THE ROLE OF DEVELOPMENT FINANCIAL INSTITUTIONS IN REAL ESTATE IN KENYA: A CASE OF SHELTER AFRIQUE

BY

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UNITED STATES INTERNATIONAL UNIVERSITY

FALL 2015
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A Project Report Submitted to the Chandaria School of Business in Partial Fulfilment of the Requirements for the Degree of Masters in Business Administration (MBA)

UNITED STATES INTERNATIONAL UNIVERSITY

FALL 2015
STUDENT’S DECLARATION

I, the undersigned, declare that this is my original work and has not been submitted to any other college, institution or university other than the United States International University in Nairobi for academic credit.

Signed: ___________________________  Date:____________________________
Anthony Ngumi Githua (ID No. 620774)

This project has been presented for examination with my approval as the appointed supervisor.

Signed: ___________________________  Date:____________________________
Marion Mbogo

Signed: ___________________________  Date:____________________________
Dean, Chandaria School of Business
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ABSTRACT

The purpose of the study was to investigate the role of development financial institutions in real estate in Kenya. The research was conducted guided by the following specific objectives: To review the lending policy of Development Finance Institutions (DFIs), to investigate nature of development constraints and to explore alternative approaches to financing real estate in Kenya.

A descriptive research methodology using a case study of Shelter Afrique guided the study to address the three research objectives. A census was conducted for the 30 Shelter Afrique’s Kenya clients and the information collected through questionnaires. Once collected, the data was cleaned, coded, analyzed using descriptive statistics with the aid of SPSS and MS Excel, following which inferences were drawn from the analysis of results and the findings provided. Visual aids such as charts and tables were used to aid the reader in understanding the findings.

The findings showed that in respect to the adequacy of lending policies of DFIs, majority of Shelter Afrique’s clients are still dissatisfied mostly with the high fees charged and also the composition of the equity ratio. Measures of improving the lending policy were highlighted in the research with flexibility to the changes in the lending policy scoring the highest mean which was followed by the loan approval timelines, better customer care, increase target market and fee reduction. The findings revealed that lending of loans by financial institutions is a risky affair due to the uncertainties revolving around it.

With regard to the nature of development constraints, the study found out that majority of the clients experience constraints during the delivery of their objectives. Some of the highly experienced constraints include inefficient professional team, equity mobilization and cost escalations. The study established that most clients have endured a hard time trying to mitigate the constraints.
Concerning the alternative approaches to the financing of real estate, the study highlighted practices such as better pricing accompanied by better customer care and improved efficiency as the alternative practices that would motivate the clients of Shelter Afrique to become loyal. Client inclusiveness also stood out as a key motivator for repeat business in terms of capacity building and insight into the business model.

The study concluded that the adequacy of DFIs’ lending Policy can only be seen if the DFIs are able to avail a package of services that not only fills the fiscal gap between capital for public good and finance availed by the state on one side and commercial projects on the other, but also pursue to limit the gap in the finance system.

The nature of development constraints can be handled if DFIs insist on project teams, that are professional and the contractor are well experienced in the market and that there is no room for errors in the rolling out of the project. In addition, advisory services should be offered to the developers, as a guide or reference point as the move along with the project both on a technical and a regulatory platform. The alternative approaches to financing Real estate can only be adopted if they are cost effective and have a proven track record.

The study recommended that to attain adequacy of DFIs lending policies, DFI’s should be able to set limits to safeguard liquidity or alternatively they may choose to comply with limits set by financial regulators and if not actively regulated, be at par with international standards. To be able to have a good approach to development constraints DFIs require sound governance and financial management, an ability to balance cost effective intermediation and risk management with outreach through smart partnerships, capacity building and knowledge management and flexibility. To enhance acceptance of alternative approaches to financing Real Estate, DFIs therefore need to review and analyze their areas of comparative advantage and complement each other rather than compete with the banking institutions. This will go a long way in ensuring that DFIs remain relevant in the market in this turbulent environment.
ACKNOWLEDGEMENT

This project could not have been completed were it not for the grace and favor of the Almighty God, who has given me the strength and guidance until now, my extreme reverence go to Him. I want to acknowledge the support of my lovely wife, love you so much Jaime and am thankful for your kindness and love. Also, to my mum who passed away while I was doing my MBA. Rest in Peace mum, always an inspiration to me. I want to thank all my professors who have taught me and expanded my knowledge in this field. Special recognition goes to Mrs. Marion Mbogo who has offered so much guidance while doing this paper. I would also want to thank Shelter Afrique Management for the opportunity to use it as a case and make a presentation to them after doing my research. Lastly I want to thank my friends for their encouragement and especially the rest of my family for their love and support all through my MBA.
DEDICATION

This project is dedicated to the Shelter Afrique Management for allowing me to conduct this assessment using the company as a case study, and also to talk to the company’s past and current clients.
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# ACRONYMS AND ABBREVIATIONS

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<tr>
<td>AfDB</td>
<td>African Development Bank</td>
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<tr>
<td>CBK</td>
<td>Central Bank of Kenya</td>
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<tr>
<td>CBR</td>
<td>Central Bank Rate</td>
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<td>DFCK</td>
<td>Development Financial Corporation of Kenya</td>
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<td>DFIs</td>
<td>Development Finance Institutions</td>
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<td>FMO</td>
<td>Dutch Development Bank</td>
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<tr>
<td>GDP</td>
<td>Growth Domestic Product</td>
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<td>GoK</td>
<td>Government of Kenya</td>
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<tr>
<td>ICDC</td>
<td>Industrial and Commercial Development Corporation</td>
</tr>
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<td>IDB</td>
<td>Industrial Development Bank</td>
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<tr>
<td>IFC</td>
<td>International Finance Corporation</td>
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<td>KIE</td>
<td>Kenya Industrial Estates</td>
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<td>SACCOs</td>
<td>Savings And Credit Co-operative Societies</td>
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<td>SHAF</td>
<td>Shelter Afrique</td>
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<td>SPSS</td>
<td>Statistical Package for Social Science</td>
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CHAPTER ONE

1.0 INTRODUCTION

1.1 Background of the Problem

Present-day economies in both developed and developing countries depend upon efficient allocation and optimal utilization of resources and especially financial resources. Financial services influence all sections of the society with the financial institutions playing a vital role in ensuring financial services are distributed to all sectors of the economy including the property investment and development (Ogedengbe and Adesopo, 2003). According to research by the African Development Bank (2011), Africa’s middle class grew from 26.3 percent in 1980 to 34.3 percent of the population in 2010 with this phenomenon being accompanied by rapid urbanization and increased consumption for certain types of goods and services such as housing. In Kenya, financial institutions have facilitated the growth of the economy and the outlook remains positive.

According to a report by the World Bank (2015), Kenya’s economy is estimated to have grown by 5.4 percent in 2014 and is projected to grow by 6 percent in 2015. The resilience is likely to continue with the economy expanding at 6.6 percent in 2016 and 6.5 percent in 2017. Kenya is emerging as one of Africa’s key growth centers and is also poised to become one of the fastest growing economies in East Africa, supported by lower energy costs, investment in infrastructure, agriculture, manufacturing and other industries (World Bank Group, 2014). The momentum for growth is expected to be sustained by a stable macroeconomic environment, continued investment in infrastructure, improved business environment, exports and regional integration.

The government has also maintained discipline in fiscal and monetary policy, despite increasing pressure from devolution and rising public sector wage bill (World Bank, 2015). This growth has attracted investors and in the last two years, the number of investors seeking information and advice on the potential to develop housing, whether for rental or ownership, whether targeted at students, new families or the elderly, has grown exponentially. Hoskins, Higgins, and Cardew (2004) find that Gross Domestic Product
(GDP) growth has a significant correlation with composite property returns and therefore changes in housing price yields changes in GDP as property is a strong asset class which has been under-exploited as real estate prices have been stable during recession and political instability.

Developers, investors, and lenders are crossing borders, taking local experience with them into new contexts, expectant of the obvious opportunity. Local players are also working hard to build their markets and compete with the international players. According to Centre for Affordable Housing Finance in Africa (CAHF) (2013), there are two big stories in the housing finance picture. First, policy makers and practitioners work hard to expand the reach of Africa’s nascent mortgage markets. The potential opportunity in this market is significant and deserves increasing attention. Second, mortgage markets have continued to serve the minority. Investors will miss the market if they do not consider the realities of affordability across the continent and design their products accordingly. If this issue of affordability is not keenly looked at, the demand for housing in Africa will continue to increase as fewer and fewer people will be able to afford mortgages.

The Kenyan government estimates the annual housing demand to be at 206,000 units per year against an annual supply of 50,000 units only (CAHF, 2013). Furthermore, the housing sector development is mainly driven by the private sector, and continues to register growth with many new upcoming residential and commercial projects. The housing sector in the country is still faced with major challenges such as unavailability of decent housing, lack of adequate infrastructure and access of finance for affordable housing. The financial institutions fund approximately 20 percent of the country’s housing needs, and focuses mainly on urban areas. In terms of access to finance, the only segment that can benefit to some extent is the middle-to-high income earners, which accounts for about 17,000 mortgages in the country. This demonstrates that the mortgage market is still small and out of reach for the majority of the populace (CAHF, 2012).

The year 2013 was a challenging year for the housing market in Kenya. Overall, activities in the housing sector reduced substantially from both the supply and demand side. The majority
of developers, buyers and other investors put on hold decisions to invest in new projects, seeking mortgages or expanding investments in the sector respectively. The trend of minimal activities in the sector is typical within any year when the country holds elections as most participants tend to wait until the aftermath. It was expected that the market, in 2014, would pick up significantly (Njiru and Moronge, 2013).

In the Sessional Paper no. 10 of 2012, the Government of Kenya (GoK) has attempted to address the constraints of financing Real Estate by developing policies and strategies in these policy documents. The problems facing the financial sector include access to financial services outside the main cities which remains limited. Besides more coverage by regular banks, addressing the issue of access will require strengthening of the alternative financial service providers, namely: micro-finance institutions, Savings and Credit Co-operative Societies (SACCOs) and Development Finance Institution (DFIs), in addition to improving investors’ access to term finance. According to the same Sessional Paper no. 10, Kenya also experiences low utilization of pensions, insurance, capital and securities markets in realizing the investment goals set for Vision 2030. In addition to trying to improve the regulatory environment, the Government of Kenya has dedicated huge resources to help the sector to become technologically competitive (Government of Kenya, 2012).

