivariate analysis shows that households whose members lost a job had a 40 percent higher probability of liquidating their assets by selling or pawning and were 3.4 times more likely to draw on savings. In contrast, households that reported a generic loss of income but not a job loss following the crisis were 2.6 times as likely to sell or pawn assets and 16 percent more likely to draw on savings. These differences may be due to the different expectations about future income flows by people who experienced different types of income shocks.

Uruguay

- Some 68 percent of households reported to be relying on at least one strategy based on financial or physical assets (drawing on savings or selling, mortgaging, or pawning goods), and 53 percent of those who did cited living expenses as the reason for doing so. Taking informal loans and monetizing the value of assets were the two most important "new" strategies that people adopted after the crisis.
- Multivariate analysis shows that rich people were more likely to draw on savings and credit, while people in the bottom three quintiles of the wealth distribution were more likely to sell, mortgage, or pawn assets.
- Households appear to be sequencing their responses. All else being equal, those who experienced negative income shocks were more likely to draw on savings. Households experiencing an emergency, particularly a severe emergency, that was more serious than they were used to relied on monetizing the value of their physical assets. Having lived off savings in the past increased the chances of relying on selling, mortgaging, or pawning assets.

Sources: Fiszbein, Giovagnoli, and Adúriz 2002; Fiszbein, Giovagnoli, and Thurston 2003; Ruggeri Laderchi 2003.

portfolio choice. In addition, there are some "absolute" characteristics that make an asset more or less desirable.

For assets to perform their primary function as a store of value, they should provide adequate returns, or at the very least, not depreciate. Inflation presents the greatest threat of depreciation for financial savings. For physical assets, such risks depend on the depth and volatility of the secondary market in which the asset can be liquidated. In the case of a large covariant shock, if many affected households sell their belongings in a shallow market, prices fall significantly. Financial savings, therefore, represent a better asset than physical assets, provided there is macroeconomic stability and a reliable banking system.

Poor households facing a limited choice of savings instruments are often willing to hold assets even when their returns are low (as, for example, in the case of rotating savings schemes). Valuation of an asset also needs to take into account its nonmonetary returns, whether in kind (for example, the use value of housing or appliances), in status within the community, or in inclusion in some reciprocity network. Risk aversion may also play a role in poor households' holding of low-risk, low-return assets.

For poor people who have limited access to formal financial savings and credit instruments, another important role of assets is to help them manage small balances and deal with cash flow problems. Good assets for the poor allow for high-frequency operations of limited size and for flexibility. Examples of assets that offer the possibility of high-frequency operations are rotating savings pools, such as Mexico's *tandas,* to which 20 percent of urban Mexican households belong. In order to be appropriate for frequent small-scale operations, good assets should involve moderate transaction costs. This can represent a barrier to the expansion of formal financial services to the poor, as instruments devised for larger operations, such as creditworthiness assessments, may involve lengthy and expensive administrative procedures. To avoid these costs, microcredit programs rely on alternative ways to assess whether they can trust their clients, such as group responsibility.

Consumer Durables

Durables (furniture, consumer appliances, bicycles) play an important role in the asset portfolios of the urban poor, because they offer the opportunity to invest relatively small amounts and can be easily pawned or resold. Uruguayan households' responses to crises suggest that poor households are more likely than richer ones to sell home furnishings but less likely to sell more expensive durables, such as cars. Where labor is cheap, the life of durables can often be extended with small improvements and repair. The stream of consumption benefits and the option of selling the asset can therefore be extended almost indefinitely. Extending the life of semidurable goods (such as clothes or dishes) offers an opportunity for households to resort to an "internal capital market" (Browning and Crossley 1999).

Housing

Housing is likely to be the most valuable single possession that poor urban households have. In addition to providing shelter, it also plays a more standard role as an asset, one whose main modality of acquisition for the urban poor (progressive housing, discussed in chapter 3) offers the opportunity for small incremental investments. Evidence from specialized surveys on risk management in Chile and Peru finds that investment in housing and other residential property acts as a substitute for formal retirement systems (Gill, Packard, and Yermo 2004). Indeed, as discussed in chapter 3, most landlords tend to be small scale and substantially older than their tenants or other homeowners.

But is housing such a great asset to hold? Being a homeowner does have a variety of advantages. It provides a constant flow of services, and it frees low-income households, who typically improve their houses gradually based on the cash on hand and generally "own" their home outright, with no debt and mortgage, from the constraint of having to generate a fixed sum for rent every month. This can be important, especially at times of crisis. For example, in Uruguay 10 percent of renters declared that they had to move following the crisis in order to cut down on housing costs, and 4 percent of households (7 percent in the bottom quintile) declared they had to merge with other households rather than just rent a cheaper home. Furthermore, housing services can be monetized quite easily, by taking renters or additional household members in.

Being a homeowner may also have some downsides, particularly in the presence of thin or poorly developed resale or rental markets. Home ownership can tie the poor to undesirable locations—locations that are unsafe because of crime and violence or the risk of natural disasters, locations that are removed from the main labor market centers, or locations that may carry stigma, making job search more difficult.[6] It is unclear how liquid or buoyant housing markets are, particularly in poor neighborhoods. Work on the *favelas* of Rio shows the picture to be complex. In some *favelas*, rental and sales prices are higher than in parts of Copacabana or Botafogo (middle-class neighborhoods). In others, residents complain about the stigma associated with their neighborhood, which makes it difficult to get a job ("If you interview for a job, and they see your address, they say the job has been filled"), or the exploding crime and violence, which make it difficult to sell their homes (Perlman 2003).

There is a debate in Europe and the United States as to whether homeownership limits labor mobility and therefore contributes to a high equilibrium unemployment rate. One argument is that homeownership makes it expensive to move (Oswald 1996,) and is therefore correlated with higher unemployment, at least for middle-age households (Green and Hendershott 2001). Most studies, however, find either no relationship between homeownership and unemployment (Robson 2003 for the United Kingdom; Flatau, Forbes, and Hendershott 2003 for Australia) or that homeowners actually fare better than renters in the labor market (Coulson and Fisher 2002 for the United States; Van Leuvensteijn and Koning 2004 for the Netherlands; Munch, Rosholm, and Svarer 2003 for Denmark). One explanation is that even if homeownership reduces labor mobility, individuals may accept lower reservation wages in order not to have to move (see Munch, Rosholm, and Svarer 2003 for a review of the literature).

Labor mobility is much more likely to be affected by the buoyancy and dynamism of the housing market. In fact, there is evidence that regions with relatively high housing prices exhibit lower unemployment (Robson 2003). In addition, while the incidence of private rental shows no relation with unemployment, public (social) rental and rent control tend to be associated with higher unemployment (Robson 2003; Munch, Rosholm and Svarer 2003). Thus the issue is clearly not simply one of owning or renting one's home.

There is very little research on the liquidity or buoyancy of low-income housing markets in developed or developing countries. The only source of systematic analysis is from the United States, where recent work has sought to determine whether housing is a good asset for low-income families (box 6.3). Some of the limited data and research in the developing country context are reviewed here.

Housing Exchange Value

Little information is available on the secondary housing market in poor neighborhoods. The presumption is that the market is not very developed, given poor households' preference for progressive housing. The limited research available suggests that low-income settlements tend to be dominated by a land market rather than a housing one, as low-income households prefer to acquire land for self-help housing rather than finished housing (Gough 1998). The research also shows that about half of households that do acquire finished housing in low-income neighborhoods previously built a home themselves, having originally entered the housing market through self-help construction.

Box 6.3 Low-Income Homeownership: Examining the Unexamined Goal

Homeownership is a valued and promoted goal of the U.S. government, which has aggressively developed policies to make it an attainable goal for all, including poor households and minorities. Access to credit is generally no longer a binding constraint; keeping up mortgage payments and finding inexpensive homes to buy are now the key issues for poor households. Until recently, no research had documented whether homeownership is in fact good for low-income buyers, for their communities, or indeed for the country. A large research project funded by a number of housing-related organizations has attempted to shed light on the issue.