The formation of county governments means that there is more interest in real estate development in other towns apart from Nairobi, the country capital. For instance, Kenya Commercial Bank and other commercial banks have continued to record an increase in the uptake of mortgages with the uptake expected to grow due to the lowering of interest rates, a stable shilling and stable political environment. In addition, the Central Bank of Kenya (CBK) lowered its rate by one percentage point to 8.5 percent, a signal that commercial banks should lower their lending rates to push up demand for credit and spur economic growth in the country. The impact is that Nairobi and other major towns will attract investors as there is potential to offer high returns on the property market. However, no major reduction in interest rates has been noted by commercial banks (Nyakundi and Jagongo, 2013).
There is also a notable high demand for housing especially in the high-end market, which is expected to grow even more as interest rates come down. Nairobi County approves an estimated 12,000 residential and commercial building plans each month (Ojijo, 2012). The growth drivers are quite similar across the region with factors such as rapid urbanization, modern household formations, regional economic growth, and improved government policies among others. There is therefore the need to involve more players in the real estate market to drive competition up and consequently improve access to construction finance and ultimately the housing stock in Kenya.

Financial services will play a critical role in the next phase of the development of our country by providing better intermediation between savings and investments than at present. This will assist the mobilization of investment funds that are required to implement the projects of Vision 2030. Kenya also intends to become the leading financial center in Eastern and Southern Africa, in competition with similar centers in the region. According to CBK (2013), Kenya has a relatively refined banking sector with 43 commercial banks of which six dominate the sector and that also accounts for 52 percent of all deposits, 60 percent of the credit volumes and control over 75 percent of the branch network. The sector has more than 225 fully operating branch offices and over 70 sub-branches all over the country. The commercial banking industry has attempted to join the real estate market and has to some extent achieved this. However, the commercial banks have focused on bankable clients with enough collateral to cover the risks associated with construction. Commercial Banks have also focused on taking up mortgages to the end-users as opposed to construction finance.

Namusonge (2004) states that, the second set of financial institutions that have historically been the most active in financing real estate in Kenya are development financial institutions (DFI). According to CBK (2013), the five DFIs in the country operate in the industrial and commercial sectors. The Government of Kenya started DFIs to promote industrial development. Some key DFIs include the Industrial and Commercial Development Corporation (ICDC), the Development Financial Corporation of Kenya (DFCK), the Kenya Industrial Estates (KIE) and Industrial Development Bank (IDB). The aim of these DFIs was
to provide long-term finance of up to ten years with grace periods of up to two years to foster industrial growth. Other major DFIs in the country include: Dutch Development Bank (FMO), African Development Bank (AFDB), Shelter Afrique, and International Finance Corporation (IFC). Commercial banks have a tendency of insisting on 100 percent security unlike DFIs whose collateral is progressively enhanced as a project is undertaken. DFIs also provide other non-financial benefits to a development project such as conducting appraisals, close monitoring and implementation and in addition transaction advisory services (Namusonge, 2004). This study therefore was concerned with how Shelter Afrique- a development financial institution in Kenya, has helped ease access to construction finance to the real estate industry participants’ and consequently led to the increase in the housing stock in Kenya.

1.2 Statement of the Problem
Alongside the strong economic growth rates registered in the past decades, empirical evidence has shown that the African middle class has been growing. In Kenya, the middle class encompasses 44.9 percent of the population (AfDB, 2013). This phenomenon has been accompanied by rapid urbanization and strong growth in consumption expenditure and demand for certain types of goods and services such as housing. However, supply of formal housing to meet the rapid growth has always been a contentious issue (AfDB, 2013). The Kenyan market is characterized by a large demand and a continuing shortage of formal housing (AfDB, 2013). Empirical evidence shows that one of the key elements to the delivery of housing stock is access to finance which holds the key to competitive advantage of financial institutions. The AfDB (2013) report states that one of the factors affecting the Kenyan housing market is lack of access to finance by developers. Aden Van Noppen (2012), states that housing developments are extremely capital intensive and highly leveraged. Furthermore, it is difficult for the housing developers to secure debt, especially at reasonable rates, which are a key component of bringing down the cost for the end-user. In fact, the cost of finance is one of the most prohibitive factors in the Kenyan market.

Housing Development borrowers are faced with challenges such as the banks not lending at reasonable rates, delayed approvals and untimely disbursals. The developers tell cautionary
tales about banks committing project finance but neglecting to disburse, making claims that funds will only be disbursed after construction is complete. This clearly defeats the purpose of project finance, which is meant to fund the construction itself. Hence this study which sought to assess and establish the extent to which existing DFIs have promoted acquisition of construction finance in Kenya. Consequently, the study focused on the case of Shelter Afrique as an institution that provides access to finance real estate players that include both developers and SACCOs.

1.3 General Objective
The general objective of this study was to examine how Shelter Afrique, a development finance provider, has performed its role in real estate sector in Kenya.

1.4 Specific Objectives
The specific objectives are:-
1.4.1 To review the lending policy of DFIs
1.4.2 To investigate nature of development constraints
1.4.3 To explore, alternative approaches to financing real estate

1.5 Importance of the Study
The results and findings of this research study with regards to the information obtained is anticipated to be beneficial and valuable to the following entities among others:

1.5.1 Shelter Afrique Management
The research focuses on both the existing and potential clients of Shelter Afrique. Management will be able to get response on the following: Gaps in its lending policies that its clients do not deem admirable, effectiveness of its lending policies as stated by its clients, effectiveness of the products it currently promotes, other innovative products that can be used to penetrate its existing markets, the impact of its financing to the populace

1.5.2 The Real Estate Players – Financial Institutions and Non-financial Institutions
The research focuses on feedback from these clients and at the same time foster changes that Shelter Afrique might deem necessary. These changes include: Change in some of the lending processes in Shelter Afrique, more innovative products could be promoted by Shelter
Afrique, better service delivery and cheaper financing that would eventually reduce their total project costs

1.5.3 The Government
The research would benefit both the DFI s and the borrowers of their facilities. Consequently, the impact would be felt through improved access to houses to the general populace and thereby be able to meet an annual demand of 250,000 housing units (Kibiru, Pokhriyal, and Obwocha, 2014) and improve the current mortgage standing of 20,000.

1.5.4 Individual and Corporate Investors
The real estate sector is currently booming and for this reason if any improvements would result in reduced prices of units and especially the financing costs, the country would see increased investors in the sector which would result in increased revenues for investors and financial institutions.

1.5.6 Researchers and Academicians
This research is an important addition to the existing repository of knowledge and would expand that which is already known on the development finance providers in Kenya. Academicians and researchers endeavoring to further the study on perception of the role of DFI s in Kenya and the impact this has on various market players and the prices of housing units would find this study to be an important tool in the course of their research.

1.5.7 The General Public
The general public may find this research quite interesting to study and by so doing expand their knowledge in asset backed securities and perceived benefits and impact upon introducing these instruments to the Kenyan market.

1.6 Scope of the Study
This study was carried out in the Shelter Afrique Head office in Nairobi, Kenya. Shelter Afrique was established in 1982 by African governments, the African Development Bank (AfDB), African Reinsurance Corporation (Africa-Re) and CDC (UK’s Development Finance Institution) with the mandate of mobilizing resources for housing development in Africa. One of the major functions of the institution is to mobilize credit to developers and
other financial institutions through lines of credit and construction loans. This assisted in the research as it gives feedback to the company on their performance as rated by the clients. The findings of this study to some extent are expected to apply to other development finance institutions in the country that focus on construction finance. First, there are similarities in credit mobilization, provision and information dissemination. Secondly the instrument used for data collection (questionnaires) is reliable. The research was conducted between April 2014 and June 2015.

1.7 Definition of Terms

1.7.1 Real Estate
Real estate refers to land including all the property on it that cannot be moved and any attached rights. It is a physical entity including the land and improvement affixed to the land while real property is a legal concept that gives the individual the right to use and control the real estate or physical entity. Land is also a finite and valuable resource, which is affected by numerous legal, physical and environmental constraints and interests. Real estate property is bound to land making it an immovable asset (Dervort, 2000).

1.7.2 Price
Price is defined as a value that will purchase a finite quantity, weight, or other measure of a good or service. In commerce, price is determined by what a buyer is willing to pay, a seller is willing to accept, and the competition is allowing to be charged (WebFinance, 2014).

1.7.3 Construction Finance
It is any value added loan where the proceeds are used to finance construction of some kind. A construction loan is a more specific type of loan, designed for construction and containing features such as interest reserves, where repayment ability may be based on something that can only occur when the project is built (Ellenoff Grossman & Schole LLP, 2014).
1.7.4 Lines of Credit
Lines of credit are credit sources often extended by banks, financial institutions and other licensed consumer lenders to creditworthy customers to address liquidity problems. Lines of credit can be secured by collateral, or may be unsecured (Majestic Boulevard Bank, 2014).

1.7.5 Developers
Developers are the coordinators of the activities, converting ideas on paper into real property. Developers buy land, finance real estate deals, build or have builders build projects, create, imagine, control and orchestrate the process of development from the beginning to end (Frej and Peiser, 2003).

1.8 Chapter Summary
This chapter has introduced the topic on the role of DFIs in the real estate sector in Kenya. Further, the research questions have been outlined as: What guides the lending policies of financial institutions in Kenya and do they articulate the expectations of borrowers? What are constraints in terms of delays and disruptions affecting the rolling out of a project? What innovative ways can be introduced in the real estate financing that could change the way project financing is done?