Building Families' Financial Capital

Behind the push for homeownership for the poor is the notion that it is a good asset-building strategy for them. Because the poor seldom hold any kind of financial wealth and are much less likely to have pensions, the question of whether they manage to build housing wealth through homeownership is an important one. The answer in the United States is yes, in most cases. Although housing prices do fluctuate, most lower income owners benefited from housing price appreciation and actually fared better than those who bought higher priced homes. Homeownership also constitutes enforced savings. And despite the fact that the housing market has historically earned lower returns than the stock market, and an even poorer risk-adjusted return, low-income households receive a host of financial benefits from owning—most of all the promise of fixing the housing cost, so that it does not rise with inflation or population pressure. Finally, in the United States, where mortgages are available with very low down payments, low-income borrowers are able to risk relatively little money on a home today in pursuit of potentially high leveraged returns later. This option is not available to poor people investing in financial instruments.

Building Families' Social Capital

Advocates firmly believe that homeownership makes families happier and more stable and children more successful at school. Yet is that stability desirable? Is a renting family better able to move to find better jobs or schools? Research finds that children in owner-occupied homes do better in school, but this could be because of a self-selection factor: parents are more concerned and therefore seek a home in a safer neighborhood with better schools. Similarly, while there is evidence that homeownership provides people with a greater sense of control over their lives, spurs them to greater civic participation, and helps their children do better, it is also true that delinquencies and default—something the poor are at risk of—have the opposite effect. Overall, however, the answer to whether homeownership is a positive thing for families seems to be a tentative yes, if only because children of homeowners have a much higher propensity to become homeowners themselves later on.

(box continues on the following page)

Box 6.3 (*continued*)

Contributing to Community Capital
Mayors and city councilors generally exhibit blind faith that homeownership will resurrect neighborhoods in decline, although there are few studies of the issue. Recent seminal work does show a demonstrable positive impact. But homeownership alone is no panacea. Renovation and rehabilitation of housing, combined with promotion of homeownership, can be potent forces.

In sum, it appears that the popular dream of owning a home is probably a rational aspiration for low-income families and that the renewed efforts in the United States to bring low-income homeownership rates closer to that of better-off families should continue.

Source: Adapted from Retsinas and Belsky 2002.

The relative importance of the land and housing market may be linked to the age of a settlement (Gough 1998). Turnover is quite high in recently occupied settlements (especially invasions), where residents attempt to cash in on the value of the land by selling the rudimentary shelters they have built to establish their claim. Subsequently, little exchange of houses takes place for decades, because even in later stages of consolidation, most newcomers acquire land rather than finished housing (Datta and Jones 2001; Gough 1998). One of the very few studies of the low-income housing markets, conducted in Pereira, a medium-size city in Colombia, finds that only about a quarter of households in poor neighborhoods had bought their house (peaking at 59 percent in areas settled through invasion). In addition, 87 percent of homeowners had performed major renovations or extensions on the purchased property, suggesting that they had not purchased finished housing (Gough 1998).

The limited evidence available is not very conclusive, although it does suggest that the low-income housing market is not very liquid. In the Pereira study, for example, selling a home was difficult. In addition, that study and others suggest that few households actually want to sell: the hardships suffered during acquisition and consolidation result in a strong attachment to the property (Gough 1998; Datta and Jones 2001).

Nevertheless, a survey of Mexican *barrios* indicates that a good share of new arrivals and recent movers purchase used housing: more than a quarter of households that had migrated in the past five years and owned the home they live in lived in a house that predated their arrival. Even more encouraging, three-quarters of the home-owning households that had moved the previous year moved to a preexisting home (Ruggeri Laderchi 2003). However, given the small number of households that migrated or changed homes recently, these figures cover no more than about 3.5 percent of all owner-occupied homes in poor neighborhoods.

The development of secondary markets for low-income housing is likely to be affected by limitations on new constructions and illegal settlements. Such limitations work against new arrivals and in favor of older settlers. Other factors are the availability of housing finance and possibly the strengths of property rights, discussed below.

Most housing finance systems in Latin America and the Caribbean work against the development of a secondary market for low-income housing, because they generally do not serve the poor; where they do, they tend to explicitly exclude financing for "used housing." One of the key aspects of the more promising low-income housing finance schemes, such as those in Chile and Costa Rica (discussed in chapter 3), is to allow for purchases of used housing.