The next chapter reviews the available literature on the research topic. In the third chapter, the study looks at the research methodology that will be applied in the study while chapter four gives an analysis of the results and the final chapter discusses the results and gives recommendations for further research.
CHAPTER TWO

2.0 LITERATURE REVIEW

2.1 Introduction
In this chapter the study sought out various critics on the objectives and research questions for the topic under research. The various literature reviews have been on the lending policies of financial institutions, the constraints faced by developers that lead to untimely completion of projects and the alternative methods that could be used in real estate financing and structuring.

2.2 Lending Policies of DFIs
Lending or loan Policy is the primary means for guiding lending activities. It forms the credit philosophy in addition to imposing standards for achieving earnings objective and risk tolerance levels (Comptroller Handbook, 1998). Lending policies vary in degree of detail, length and organization and certain aspects of the policy may vary because of factors such as economic conditions, geographic location or portfolio objectives. All lending policies are tailored to fit the needs of an institution and the scope should be proportionate with the lending activities involved with the responsibilities of those involved being clearly established (Comptroller Handbook, 1998).

A lending or loan policy contains three (3) decision variables namely, credit terms (interest charge, loan size, loan period), collateral requirement and eligibility criteria (credit standards and collection effort) (Pandey, 1995). It is therefore important to scrutinize the 3 loan policy decision variables in order to enhance loan repayment.

The Banking Act, 2012 requires all commercial Banks to have a written lending or loan policy consistent with the relevant provisions of the Act, Regulations and any other applicable laws. The lending or loan policy contains loaning procedures and their documentation, requirements for grant of a loan, loan concentration limits, loan sizes, loan types, interest rates, and collateral requirements among others. Generally Financial Institutions offer long term loans, short term loans and deposit facilities. In the real estate sector, financial institutions grant loans in two ways: 1) Commercial Banks offer both
construction loans to the developers and mortgages to the end buyer of housing units. 2) Development financial institutions (DFIs) on the other hand grant both construction loans to experienced developers and Lines of Credit (LOCs) to Commercial Banks and Savings and Credit Cooperative Societies (SACCOs) to on-lend to their various clients for: home improvements, mortgages, and construction of individual homes.

According to Nwankwo (2000), “credit constitutes the largest single income-earning asset in the portfolio of most financial institutions. This explains why Financial Institutions spend enormous resources to estimate, monitor and manage credit quality by ensuring their lending policies are up to date and also accommodative. This is understandably, a practice that impact greatly on the lending behavior of financial institutions as large resources are involved.

Financial Institutions rely heavily on the lending policy in place as this guides pricing decisions as regards to lending as they cannot charge loan rates that are too low because the revenue from the interest income will not be enough to cover the cost of deposits, general expenses as well as the loss of revenue from some borrowers who may default on payments. Moreover, charging too high loan rates may also create an adverse selection situation and moral hazard problems for the borrowers (Chodechai, 2004).

Ezirim (2005) further stressed that bank lending policies generally are meant to counter great deals of risks, as it sets out and have to consequently be formulated and implemented with a great deal of caution and tact. The burden of following the lending policies to the letter, lies heavily on Financial Institution employees to ensure that for every loan facility under review, good credit analysis, presentation, structuring and reporting is done.

The lending policy guides loaning procedures and their documentation (requirements for grant of a loan (the information to request from a client and also the information to analyze), loan concentration limits, loan sizes, loan types, interest rates, and collateral requirements among others. The theory of asymmetric information indicates that it may be complex to distinguish between good and bad information without the correct metrics to do so, which
may result into adverse selection and moral hazards problems (Richard, 2006). According to Auronen (2003) the theory states that in business, more often than not, the person that holds more facts on a particular element to be executed- for example a borrower, is most likely to be in a better position to acquire optimal terms for the transaction than the lender. The party that knows less about the same specific item to be transacted is more inclined to make judgment whether wrong or right based on the information that they have (Auronen, 2003). The party that knows less about the same specific item to be transacted is therefore in a position of making either right or wrong decision concerning the transaction based on the information they have. Failure to have well thought through lending policies could result in adverse selection and moral hazard as required information at every loan processing stage or lack thereof, would be subject to varied levels of interpretation. This would consequently lead to poor evaluation and analysis therefore leading to significant accumulation of non-performing loans or bad assets for financial institutions. It is therefore critical to have balanced lending policies (Bofondi and Gobbi, 2003). Theories relating to the lending policies by financial institutions are as explained below.

2.2.1 Adverse Selection Theory
According to Elsevier Science B.V (2002), Adverse Selection theory predicts that information sharing among lenders weakens adverse selection and moral hazard, and can therefore increase lending and reduce default rates. Using a new, purpose-built data set on private credit bureaus and public credit registers, we find that bank lending is higher and credit risk is lower in countries where lenders share information, regardless of the private or public nature of the information sharing mechanism. We also find that public intervention is more likely where private arrangements have not arisen spontaneously and creditor rights are poorly protected.

It is worth noting that information sharing reduces the probability of being affected by adverse selection as financial institutions will be able to acquire and use all available information on all credit applicants (Pagano and Jappelli 1993). In their mode of doing business, each banking institution has private information about local credit applicants, but has no information about foreign applicants. If banks exchange information about their
clients’ credit worth, they can assess also the quality of foreign credit applicants and lend to them as carefully as they lend to local customers. By reducing information asymmetry (a situation where, in a transaction involving two parties, one party has better or more information than the other), between lenders and borrowers, credit registries allow loans to be extended to safe borrowers who had previously been priced out of the market, resulting in higher aggregate lending. The impact of information sharing on aggregate lending in this model is vague. When banks exchange credit information about borrowers’ kinds, the increase in lending to good credit borrowers may fail to compensate for an eventual reduction in lending to risky types. If this rate is higher than worthy borrowers deserve, it will push some good borrowers out of the borrowing market, forcing in turn to banks charging even higher rates to the remaining borrowers. Through sharing of the credit information, the lender is able to distinguish bad borrowers from good borrowers in the market. Better access to information helps lenders measure borrower risk more accurately and to set loan terms and conditions accordingly. Good borrowers with low risk would be given more attractive prices, stimulating credit demand, and fewer higher-risk borrowers would be rationed out of the market because of lenders inability to offer these borrowers accommodating rates (Barron and Staten, 2008).

Padilla and Pagano (2000), show that if banks exchange credit information on defaults, borrowers are encouraged to apply more energy in their projects. In both models non-payment is a sign of bad quality for outside banks and carries the penalty of higher interest rates, or no future access to credit facility.

2.2.2 Moral Hazard Theory
The moral hazard problem is inclined to show that a borrower has the motivation to default on a loan given by any financial institution or any other lender unless there are consequences on their future applications for credit. This emanates from the difficulty most if not all financial institutions, have in evaluating the level of wealth borrowers have accumulated by the repayment date, as compared to during the application date. If the borrowers’ wealth cannot be evaluated during these two points in time, they will be tempted to default. According to Alary and Gollier (2001), the consequence of this is that most borrowers will be
seen as risky clients and the reaction by most financial institutions will put in a risk margin on their interest rates, resulting in high interest rates charged to loans whose consequence is a breakdown of the market. According to Kipyego and Wandera (2013), Prof. Njuguna Ndung’u the former governor of Central Bank of Kenya, noted that credit information sharing achievement in the banking sector will not only be good news to the banks and the banking sector but also to the borrowers and the economy as a whole.

2.2.3 Interest Rates

Interest Rates according to Crowley (2007), an interest rate is the charge or cost a borrower pays for the use of the money they borrow from financial institutions (Crowley, 2007). Interest rates are normally expressed as a percentage rate over one year and as a charge or cost of money; it indicates market information vis-à-vis probable change in the purchasing power of money or future inflation (Ngugi, 2001). Financial institutions help mobilize money through savings by its customers. They then investment this money through diversified ventures by looking at ways and means of mitigating risks of losing it (Collins and Wanjau, 2011). Considering that there is always a mismatch between deposits and loans, these financial intermediaries like banks incur certain costs to gather additional monetary resources to ensure that all borrowers can be served with loans and that all depositors can always access their money as and when it falls due (Ngugi, 2001). This is why all costs of being a financial intermediary, are passed to depositors and Borrowers of loans. The disparity between the gross costs of borrowing and the net return on lending defines the intermediary costs which include information costs, transaction costs, administration, default costs and operational costs (Rhyne, 2002). According to Ngugi (2001), interest rate spread is well-defined by market microstructure characteristics of the banking sector and the policy environment.

Chand (2002) and Asian Development Bank (2001) have listed several reasons for high interest rate spread after conducting several independent studies. These are lack of sufficient competition, diseconomies of scale due to small size of markets, high operating and fixed costs, high transportation cost of funds due to expensive telecommunications, existence of regulatory controls and perceived market risks. They noted that the factors mentioned above
lead to high intermediation costs, which cause high spread. These studies have recognized one of the most understandable costs, which is associated with the capacity to enforce debt contracts. Small borrowers with no fixed assets rights have no guarantee to offer and are therefore perceived as high risk borrowers because of the high transaction costs involved, and consequently charged punitive rates of interest.

Chand (2002) points out governance issues as another unique cause. The latter encompasses maintenance of law and order and provision of basic transport and communications, all imposing on security, a lack of which has been found to be a cause for high transaction costs resulting in large intermediation costs. High intermediation cost, reflected in the high interest rate spread results in default and consequently high non-performing loans in a financial institution (Chand, 2002).

2.2.4 Credit Criteria
Credit criteria are dynamics used to determine a credit seeker’s creditworthiness. The factors include availability of disposable income, accumulated debt from current or other financial intermediaries and credit history of the borrower. Swaren (1990) suggested that the most inescapable area of risk is concentrated on the lending exercise. The riskiest practice in the lending exercises is offering loan facilities beyond the useful life of their corresponding collateral. Furthermore, financial information is sometimes unreliable and the legal framework in certain areas does not always support debt recovery or is not comprehensive enough to capture all aspects of collateral (Mueller and Henry, 1988).

Rouse (1989) indicated that problematic loans can come from overdrawn accounts where there is no overdraft limit, or overdraft taken in excess of reasonable functioning limits. In addition, lack of good technical skills and judgment on the part of a financial institution is a possible cause of bad loans. A lot has been reviewed in terms of lending activities of various commercial banks and on the factors responsible for banks willingness to extend much credit to some sector of the economy, while some discussed effect of such extension of credits on productivity and output. Most of these earlier studies agreed on the fact that it is logical for banks to have some basic lending principles or consideration to act as a check in their lending
activities. Since there are many studies in respect of bank’s lending behavior, it is therefore imperative to highlight and consider some factor that economists and professionals alike have proposed as virtually significant in explaining the determinants of financial institutions’ lending behavior.

2.3 Constraints in Real Estate

In the process of delivering real estate projects, developers undergo numerous constraints such as delays, disruptions, risks in construction projects and delays, limited access to mortgages and buyer deposits. These are explained in the following sections.

2.3.1 Delays

Delays in construction, refers to project delivery at a later time than had been planned, or expected, or stated in an agreed contract (Pickavance, 2005). Lo, Fung, and Tung (2006) define delay as the reduction of progress on site without necessarily bringing construction to an end. This is noted to lead to both time and cost overruns as stated by the project contracts with the professional team. Syed, Salman, Mauricio, and Kappagantula (2002) classify delays into non-allowable delays, allowable non-payable delays, allowable payable delays and concurrent delays. Non-allowable delays are delays, which the contractor is liable for and has agreed to the same. Allowable non-payable delays are non-foreseeable circumstances beyond any parties’ comprehension and not attributable to the professional teams control or negligence. Payable allowable delays are excusable delays, because they are contributions by an act or a failure by one or two involved parties to the construction transaction which results to a breach of contract. Concurrent delays occur when both owner and the contractor are responsible for the delay.

2.3.2 Disruptions

Disruptions are actions by either party of a project that interfere with construction work program (Howick, Ackermann, and Williams, 2009). Howick et al (2009) notes that for the most part most disruptions can be foreseen and are therefore easily planned for during the planning stages of the project. A few examples include defects and liabilities, normal errors
in calculation by the project teams, oversight issues by the monitoring team especially if the project is in a far off jurisdiction and many others.

2.3.3 Risks in Construction Projects and Delays
Cohen and Palmer (2004) state that sources of construction risk could include significant changes on the project scope, errors in the design of the project, significant omissions, confusion in the assignment of roles and responsibilities, engaging unskilled staff, force majeure (unforeseeable circumstances that prevent someone from fulfilling a contract), and new technology. Baloi and Price (2003) categorize construction risks as technical that involves the professional team chosen, social that includes lack of adherence to the environmental regulations, economic which relates to financing gaps in the project, legal which lack of adherence to the project legal structures and political which relates to the political climate of a country where the project is being implemented. Similarly, Mills (2001) states that there are a number of construction risks involved including: weather interference, poor productivity of labor that has been commissioned and quality of material bought to undertake the project.

Zou, Zhang, and Wang (2007) noted that constrained project schedules, changes in scope and design, long approval processes at regulatory level and by the client and improper planning are some of the key construction risk drivers. Aiyetan, Smallwood, and Shakantu (2008) note that poor management during design, during construction and monitoring and control are drivers of construction risk. Construction projects are carried out within a specified time. This calls for proper time management that eliminates all avenues of delays and disruptions. A study by Kumaraswamy and Chan (1999) noted that perception is a key ingredient that lead to serious delays on a project. Different perceptions by the project teams need to be noted early enough and then synergised to have all team members appreciating the uniqueness of each project. Noulmanee and Sittivijan (1999) identified some causes of delays in construction attributable to all parties involved in projects are poor project drawings, financing gaps to the project, lack of synergy between project consultants, the main contractor and the sub-contractors. Aiyetan et al (2008) noted that the main causes of delays in projects were delays in change of user from agricultural to commercial or residential, bad
weather conditions, bad site conditions, and increasing the scope of the project without properly considering the implications thereof.

Al-Kharashi and Skitmore (2009) noted that the use of unskilled labor for skilled roles, and a study by Syed et al (2002), noted that delays in attaining building permits, unplanned changes of scope and poor implementation can all cause delays in project implementation. Sambasivan and Soon (2007), identify causes of delay in the construction industry as contractor’s improper planning for the project, contractor’s poor site management, inadequate contractor experience, inadequate client’s finance thereby delaying payments for completed work, inefficient subcontractors, shortage in material, shortage in labor supply and equipment and lack of communication between parties involved in the project.

Chan and Kumaraswamy (1997) noted that poor risk evaluation methods, slow decision making, introduction of variations in the middle of a project and introducing untrained teams in the middle of a project could have dire consequences in terms of delay. A study by Kaming, Olomolaiye, Holt, and Harris, (1997) reveals that the major factors influencing cost overruns are: material cost increase due to inflation, inaccurate material estimation and degree of complexity. The study also acknowledged other causes as: financial and payment problems, improper planning, poor site management, insufficient experience, and shortage of materials and equipment.

2.3.4 Limited Access to Mortgages and Consequently Pre-sales (Buyer Deposits)

According to Pittman (2008), obtaining a mortgage in today’s mortgage market is a complicated process as it involves many procedures like identifying the best service provider with the best interest rates. This in turn hinders accessibility to mortgage funding. According to CBK (2011), the mortgage holders stood at 15,049 in May 2011, 16,135 mortgage holders in December 2011, while by end of 2012 there were 17,000 holders. This shows low uptake of mortgage in the country. World Bank Group (2014), attributes this to the fact that mortgage is accessible to only a small majority of the Kenyan population. Further, an article by Loutskina and Strahan (2007), points to securitization, cost and availability of mortgage as discriminating factors on those intending to take up the mortgage.
The Central Bank Survey of Risk Management (2011) found out that only 11 percent of Kenyans can afford an average mortgage loan. An average mortgage loan in Kenya is Sh6.6 million, and demands a monthly repayment of about Sh90,000 for a period of 20 years. More so, there is a continuing upward surge in the prices of construction materials hence the selling prices of houses move up too. The prices in Nairobi for instance up surged by 7.4 percent between April and September 2010. There is very little that has been done to address these challenges in Kenya hence the minimal growth in the mortgage industry, according to the same survey. Even with mortgage institutions offering 105 percent financing of mortgages, prospective buyers may be unable to engage in mortgage uptake as it is out of reach.

2.3.5 Effects of Delays and Disruptions

Effects of Delays and Disruptions of construction projects according to Aibinu and Jagboro (2002) begin from time overruns, cost overruns, unresolved disputes, abrupt litigation and many others. Haseeb et al (2011) identifies other effects of delays in the construction industry as clash, claims, total desertion and slowing down the growth of the construction sector. Ramabodu and Verster (2010) identify other effects of delays in construction projects as changes in scope of work on site, incomplete design at the time of tender, contractual claims (extension of time with cost), lack of proper cost planning and monitoring of funds, delays in amending costing variations and additional works.

Chelishe and Berko (2010) indicate that other factors would include delays in monthly payments to contractors; variations; inflation, and schedule slippage. It is worth noting that management of construction projects involves a great deal of managing risks. Managing risks involves: adequate planning, identifying and developing risk handling strategies adequate for monitoring and control. Project team members particularly clients, consultants and contractors should eliminate or mitigate delays when playing their respective roles.
2.4 Alternative Approaches to Construction Finance

Credit risk mitigation techniques have evolved overtime, courtesy of global financial innovation. Traditionally, collateral and guarantees have remained the most popular credit risk reduction strategies. These are largely ‘ex-ante’ considerations, implying that any loan appraisals that do not pass this test are rejected. Moreover, the bank conducts a monitoring exercise to keep track of adverse changes that might affect the value of the collateral, periodic repayments as well as the total value of the loan (Radevic and Ahmedin, 2010). The most outstanding feature of the traditional credit risk mitigation measures is that loans remain in the balance sheet of the bank and a capital charge on this risky asset is subsequently conducted.

Perhaps, a general way of looking at the evolving credit risk mitigation measures is to make a distinction between the traditional and modern banking models. Boot, Milbourn, and Schmeits (2005) note that in the former model, the originating bank holds risky, non-marketable and illiquid loans that are largely funded by deposits. However, the latter model introduces a way of transferring the risk associated with such holdings through credit risk transfer mechanisms and instruments. Simply speaking, the originating bank assumes all responsibilities and risks of the entire credit process in a traditional model while in the modern model the credit process is unbundled with the originating function remaining with the bank as the associated credit risk is transferred to other market players. The traditional banking model brings on board other institutions like insurance companies and other agents that are best placed to handle that kind of business.

2.4.1 Credit Market Clearing (Neo-Classical) Theory

According to Pindyck (1991) this theory states that if collateral and other pertinent restrictions remain given, then it is only the lending rate that determines the amount of credit that is dispensed by the banking sector. Therefore with an increasing demand for credit and a fixed supply of the same, interest rates will have to rise. Any additional risk to a project being funded by the bank should be reflected through a risk premium that is added to lending rate to match the increasing risk of default. Subsequently, there exist a positive relationship
between the default probability of a borrower and the interest rate charged on the advance (Ewert, Schenk, and Szczesny, 2000).

According to Romer and David (2011), despite the models’ complications, there is a great deal of information that is left out. For example, until the recent crisis, the models’ treatment of credit-market imperfections was generally minimal. Secondly, the microeconomic case for some important features of the models is questionable. Most notably, the models include assumptions that generate inertia in decision making that is mainly motivated not by microeconomic evidence, but by a desire to match macroeconomic facts.

Although this theory does not explicitly discuss how collateral would impact on the risk premium, it creates the impression that collateral has no effect on lending rate, and if a risky borrower would wish to face the same lending rate as a borrower with a lower risk, then all that is required is to pledge more collateral to lower his risk profile and therefore enjoy a lower risk premium. This brings about the ‘moral hazard’ and ‘adverse selection’ phenomena, firstly because of information asymmetry existing between the lender and borrowers. The borrower has a more accurate assessment of the risk profile of this investment that is not known by the lender and thus may perform secret actions to increase the risk of his investment without the realization of the lender. The adverse selection problem appears as lenders raise their interest rates to shield themselves from default and on the other hand attract only high risk borrowers and eliminate low risk borrowers (Mason and Roger, 1998).