Security of tenure increases the exchange value of a house in several ways. First, recognized property rights contribute to creating a market. The data from Mexico's *barrios* show that the share of households that own a house built before their arrival is higher in older settlements, where supposedly more mature institutional arrangements prevail and property rights, formal and informal, are better established. Second, there is a presumption that prospective buyers would be willing to pay a premium in order to purchase property whose ownership is clearly established. Evidence from many surveys supports this claim. Following the massive titling campaign that occurred in Peru between 1996 and 2001, 64 percent of newly titled homeowners considered that the title increased the value of their home, and three-quarters believed that the title increased ownership security (Mosqueira 2003).

Security of tenure also has additional indirect effects on the value of a home, through "neighborhood quality." Titles often make it easier to access utilities—in some countries, such as Mexico, utilities, road, and transport services cannot be provided until a settlement's status is legalized—so that as communities become legalized they tend to benefit from more public services. Hoy and Jimenez (1996) provide evidence from squatter communities in Indonesia where increased titling led to increased availability of local public goods. This, combined with the fact that secure homeownership often translates into more investment in homes, results in a price differential between nonsquatting and squatting sectors of cities.

The advantages conferred by formal tenure vary, however. Recent analysis has identified a number of factors other than formal titling that contribute to tenure security, including age of the settlement, existence of public services, and presence of community leaders (Lanjouw and Levy 2002). This work, conducted in Guayaquil, Ecuador, finds that the age of the community, the presence of a community organizer, and a formal title substitute for each other as sources of transferable claims to sell or rent property. Thus the value of a title is lower in older, more established, and better organized communities. Household characteristics seem to matter too, since having a title is associated with larger gains in expected sale prices for female-headed households, who presumably may be less able to enforce their claim to a house.

OTHER RETURNS TO HOUSING

The returns to housing as an asset include the flow of housing services it provides, some of which can be monetized in case of need by taking in tenants or extended household members who share in the upkeep of the household. Indeed, as discussed in chapter 3, the bulk of landlords in Latin America and the Caribbean are homeowners who let out rooms or parts of their house (Rakodi 1995). While surveys and interviews with these small-scale landlords suggest that this is not a very profitable way of investing their resources, renting is perceived as offering a number of benefits (box 6.4).

Returns to housing also include better access to credit by providing collateral, although this is generally dependent on having formal tenure. In Peru access to formal credit increased from 7 percent to 42 percent among beneficiary households, while recourse to informal credit decreased from 31 percent to 9 percent following the titling campaign (Mosqueira 2003).

Formal tenure can also affect the returns of the overall portfolio of resources by freeing up labor otherwise engaged in protecting insecure property rights and allowing home businesses to move into more appropriate locations. In Peru formal titling increased labor force participation, due to

Box 6.4 How Profitable Is Small-Scale Landlordism?

Surveys and interviews with small-scale landlords in Guadalajara and Puebla, Mexico, reveal that they believe renting is not a very profitable activity but that it offers a number of advantages. Renting out a room or a floor of their house generates resources for housing improvements. It also provides temporary income in times of need and makes use of accommodations built to one day house a child's or relative's family. A number of landlords indicated that rental accommodations could provide a modest income during their old age. Many seemed to admit that beyond investing in bricks and mortar they did not know what to do with their limited savings. Small-scale landlords are thus motivated by a mixture of factors related to family, old age, and the lack of perceived alternatives.

Source: Gilbert and Varley 1991.

the reduced need for constant presence in the house (to demonstrate ownership) and the time required to pursue formalization. The result was a substantial increase in family income, as well as a significant decline in child labor, for which adult labor was substituted (Field 2002; Mosqueira 2003).

Finally, homeownership in the United States has been shown to be associated with higher social capital and better educational outcomes for children, possibly due to greater social capital and stability (see box 6.3). Whether such findings are applicable to poor neighborhoods in developing countries is unclear.

Financial Assets

Financial exclusion and the reliance on informal financial tools and physical assets are likely to result in portfolios whose return and liquidity characteristics do not compare favorably to those of the better-off. Matin, Hume, and Rutherford (1999) argue that improved access to financial services induces the following changes in the composition of a household's assets and liabilities:

- A decline in the holding of assets with lower risk-adjusted returns.
- A shift away from assets held for precautionary savings toward assets held for speculative purposes.
- A decline in the level of credit obtained at high cost (usually from informal sources).
- A decline in the frequency and amount of asset sales at low price.