2.4.2 Signaling Argument

According to Flannery (1986), the theory of signaling states that information asymmetry between a firm and outsiders leads the former to make certain changes in its capital structure. Myers and Majluf (1984), have shown that under asymmetric information, firms may prefer debt to equity financing. In other cases, the asymmetric information may leave corporate insiders with a degree of residual uncertainty leading to the pecking order effect, that is, the relative preference of equity financing (Noe, 1988). This may lead the firm to make certain
changes in its capital structure and send certain signals to the outsiders concerning the quality of its financial decisions.

According to Derban et al (2005) this theory, borrowers who always have private information will be forced to reveal (signal) their better quality through pledging of collateral to show their better status as opposed to lower quality borrowers. This is because in the absence of full information the bank is not able to assess the true quality of a borrower and may resort to credit rationing in an attempt to mitigate the problem of adverse selection. Pledging more collateral is therefore viewed by borrowers a most credible signal of their commitment towards repayment of the advance amount Manove and Padilla (1999 and 2001). Lower quality buyers who have private information regarding the true risk profile of their investment will shy away from pledging valued collateral, since they privately know that there is a higher chance of losing it because they will be unable to service the loans. Thus, they unknowingly send a signal regarding their ability to meet the contractual obligations. Higher premiums will be observed in borrowers pledging lower collateral while lower premiums will be observed for borrower pledging more collateral.

2.4.3 Firm Characteristics
Lending institutions can study the characteristics of an individual firm and form unbiased opinion about the firm’s future and ability to repay a credit advance. According to Ewert et al (2000), “there are firm-specific agency problems that can be mitigated using collateral or such covenant and each firm chooses a financial contract that maximizes firm value by trading off additional bonding and monitoring costs against reductions in interest rate premiums”. A firm-specific financial contract is thus made for each firm depending on the perceived problems of the firm in question, and the use of collateral by a specific firm can be observed to reduce the credit costs (high interest premiums). However, such conclusion will most likely not hold for many firms because, as mentioned before, there are high-risk firms that will offer valuable collateral and probably accept high premiums, (Ewert et al 2000).
2.4.4 Loan Pricing Theory
This theory explains why it is not prudent for banks to set very high interest rates to optimize profit from loan sales. If banks set up very high interest rates, they could induce the problem of adverse selection and moral hazard by attracting borrowers with very risky projects into their portfolio. The high interest rates would later act as an incentive for the risky borrowers to consider adding more risk to their investment portfolio due to high affinity for high returns.

According to Stiglitz and Weiss (1981), banks should consider the problems of adverse selection and moral hazard since it is very difficult to forecast the borrower type at the start of the banking relationship. If banks set interest rates too high, they may induce adverse selection problems because high-risk borrowers are willing to accept these high rates. Once these borrowers receive the loans, they may develop moral hazard behavior or so called borrower moral hazard since they are likely to take on highly risky projects or investments (Chodechai, 2004). From the reasoning of Stiglitz and Weiss (1981), it is usual to find that in some cases the interest rate set by banks are not commensurate with the risk of the borrowers.

It is worth noting that by its very nature, banking institutions are faced with the probability of default by counterparties in financial contracts. Loans constitute the biggest assets for banks, thus credit risk is arguably the biggest risk that banks face. It is therefore necessary for banks to put in appropriate measures to first of all prevent occurrence of these risks, and be able to deal with the risk if and when it occurs and preferable in the most innovative of ways.

2.4.5 Firm Characteristics Theories
These theories predict that the number of borrowing relationships will be decreasing for small, high-quality, informationally opaque and constraint firms, all other things been equal. (Godlewski & Ziane, 2008)

2.4.6 Theory of Multiple-Lending
It is found in literature that banks should be less inclined to share lending (loan syndication) in the presence of well-developed equity markets and after a process consolidation. Both
outside equity and mergers and acquisitions increase banks’ lending capacities, thus reducing their need of greater diversification and monitoring through share lending. (Carletti et al, 2006; Ongene & Smith, 2000; Karceski et al, 2004; Degryse et al, 2004). This theory had a great implication for banks in Nigeria in the light of the recent 2005 consolidation exercise in the industry.

2.4.7. Hold-up and Soft-Budget-Constraint Theories

Financial Institutions choice of multiple-lending is in terms of two inefficiencies affecting exclusive institution-firm relationships, namely the hold-up and the soft-budget-constraint problems. According to the hold-up literature, sharing lending avoids the expropriation of informational rents. This improves firms’ incentives to make proper investment choices and in turn it increases banks’ profits (Von Thadden, 2004; Padilla and Pagano, 1997). As for the soft-budget-constraint problem, multiple-bank lending enables financial institutions not to extend further inefficient credit, thus reducing firms’ strategic defaults. Both of these theories consider multiple-lending as a way for financial institutions to commit towards entrepreneurs and improve their incentives. None of them, however, addresses how multiple-lending affects financial institutions’ incentives to monitor, and thus can explain the apparent discrepancy between the widespread use of multiple-lending and the importance of financial institution monitoring. But according to Carletti et al (2006), when one considers explicitly financial institutions’ incentives to monitor, multiple-bank lending may become an optimal way for banks with limited lending capacities to commit to higher monitoring levels. Despite involving free-riding and duplication of efforts, sharing lending allows banks to expand the number of loans and achieve greater diversification. This mitigates the agency problem between financial institutions and depositors, and it improves financial institutions’ monitoring incentives.

2.5 Chapter Summary

In this chapter the researcher has reviewed previous literature based on the objectives and research questions for the topic under research. The various literature reviews have been on the lending policies of financial institutions, the constraints faced by developers that lead to untimely
completion of projects and the alternative methods that could be used in real estate financing and structuring.

In the next chapter the research methodology used in the study is shown. This includes the research design, population and sampling design, data collection methods, research procedures and data analysis methods.
CHAPTER THREE

3.0 RESEARCH METHODOLOGY

3.1 Introduction
This chapter starts by addressing the research design of the study. It then discusses the population and sample design and the research procedure. Under the research procedure, the method of pre-testing adopted is reviewed. The chapter further discusses the data collection technique used and data analysis. A summary of the chapter is provided at the end.

3.2 Research Design
Research design is a plan of what data to gather, from whom, how and when to collect the data, and how to analyze the data obtained. A research design can also be described as a systematic planning of research, usually including; the formulation of a strategy to resolve a particular question; the collection and recording of the evidence collected; processing and analysis of these data and its interpretation; and finally the publication of results (Kay, 1997).

The descriptive research design was adopted in this study. The principal use of descriptive research statistics is to describe information or data through the use of numbers. The characteristics of groups of numbers representing information or data are called descriptive statistics (Kay, 1997). Saunders, Lewis, and Thornhill (2007), have shown that surveys are one of the most utilized methods in business research since they allow the collection of large amount of data from a sizeable population in a highly economic way while describing the status quo. The survey method was therefore justified for this research as it contained the most advantageous traits given the large sample size and short time span for administration. Some of the traits include; flexibility of data collection, range of questions, sample management, control of the data collection environment, number of data, response rate, rate and expenditure.

The dependent variable in this study was the real estate sector and the independent variable was Shelter Afrique which is a development financial institution.
3.3 Population and Sampling Design

3.3.1 Population

A population is the total collection of elements about which we wish to make inferences (Cooper and Schindler, 2003). The target population for the study consisted of current clients of Shelter Afrique in Kenya. The population in Kenya by the time of carrying out this study stood at thirty (30) clients. These clients represent a good demographic since Kenya has been very active in the sourcing of funds from Shelter Afrique as compared to any other Shelter Afrique member country. Kenya also has a good proportion of both lines of credit clients and project financing clients.

3.3.2 Sampling Design

3.3.2.1 Sampling Frame

A sampling frame is an objective listing of the population from which the researcher can make a selection (Denscombe, 2007). A sampling frame was developed from the Kenya client list provided by Shelter Afrique.

3.3.2.2 Sampling Technique

Due to the small size of the population, a census method was used in the study and information received from all the thirty (30) clients.

3.4 Data Collection Methods

Primary data was used. Data was collected using a structured questionnaire administered to the selected population, Kenyan clients. The structure of the questionnaire was derived from the objectives. Section one consisted of demographics, section two sought to obtain adequacy of the lending policies to the needs of the clients, section three sought to find out the constraints in terms of delays and disruptions affecting the rolling out of a project and section four sought to find out what innovative ways can be introduced in the real estate financing that could change the way project financing was done. The questionnaire consisted of dichotomous Yes and No questions, multiple-choice questions with checkboxes in which respondents were given options of checking several boxes and questions in which respondents were giving their views in their own words.
3.5 Research Procedure

The researcher also held discussions through meetings with the Kenya Country Manager who is the head of Investments carried out in the area where the study was carried out. The purpose for the meeting was to discuss the composition of investments done by Shelter Afrique in the country. Thereafter, the country manager introduced the researcher to various clients.

A visit to the selected client’s offices was made to discuss the projects with the relevant company authorities who assisted in giving feedback on the questionnaires. With guidance from the research supervisor, the questionnaires for the exercise were finalized by the researcher using references from existing literature.

A pilot test was administered to three (3) clients who acted as a sample of the selected clients to gauge the level of understanding and comprehension of questionnaire by the targeted population. Corrections that arose were addressed. Thereafter the actual survey was conducted. The questionnaires were administered personally to the clients so as to clarify any matters arising.

3.6 Data Analysis Method

The overall method used was descriptive statistics. The researcher prepared the data through coding, editing, and cleaning to ensure orderliness, legibility, consistency and reduced errors. Microsoft Excel was used for data cleaning and applicable analysis. Statistical Package for Social Science (SPSS) computer software was used for statistical computations. These mostly included frequencies and frequency tables. The relationships among variables was measured by way of inferential statistics and presented as correlation. Data from the findings was presented using Microsoft Word in form of tables, graphs and charts.