When looking at financial services for the poor, savings, credit, and insurance need to be considered as a continuum. Lacking access to insurance, the poor typically rely instead on a combination of savings and credit as alternatives. As a result, the main motivation in using financial services tends to be risk management rather than the expected return of the financial service; the "protective role" dominates over the "promotional role" (Matin, Hume, and Rutherford 1999). This is likely to be equally true of the rural and urban poor.

The vast majority of households in Latin America and the Caribbean have no access to formal financial services, either savings or credit. This is certainly the case in rural areas, but even in cities access to financial services is limited: 80 percent of households in metropolitan Mexico City and 60 percent in urban Brazil are "financially excluded" (World Bank 2003a, 2003b). In contrast, only about 13 percent of families in the United States and 7 percent in the United Kingdom have no bank account.

Financial exclusion is a phenomenon that primarily, although not exclusively, affects the poor. In urban Brazil only 15 percent of the population in the lowest decile have bank accounts, while about 80 percent of the top decile do. In Mexico City the situation is even worse: only about 6 percent of the bottom half of the income distribution have access to formal financial services, while 34 percent of the upper half do. The poor account for about 16 percent of the population with bank accounts, suggesting that being poor does not preclude interest in banking services or make it necessarily unaffordable.

Lacking a bank account has costs. It makes it more expensive to engage in many transactions, such as paying or being paid.[7] Most important for the topic at hand, it makes it more difficult to save while maintaining the value of an asset. As a result, a relatively small proportion of people without bank accounts hold financial savings (28 percent in urban Mexico) (World Bank 2003a).These financial savings are held in a variety of ways: cash under the mattress, loans to relatives or friends, and informal savings institutions. Cash under the mattress loses value with inflation, and it is vulnerable to theft. In a survey of access to banking services in Brazil, two-thirds of respondents identified security as the main reason for wanting a bank account (World Bank 2003a). Little information is available about informal loans to relative or friends; it is unclear whether interest is charged or repayment is timely. As to informal savings institutions, their attractiveness in terms of products offered varies (box 6.5).

The microfinance "revolution" has increased access to loans for small businesses and, to a lesser extent, low-income households. Microfinance expansion is occurring along four different paths: servicing of "downscale" customers by commercial banks; licensing of nonbank financial intermediaries, including transformed microcredit NGOs and specially licensed microfinance institutions; start-up commercial microfinance institutions; and alliances between commercial banks and nonbank financial intermediaries, through agents or on-lending relationships.

These approaches have resulted in more efficient and broader outreach and the development of products better suited to small-scale borrowers. Lending to households by microfinance institutions is now showing more dynamic growth than microenterprise credit. Further progress can certainly be made; the reach of microfinance varies substantially across countries, and more can surely be done to further increase access to credit for the poor in a way that neither puts the poor in an unreasonable level of indebtedness nor threatens the creditworthiness of the lenders (CGAP 2001). Overall, it is clear that there is now a model that works and can be further rolled out.

Similar progress has not been made in increasing the poor's access to saving instruments. Such access is probably even more important than access to credit, particularly for the poorest.[8] For people living in urban

Box 6.5 Informal Savings Institutions in Mexico: *Tandas, Clubes,* and *Cajas de Ahorros*

Tandas are rotating savings pools that operate as both loans and savings instruments. A *tanda* might work as follows: a group of 20 people agree to contribute Mex$200 a week to a common pool for 20 weeks. Each week the proceeds are given to one member of the pool (who does not contribute that week). *Tanda* members who receive funds early effectively receive a loan that they pay off in equal monthly installments until the end of the cycle. Those who receive money at the end of the cycle effectively save with each pool contribution until the final withdrawal.

Anecdotal evidence suggests that *tandas* are usually made up of 5–20 "partners," each contributing Mex$10–Mex$20 on a weekly or biweekly basis. The prevalence of *tandas* in low-income communities shows that the poor have both the capacity and the willingness to use financial services, even with small amounts.

The *tanda* is critical to many poor Mexicans. In their own words:

"My *tanda* is sacred. I cannot fail to make a payment because it hurts the others."

"I participate only if I know I can fulfill my obligation. I'd rather not eat than fail to make a payment."

"My savings are small, but drop by drop they make a puddle. In the bank they want us to save large quantities and they ask for a lot of papers. I prefer my *tanda*."

Clubes are similar to *tandas* but are managed by stores. A group of individuals makes regular and equal payments to the store in return for an article for sale. The articles may vary from person to person, but the amounts paid are usually the same. *Clubes* select the weekly or biweekly winner in different ways, but most involve a social meeting and a game of chance, such as a door prize or bingo.

Cajas de ahorros include 15–50 members associated by a common place of work or through a church. Unlike a *tanda,* a *caja* usually requires a full year's commitment, after which members can withdraw their accumulated savings with interest, depending on the *caja*'s earnings throughout the year. C*ajas* also make loans to members and nonmembers (when recommended by a member).

Source: World Bank 2003b.

slums, it is very difficult to protect savings from theft, inflation, or the demands of everyday living. Because the poor tend to hold their financial savings in cash or in informal arrangements, they tend to be less protected than the rich against macroeconomic instability. Uruguay offers a case in point: 53 percent of those in the top wealth quintile but just 36 percent of those in the bottom decile declared not to have been affected by the 2002 financial crisis (Ruggeri Laderchi 2003). Most surveys show that a savings account is the product people without bank accounts are most interested in (after payment services) (World Bank 2003a, 2003b).

More, Broader, and Better: How to Improve the Poor's Asset Base

Increasing savings is hard for poor households, given scarce resources, the demands of everyday living, vulnerability to shocks, and the lack of good instruments. The pattern of accumulation is often suboptimal, because the poor are excluded from credit and insurance markets and because available savings instruments do not meet their needs. Given these mismatches and market failures, policies to strengthen and expand poor urban households' asset bases can play an important role. The key issues are how to increase household savings; how to broaden the range of assets accessible to the poor, particularly savings instruments; and how to make housing a better asset, since regardless of alternatives, housing remains the largest store of value held by all but the richest households.

More: How to Increase the Urban Poor's Asset Base

In general, it may be difficult to devise targeted policies to increase the savings of specific groups (Banks, Smith, and Wakefield 2002). In the case of the urban poor, however, policy changes could relax some constraints.

Increasing household resources is a first obvious way in which a household's ability to save could be increased. Policies of this type also help reduce the inherent tension between households' long- and short-term (survival) needs.[9] A wide variety of policies can be classified under this heading. Conditional cash transfers, such as Mexico's Oportunidades, discussed in chapter 7, in which poor households receive monthly cash allocations in exchange for continuous school and preventive health clinic attendance, increase income while promoting positive behavior. Creating employment and increasing access to education and training, providing security of tenure for housing, and providing basic services and infrastructures are other examples of policies that raise the returns to households' assets, either directly or by freeing household resources for other uses. For example, the provision of water or secure property rights allows household members to find more productive uses for their time. Indeed, recent work by Calderón and Servén (2004) shows that improved access to infrastructure, particularly water and sanitation, reduces income inequality.

Decreasing households' vulnerability to risk and protecting assets at times of crisis can also help increase savings by providing greater incentives for households to save in different assets than they would otherwise. As part of their risk management strategy, households save in relatively liquid items, which tend to be low risk and low return. Additional instruments, such as insurance mechanisms (including catastrophic insurance for the poor, discussed in chapter 3) or public schemes (including workfare and noncontributory pension schemes, reviewed in chapter 7), could provide households with incentives to create more efficient portfolios. Efforts currently under way to develop microinsurance programs could also improve the risk management options available to the poor (http://www.microinsurancecentre.org).

Better: The Housing Issue

Housing tends to be the most valuable asset held by the poor, and it is likely to remain so even if the poor are provided with good alternative savings instruments. Even in developed countries, such as Belgium and the United Kingdom, the only form in which the poor hold wealth is home ownership (Van den Bosch 1998). Thus improving the assets held by the poor will necessarily entail making the low-income housing market more liquid. Policy options for doing so include housing finance schemes for the poor that allow a secondary market to develop (such as the schemes in Chile and Costa Rica), titling, slum upgrading, and better provision of services (see chapter 3). Improving services, including transportation links in poor neighborhoods, will typically translate into both an increase in property values and easier resale. Reducing crime and violence in poor neighborhoods can help a secondary market develop.[10]

Broader: Increasing Access to Financial Services

How can policy makers broaden the range of assets that the poor can access? Savings, access to credit, and insurance mechanisms form a continuum in helping the poor cope with risk and vulnerability. Access to credit has increased significantly thanks to the "microfinance revolution," but more can be done. And much more needs to be done to increase access to good savings instruments and insurance, which lag behind credit.