3.7 Chapter Summary

This chapter identified the key issues to consider when collecting data. These ranged from identifying the population of interest, the sample frame, data collection instrument, and data
analysis. The research exercise adopted a descriptive research where a census was conducted for Shelter Afrique’s Kenya clients and the information collected through questionnaires.

The findings of the study are discussed and presented in the next chapter with conclusions and recommendations from study made in chapter five.
CHAPTER FOUR

4.0 RESULTS AND FINDINGS

4.1 Introduction
This chapter presents the results of the data gathered from the survey. The study sought to investigate the Role of Development Financial Institution in the real estate sector in Kenya using a case study of Shelter Afrique. Thirty (30) questionnaires were administered to Shelter Afrique’s Kenyan clients and specifically to both developers and SACCOs. The research instrument was structured according to the objectives of this study. All the respondents returned completed questionnaires. The data collected was analyzed using descriptive statistics and presented using tables and charts. A brief explanation of the results follows in each case.

The study results are organized according to the following outline that is based on the research objectives and general findings that are arranged in the following sequence: general findings, lending policies of DFIs, nature of development constraints and alternative approaches to financing real estate.

4.2 General Findings
The data in the study was collected from a target of 30 respondents and all of them provided valid responses. The following conclusions are made from the responses obtained from all the clients contacted.

4.2.1 Respondents Details
From Figure 4.1 below, 93% of the respondents were male with only 7% of the respondents being female.

![Gender of Respondents](image)

Figure 4.1: Gender of Respondents
Table 4.1 below depicts the frequency as well as the percentage and cumulative percentage of the respondents. Majority of the respondents as presented below were male which shows that the sector is currently dominated by men.

<table>
<thead>
<tr>
<th>Gender</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Male</td>
<td>28</td>
<td>94%</td>
</tr>
<tr>
<td>Female</td>
<td>2</td>
<td>7%</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>100</td>
</tr>
</tbody>
</table>

4.2.2 Age of Respondents

Thirty percent of the respondents were aged 25-35; 47% aged 35-45; and 23% aged above 45 years. The findings reveal that the sector is dominated by persons between the age of 36 years and 45 years of age. This has been summarized in the chart below.

4.2.3 Years Company has been in the Industry

Thirty three percent of the respondents’ company had been in the industry for between 1-5 years, 27% between 6 – 10, 23% between 11-15 years, 10% between 16 – 20 years, and 7% for over 20 years. This has been summarized in the following chart:
4.2.4 Positions of Respondents

Majority of the respondents at 43% owned the companies, 30% were directors, 17% in management positions while 10% were employees. This is depicted in the figure below:
4.3 Adequacy of Lending Policy

4.3.1 Frequency of Loan Uptake at Shelter Afrique

In trying to understand Shelter Afrique’s lending policy, the researcher asked the respondents how often they had taken up a loan with Shelter Afrique and whether they were comfortable with the lending policy. The results revealed that 83% had taken up the loan once, 14% had taken up the loan twice with 3% of the respondents had taken the loan 3-5 times. It is good to note that none of the respondents had taken up the loan for more than six times.

![Figure 4.5: Number of Loans](image)

4.3.2 Terms of Loans at Shelter Afrique

When asked whether they were comfortable with the lending policy that directed the terms of the loans, 87% of the respondents said they were comfortable with only 10% of the respondents expressing dissatisfaction. Three percent of the respondents did not respond to this question.

The study also sought to find out exactly what the clients who stated their dissatisfaction with lending policy were dissatisfied with. Thirty three percent of the respondents who had expressed dissatisfaction with the policy stated that they were uncomfortable with the equity ratio contribution, two of them felt that the upfront fees charged were too high while the another 33% felt that the inflexibility in negotiations made then uncomfortable.
Further to the above analysis, a correlation test was done to find out whether a relationship existed between the numbers of times the respondents took up a loan with Shelter Afrique and whether they were comfortable with Shelter Afrique’s lending policy terms. A significant relationship exists between these two variables where, \((P=0.419, r=0.026)\). This indicates that the number of loans a client took with Shelter Afrique was influenced by the organizations lending policy. This analysis is illustrated in the table below.

Table 4.3: Correlation (Shelter Afrique’s Lending Policy)

<table>
<thead>
<tr>
<th>No. of Loans</th>
<th>Pearson Correlation</th>
<th>Sig. (2-tailed)</th>
<th>Satisfaction of SHAF Policy</th>
<th>Pearson Correlation</th>
<th>Sig. (2-tailed)</th>
</tr>
</thead>
<tbody>
<tr>
<td>N</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>30</td>
<td>.419*</td>
<td>.026</td>
<td>1</td>
<td>.419*</td>
<td>.026</td>
</tr>
</tbody>
</table>

* Correlation is significant at the 0.05 level (2-tailed).

### 4.3.3 Adequacy to the Kenyan Market

When asked whether Shelter Afrique’s lending policy was adequate for the Kenyan market, 90% of the respondents agreed that the lending policy is adequate with 10% disagreeing with this statement. The findings are presented in figure 4.6 on the next page.
The reasons cited were that the policy was not well accommodative to the new entrants in the real estate industry; it delayed approval of a loan as every proposal had to be forwarded to the Board for approval thereby delaying disbursement. In addition, others cited that the minimum amounts guided by the lending policy were not accommodative to the smaller players in the industry and also the owner build concepts being done by the Commercial Banks.

4.3.4 Gaps in Shelter Afrique’s Lending Policy

In order to find gaps in the current lending policy, the researcher sought to find out if the Shelter Afrique’s lending policy was able to achieve some listed outcomes. Below is a summary of the findings.

4.3.4.1 Outcome - Reduces response time

According to the findings, 40.7% of the respondents strongly agreed that the current lending policy reduces response time, 51.9% of the respondents agreed while 7.4% of the respondents were neutral that the current lending policy reduces response time. A summary of these is outlined in the figure on the next page.
4.3.4.2 Outcome – Fosters Negotiations

As outlined in the figure below, 25.9% of the respondents strongly agreed while 55.6% of the respondents agreed that the current Shelter Afrique’s lending policy fosters negotiations, 14.8% were neutral and 3.7% disagreed with this.

Figure 4.7: Reduced response time

Figure 4.8: Fosters Negotiations
4.3.4.3 Outcome – Minimum and Maximum Amounts

When asked whether the current Shelter Afrique’s lending policy sets the minimum and maximum amounts of loans, all the respondents agreed with this statement with 77% of them strongly agreeing as outlined in the figure below.

![Figure 4.9: Maximum and Minimum Amounts](chart)

4.3.4.4 Outcome – Relationship with Client

The response received from this question indicates that the lending policy does not guide the client on how to relate with Shelter Afrique. This is so because 67% of the respondents disagreed that the policy led to this outcome with 30% of these respondents strongly disagreeing. Only 17% of the respondents agreed with this statement with another 17% choosing to be neutral. These findings are presented in the table below.

<table>
<thead>
<tr>
<th>The lending policy guides the relationship with the client</th>
<th>Frequency (N=30)</th>
<th>Percent Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strongly Disagree</td>
<td>9</td>
<td>30</td>
</tr>
<tr>
<td>Disagree</td>
<td>11</td>
<td>37</td>
</tr>
<tr>
<td>Neutral</td>
<td>5</td>
<td>17</td>
</tr>
<tr>
<td>Agree</td>
<td>3</td>
<td>10</td>
</tr>
<tr>
<td>Strongly Agree</td>
<td>2</td>
<td>7</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>30</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>
4.3.4.5 Outcome - Indication of Level of Assistance

According to the findings of the study, tabled below, 70% of the respondents agreed that the current lending policy indicates the level of assistance that the lender gives to the client. Twenty three percent of the respondents remained neutral on this and 7% of them disagreed that the policy indicates the level of assistance Shelter Afrique accords to the client.

Table 4.5: Indication of Level of Assistance

<table>
<thead>
<tr>
<th>The lending policy indicates the level of assistance by the lender</th>
<th>Frequency (N=30)</th>
<th>Percent Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disagree</td>
<td>2</td>
<td>7</td>
</tr>
<tr>
<td>Neutral</td>
<td>7</td>
<td>23</td>
</tr>
<tr>
<td>Agree</td>
<td>13</td>
<td>43</td>
</tr>
<tr>
<td>Strongly Agree</td>
<td>8</td>
<td>27</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>100</td>
</tr>
</tbody>
</table>

4.3.4.6 Outcome - Credit Analysis Process

The researcher also sought to find out if the current lending policy guided the credit analysis process. As indicated in the figure below, the study established that 33% of the respondents strongly agreed that the lending policy guided the credit analysis process 57% agreed and 7% were indifferent on the issue. Meanwhile 3% of the respondents disagreed that the lending policy guided the credit analysis process.

Figure 4.10: Credit Analysis Process
4.3.4.7 Outcome – Pricing Decision

The findings in the study established that 59% of the respondents agree that the loan policy guided the pricing decision, 4% of them were neutral while 37% of the respondents disagreed that the lending policy guided the pricing as shown in figure 4.11 below.

![Pricing decision](image)

Figure 4.11: Pricing Decision

4.3.4.8 Outcome – Ease of Credit Referencing

To conclude the understanding of gaps in the current lending policy, the researcher asked the respondents whether the current lending policy eases credit referencing. According to the findings of the study 43% strongly agree that the lending policies made it easier for credit referencing, 37% agree while 20% of the respondents disagree that the lending policies made it easier for credit referencing, as shown in the table below.

Table 4.6: Ease of Credit Referencing

<table>
<thead>
<tr>
<th>The lending policy eases Credit Referencing</th>
<th>Frequency (N=30)</th>
<th>Percent Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Neutral</td>
<td>6</td>
<td>20</td>
</tr>
<tr>
<td>Agree</td>
<td>11</td>
<td>37</td>
</tr>
<tr>
<td>Strongly Agree</td>
<td>13</td>
<td>43</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>30</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>
4.4 Constraints Experienced in Delivering Real Estate Projects/ Mortgages

The researcher sought to find out if the respondents were experiencing any constraints in their companies to see how the organization would fill this gap to ensure that these are minimized.