A full discussion of the policy reforms that can help promote more access to banking services by the poor is beyond the scope of this chapter (for a discussion in the context of Latin America and the Caribbean, see World Bank 2003a, 2003b). Briefly, some of the approaches that have been advocated for the formal banking sector include the following:

- Reduce the cost of banking products. This can be done by encouraging banks to offer "lifeline" accounts with low or no minimum balance requirement and no option for overdrawing the account; promote competition and the use of new technology (personal digital assistants, smart cards, and handheld computers) by banks to reduce transaction costs.
- Reduce the remoteness of banks from the poor, by setting up automatic teller machines in vans and supermarkets, for example, and creating a less formal atmosphere in banks targeting poorer clients.
- Reduce the lack of familiarity between poor households and banks, by creating financial literacy programs, publishing information on the profitability of reaching down, and encouraging large employers to pay their employees through electronic transfers rather than checks.

The reach of microcredit could be increased by adopting best practice approaches (see, for example, www.cgap.org). Given their proximity and cost structure, microfinance institutions are better placed than formal banks to offer savings services to the poor. The poor save, but they do so in small, uneven increments. A savings instrument that fits their needs is one that allows frequent deposits with low transaction costs. This requires physical proximity and accounts that do not require high minimum balances. In addition, the microfinance institutions would benefit from the additional sources of funding that savings deposits would create. Unfortunately, microfinance institutions in most countries are either prohibited by law from offering savings accounts or are limited by high levels of minimum capital required to accept deposits. Countries in which the sector is sufficiently mature should contemplate letting microfinance institutions accept deposits. Doing so may require modifying the regulatory structure.

In sum, the urban poor do accumulate assets, but they are constrained in their choices—because of their lack of resources, their risk aversion, and the lack of savings and insurance instruments adapted to their needs. As a result, they probably overinvest in housing and durable goods and underinvest in financial assets. Policy measures to make housing a more liquid asset and increase access to financial services are therefore essential to help the urban poor cope with poverty and vulnerability.

Notes

1. There is nevertheless evidence of the importance of urban and peri-urban agriculture in providing access to food and incomes for the poor (Bakker 2000), pointing to the importance of access to land for more than housing purposes.

2. Matin, Hume, and Rutherford (1999) suggest three main motivations: life-cycle needs, such as burial, childbirth, education, and old age; emergencies, including personal emergencies, such as sickness or injury, death of a breadwinner, loss of employment, theft, and impersonal emergencies, such as war, floods,

and fires; and opportunities to invest in a business or acquire a plot of land on which to buy a house. See also Browning and Lusardi (1996) on the motivations for saving.

3. As Matin, Hume, and Rutherford (1999) put it, the poor have three common methods for accessing the lump sums they need: selling assets they already hold (or expect to hold), taking a loan by mortgaging or pawning those assets, and turning their many small savings into large lump sums, through savings deposits, loans, or insurance.

4. Kochar (2000) notes the difficulty of obtaining accurate measures of the income of the self-employed, of the consumption of self-produced goods, and of the market value of inputs that are not perfectly marketable.

5. Interestingly, rotating saving associations are seen by some as ways of avoiding more traditional networks and the social obligations they entail. See chapter 8 for a discussion of these issues.

6. A comment by a resident of a Rio slum is telling: "The violence is so bad here that no one will deliver anything to my house. They are afraid of being robbed" (Perlman 2003).

7. A survey of Mexico City finds that 88 percent of people without bank accounts are paid by check. While it is not clear how much banks charge to cash checks, there is a cost, if only in terms of having to go to a bank or check cashing service (World Bank 2003b).

8. There is general agreement among donor institutions and microcredit agencies that microcredit is not necessarily the most appropriate instrument to reach the very poor. See Dugger (2004) for a discussion of the debate on the issue.

9. This tension can often have a gender or intrahousehold allocation dimension. For example, assets can be accumulated while the needs of some household members go unmet.

10. For a discussion of community-based and municipal strategies to cope with crime and violence, see chapter 5 and Van Bronkhorst (2003).

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