4.4.1 Constraints during Project Delivery

All the respondents admitted to have experienced a constraint during the delivery of company objectives. Twenty seven of the respondents listed the constraints outlined in the figure below:

![Constraints during project delivery](image)

Figure 4.12: Constraints during Project Delivery

4.4.2 Constraints Mitigation

The researcher wanted to find out whether the clients were able to mitigate constraints faced on their own. The results indicated that 33% of the respondents were not able to mitigate the constraints on their own, with only half of the respondents able to mitigate constraints by themselves. The tabulation of their responses is outlined in the table on the next page.
Table 4.7: Self Mitigation of Constraints

<table>
<thead>
<tr>
<th>How well would you say you are able to mitigate constraints?</th>
<th>Frequency (N=30)</th>
<th>Percent Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Not Well</td>
<td>3</td>
<td>10</td>
</tr>
<tr>
<td>Just an Idea</td>
<td>7</td>
<td>23</td>
</tr>
<tr>
<td>Moderately</td>
<td>5</td>
<td>17</td>
</tr>
<tr>
<td>Well</td>
<td>10</td>
<td>33</td>
</tr>
<tr>
<td>Very Well</td>
<td>5</td>
<td>17</td>
</tr>
<tr>
<td>Total</td>
<td><strong>30</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

All the respondents saw the importance of Shelter Afrique (SHAF) in assisting in the mitigation of the constraints, with 63% of the respondents stating that it is very important and 37% of them saying that it is necessary for Shelter Afrique to assist in constraints mitigation.

This study further sought to establish what Shelter Afrique can do to assist in mitigating these constraints. Twenty seven respondents gave their feedback as follows: Offer a prequalified list of professionals, reduce conditions precedent (CP), Shelter Afrique to join in as an equity partner, capacity building and improving access to SMEs. A summary of the responses is outlined in figure 4.14 on the next page.
4.4.3 Factors that Enhance Delivery of Projects

Further to these, a listing of factors that enhance efficiency in delivery of projects was provided for the respondents to validate whether they actually enhance project delivery. A summary of the response obtained is presented below.

4.4.3.1 Enhance Efficiency in Delivery of Projects - Loan Tenure

The study sought to investigate if increase of the loan tenure would enhance in delivery of projects. According to the findings of the study 17% of the respondents strongly agreed that increase of the loan tenure would enhance delivery of projects, 67% agreed with this while 17% were neutral as shown in the figure on the next page.
4.4.3.2 Enhance Efficiency in Delivery of Objectives – Grace Period

The study further sought to investigate if increasing the grace period would enhance efficiency in the delivery of projects. According to the findings 43% of the respondents strongly agree that increasing the grace period would enhance efficiency in the delivery of projects, 50% of the respondents agreed while 7% of the respondents had a neutral opinion.

Table 4.8: Grace Period

<table>
<thead>
<tr>
<th>Increase of Grace Period</th>
<th>Frequency (N=30)</th>
<th>Percent Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Neutral</td>
<td>2</td>
<td>7</td>
</tr>
<tr>
<td>Agree</td>
<td>15</td>
<td>50</td>
</tr>
<tr>
<td>Strongly Agree</td>
<td>13</td>
<td>43</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>100</td>
</tr>
</tbody>
</table>

4.4.3.3 Enhance Efficiency in Delivery of Projects – Involvement in Vetting the Professional Team

The study sought to establish if Shelter Afrique involvement in vetting the professional team would enhance efficiency in delivery of projects. The findings revealed that 41% of the
respondents strongly agreed that Shelter Afrique involvement in vetting the professional team would enhance efficiency in delivery of projects, while 59% of the respondents agreed, making it majority of the respondents as shown in the figure below.

![Figure 4.16: Involvement in Vetting the Professional Team](image)

### 4.4.3.4 Enhance Efficiency in Delivery of Projects - Involvement in Tendering Process

On the issue of involving Shelter Afrique in the tendering process so as to enhance efficiency in the delivery of projects, 53% of the respondents strongly agreed that involving Shelter Afrique in the tendering process would enhance efficiency in the delivery of projects, 47% of the respondents agreed with this opinion.

<table>
<thead>
<tr>
<th>Involvement in Tendering Process</th>
<th>Frequency (N=30)</th>
<th>Percent Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agree</td>
<td>14</td>
<td>47</td>
</tr>
<tr>
<td>Strongly Agree</td>
<td>16</td>
<td>53</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>100</td>
</tr>
</tbody>
</table>

### 4.4.3.5 Enhance Efficiency in Delivery of Projects – Selection of the Marketing Team

The study sought to establish if involving Shelter Afrique in the selection of the marketing team would enhance efficiency in delivery of projects. The findings revealed that 87% of the respondents agree that involving Shelter Afrique in the selection of the marketing team
would enhance efficiency in delivery of projects, while 13% percent of the respondents were of a neutral opinion as shown in figure 4.17 below.

![Figure 4.17: Involvement in Selection of the Marketing Team](image)

**4.4.3.6 Enhance Efficiency in Delivery of Projects - Monitoring and Evaluation**

All the respondents agreed that constant monitoring and evaluation by Shelter Afrique to improve efficiency in delivery of projects. Forty percent of the respondents strongly agreed while 60% of the respondents agreed.

<table>
<thead>
<tr>
<th>Table 4.10: Constant Monitoring and Evaluation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant Monitoring and Evaluation</td>
</tr>
<tr>
<td>-----------------------------</td>
</tr>
<tr>
<td>Agree</td>
</tr>
<tr>
<td>Strongly Agree</td>
</tr>
<tr>
<td>Total</td>
</tr>
</tbody>
</table>

**4.4.3.7 Enhance Efficiency in Delivery of Projects – Independent Project Managers**

The study also further sought to investigate if the use of independent project managers would enhance efficiency in the delivery of projects. The finding in the study revealed that 27%
were neutral to the idea, 40% agreed that the involvement of Independent Project Managers would enhance efficiency and 10% strongly agreed to the idea.

Table 4.11: Use of Independent Project Managers

<table>
<thead>
<tr>
<th>Use of Independent Project Managers</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Neutral</td>
<td>8</td>
<td>27</td>
</tr>
<tr>
<td>Agree</td>
<td>12</td>
<td>40</td>
</tr>
<tr>
<td>Strongly Agree</td>
<td>10</td>
<td>33</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>100</td>
</tr>
</tbody>
</table>

4.5 Alternative Approaches to Financing Real Estate

4.5.1 Relevance of Contemporary Methods of Credit Risk Mitigation

Credit risk mitigation techniques have evolved overtime courtesy of global financial innovation. The researcher sought to find out if the respondents found these modern models relevant. According to the finding, 33% of the respondents felt that contemporary methods of credit risk mitigation are very relevant while 67% of the respondents felt that they were quite relevant as shown in table 4.12.

Table 4.12: Relevance of Contemporary Methods of Credit Risk Mitigation

<table>
<thead>
<tr>
<th>Relevance of Contemporary Methods of Credit Risk Mitigation</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Quite Relevant</td>
<td>20</td>
<td>67</td>
</tr>
<tr>
<td>Very Relevant</td>
<td>10</td>
<td>33</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>100</td>
</tr>
</tbody>
</table>

The researcher went deeper into this and wanted to investigate which alternative approaches would motivate respondents to become repeat clients. This was indeed a very important question for this research and the responses by the clients were very crucial. The respondents listed the below as some of the things that can be done to motivate them to be repeat clients in relation to alternative approaches: better pricing, improved efficiency, and better customer care.
4.5.2 Involvement in Activities that Define the Alternative Approaches

On the willingness to be involved in an activity/exercise that would help define the alternative approach used by Shelter Afrique in mitigating credit risk, the study found that 63% of the respondents were quite willing to be involved in the activity while 37% of the respondents were not willing as shown on figure 4.19 below.
4.5.3 Inclusiveness in defining activities

The study sought to determine if inclusiveness in the definition of alternative approaches would motivate the respondent to become repeat clients. According to the findings of the study 83% of the respondents stated that inclusiveness in the definition of alternative approaches would motivate them to become repeat clients while 17% stated it would not motivate them to become repeat clients as shown in table 4.13.

Table 4.13: Inclusiveness in defining activities

<table>
<thead>
<tr>
<th>Inclusiveness in defining activities</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>25</td>
<td>83</td>
</tr>
<tr>
<td>No</td>
<td>5</td>
<td>17</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>100.0</td>
</tr>
</tbody>
</table>

The study sought to establish how inclusiveness in defining activities would motivate one to become a repeat client of Shelter Afrique. The finding of the study revealed that the respondents felt that inclusiveness in defining activities would assist them in capacity building, give them more insight into Shelter Afrique business model and better understand the organization itself.

Figure 4.20: How inclusiveness motivates repeat business
4.5.4 Alternative Approaches to Credit Risk Mitigation

Further to these, a listing of activities that enhance clients to return to Shelter Afrique for a product was provided for the respondents to validate whether these would enhance them to be repeat clients. A summary of the response obtained is presented below.

4.5.4.1 Alternative Approaches to Credit Risk Mitigation - Use of Insurance

The study sought to establish if use of insurance as a mitigation for credit risk would motivate the respondents to become repeat client. According to the findings of the study 63% of the respondents strongly agreed that use of insurance in mitigation for credit risk would motivate the respondents to become repeat client, 26% of the respondents agreed with this statement while 11% were neutral as shown in figure 4.14.

![Use of Insurance](image)

Figure 4.21: Use of Insurance

4.5.4.2 Alternative Approaches to Credit Risk Mitigation - Use of Bank Guarantees

The study also further investigated if the use of bank guarantees as credit mitigation tools would motivate the respondents to become repeat client. Twenty seven responses were received as shown below:

Forty four percent of the respondents strongly agreed that use of bank guarantees as credit mitigation tools would motivate the respondents to become repeat client, 41% of the respondents agreed with this statement. There were 11% of the respondents who were of a
neutral opinion while 4% of the respondents’ disagreed that use of bank guarantees as credit mitigation tools would motivate the respondents to become repeat client as shown in table 4.14 below.

Table 4.14: Use of Bank Guarantees

<table>
<thead>
<tr>
<th>Use of Bank Guarantees</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disagree</td>
<td>1</td>
<td>3</td>
</tr>
<tr>
<td>Neutral</td>
<td>3</td>
<td>11</td>
</tr>
<tr>
<td>Agree</td>
<td>11</td>
<td>41</td>
</tr>
<tr>
<td>Strongly Agree</td>
<td>12</td>
<td>44</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>27</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

**4.5.4.3 Alternative Approaches to Credit Risk Mitigation- Use of positive and Negative Covenants**

The study sought to investigate if the use of positive and negative covenants as credit risk mitigation tools would motivate the respondents to become repeat client. According to the findings of the study 56% of the respondents strongly agreed that use of positive and negative covenants as credit mitigation tools would motivate the respondents to become repeat client, 37% agreed with this statement while 7% of the respondents were neutral as shown in figure 4.22.

Figure 4.22: Use of positive and Negative Covenants
4.5.4.4 Alternative Approaches to Credit Risk Mitigation- Use of Other Properties as Legal Charge

The study further sought to analyze if the use of other properties other than the one being constructed as legal charge as credit risk mitigation tools would motivate the respondents to become repeat client. According to the findings twenty seven respondents agree that the use of other properties other than the one being constructed as legal charge as credit risk mitigation tools would motivate the respondents to become repeat client with 56% of the respondents strongly agreed while 44% of the respondents agreed as shown in table 4.15.

Table 4.15: Use of Other Properties as Legal Charge

<table>
<thead>
<tr>
<th>Use of Other Properties as Legal Charge</th>
<th>Frequency</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agree</td>
<td>12</td>
<td>44</td>
</tr>
<tr>
<td>Strongly Agree</td>
<td>15</td>
<td>56</td>
</tr>
<tr>
<td>Total</td>
<td>27</td>
<td>100</td>
</tr>
</tbody>
</table>

4.5.4.4 Alternative Approaches to Credit Risk Mitigation- Use of Assignment of Receivables

The study sought to find out if the use of assignment of receivables as credit risk mitigation tools would motivate the respondents to become a repeat client of Shelter Afrique. The findings revealed that 67% of the respondents strongly agreed that the use of assignment of receivables as credit risk mitigation tools would motivate the respondents to become a repeat client of Shelter Afrique, 26% of the respondents agreed with the findings while 7% of the respondents were neutral on the issue.

Figure 4.23: Use of assignment of receivables
4.6 Chapter Summary

This chapter presented key findings of the survey by way of tables and figures. It was subdivided into four sections whereby the background information of the respondents was obtained then followed by findings of the research questions. In the next chapter, a summary of the findings was drawn followed by discussion of the finding of the specific objectives. Conclusions and recommendations will also be presented.
CHAPTER FIVE

5.0 DISCUSSION, CONCLUSION AND RECOMMENDATION

5.1 Introduction
This chapter provides a summary of the findings in chapter four relating to the concepts and frameworks in chapter two and then goes ahead to draw conclusions based on the objectives, and make recommendations in terms of improvements and further research.

5.2 Summary
The purpose of the study was to investigate the role of development financial institutions in real estate in Kenya. The research was conducted guided by the following specific objectives: to review the lending policy of DFIs, to investigate nature of Development constraints, and to explore alternative approaches to financing real estate in Kenya.

A descriptive research methodology using a case study guided the study to address the three research objectives. This research methodology was used because it involved gathering data that described events and then organized, tabulated, depicted, and described the data. The study used description as a tool to organize data into patterns that emerged during analysis. Visual aids such as charts and tables were used to aid the reader in understanding the findings. A census was conducted for the 30 Shelter Afrique’s Kenya clients and the information collected through questionnaires. Once collected, the data was cleaned, coded, analyzed using descriptive statistics with the aid of SPSS and MS Excel, following which inferences were drawn from the analysis of results and the findings provided.

The findings showed that in respect to the adequacy of lending policies of DFIs, majority of Shelter Afrique’s clients are still dissatisfied mostly with the high fees charged and also the composition of the equity ratio. Measures of improving the lending policy were highlighted in the research with flexibility to the changes in the lending policy scoring the highest mean which was followed by the loan approval timelines, better customer care, increase target market and fee reduction. DFIs usually have greater financing capacity and provide a forum for close co-operation with clients as compared to banks. DFIs can provide loans or equity
investment on competitive or even subsidized, terms. The findings revealed that lending of loans by financial institutions is a risky affair due to the uncertainties revolving around it.

With regards to the nature of development constraints, the study found out that majority of the clients experience constraints during the delivery of their objectives. Some of the highly experienced constraints include inefficient professional team, equity mobilization and cost escalations. The study established that most clients have endured a hard time trying to mitigate the constraints. Most respondents were of the opinion that Shelter Afrique plays a significant role in terms of aiding clients to mitigate such constraints. Respondents agreed that in order to abate constraints in the financing of real estate, Shelter Afrique could employ prequalified professionals and reduce conditions precedent when accessing finance.

Concerning the alternative approaches to the financing of real estate, the study highlighted practices such as better pricing accompanied by better customer care and improved efficiency as the alternative practices that would motivate the clients of Shelter Afrique to become loyal. Client inclusiveness also stood out as a key motivator for repeat business in terms of capacity building and insight into the business model. Majority of the respondents also thought that the contemporary methods of credit risk mitigation are quite relevant and were willing to take part in laying down the strategies to be employed. The use of insurance and bank guarantees to mitigate credit risk also scored high in terms of motivating clients.

5.3 Discussions

5.3.1 Adequacy of DFIs’ Lending Policy

The findings revealed that client’s perception of the lending policy is vital in assessing the lending policy. According to most banks they conform to the fact that the demand for real estate financing is tremendous and that there is no substitute for prudent lending policies. Furthermore some of these banks have withdrawn from the real estate financing market due to the effects of being saddled with incredible high rates of nonperforming loans. In addition, there have been several problems in the real estate financing with several warnings raised for cautious lending and recovery. The results therefore translate that the real estate projects financed are mostly highly inflated with regards to costs and developers are rarely committed
to them hence resulting in breaches and therefore unable to recover loans. The findings agree with the past studies on financing of real estate by Chand (2002) who averred that high intermediation cost reflected in the high interest rates may result into the client being unable to repay the loan leading to high risk of default.

In Kenya, though different banks have their own guidelines and procedures for loan approval, the general procedure followed from the very beginning of the submission of the loan application to the very end or finalization of the loan (disbursement and utilization) depicts a vexing experience. This calls for some sort of reforms and improvements in the lending procedure. Drawing from the discussions made by Nwankwo (2000), credit is said to vital for financial institutions to become profitable which translates into the lending process becoming even more hectic. The situation has further been worsened by the adverse selection and moral hazard problem out there in the market that has made the lending policy become stiffer. In addition, tight liquidity stands out as a major difficulty for the lending procedure accompanied by regulations and increasing interest rates. These alongside with the lending restrictions identified form some of the numerous challenges that DFIs face. Other challenges usually involve lack of infrastructure in emerging markets, regulatory environment, capacity in terms of skilled managers and field staff experienced in real estate financing. On the other hand, the financial condition of borrowers is normally undermined by factors such as government controls, internal and external political interferences and pressures, production difficulties, financial limitations, market disruptions and unreliable financial information among others. These results agree with the findings of a study undertaken by Auronen (2003) which suggested that the finance injected by DFIs is meant to act as a catalyst to aid in mobilizing and attracting real estate developers.

The study established that reduced response time and negotiations and better relationships with the clients are significant in order for clients to adjust their perception on lending policies. To this effect, DFIs seem to be providing better and even more subsidized terms on a broad range of financial services in Kenya, such as loans or guarantees to real estate investors and constructors. DFIs therefore tend to initiate or develop projects in industrial fields where commercial banks are reticent about investing without some form of official
collateral. DFIs therefore maintain written policies and procedures that clearly outline its risk management policies for their financing activities. The policy establishes the authority, rules and frame work to operate and administer its financing portfolio effectively.

5.3.2 Nature of Development Constraints
The study established that a majority of Shelter Afrique clients are faced with constraints which normally result into delays and disruptions of construction projects. The findings imply that clients lose confidence in institutions that do not remedy this and hence their loyalty is affected. The constraints result from the fact that some financial institutions are under-capitalized and thus unable to attract cheaper foreign credit and therefore have to sell expensive credit to the local developers. The effect is that the developers will have to deal with high interest rates which sometimes affect the project cash flows and consequently the project. Furthermore, the partnership with government, in Private Public Partnerships (PPPs), results in undue interference in operations and hence lack of stability in management and delivery of projects especially if the political scene in the country changes. Other key problematic areas in the economy such as inadequate infrastructure also have effect on the success of projects. This includes access to external roads, electricity and sewerage services that are supposed to be provided by the Government and the county councils. Also incompetence in management of the projects is another significant problem. This concurs with the findings of Haseeb et al (2011) which indicated that such delays and distractions slow down growth of the construction industry and also lead to claims and total desertion.

The findings also revealed that DFI’s strategy to subsidize policy terms by increasing the loan tenure and the grace period is likely to go a long way in mitigating the constraints. DFIs are prone to construction risks that are likely to arise from various sources such as changes in the technological environment, inexperienced contractors and other unforeseen circumstances that may hinder a party from fulfilling its contractual obligations hence forestalling projects and this is a major constraint to developers (Cohen and Palmer, 2004). The findings also strongly advocated for the idea that skills are essential for DFIs to act in their full capacity and recommended that it was necessary for the vetting of professional teams. Another important dimension of credit risk management that was highlighted in the
study is the overall credit administration and monitoring and evaluation process. This is a key element in maintaining the soundness and safety of project loans. While granting credit, DFIs roll out and implement comprehensive procedures and information systems to monitor timely the evolution of individual credits and single obligors across the loan portfolio.

The study found out that DFIs have a better understanding of developmental risk, a higher risk appetite, and a stronger risk rating, all of which they can use to benefit real estate developers. The inclusion of more commercially orientated projects in their portfolios also allows them to cross-subsidize development projects in poor areas. An effective monitoring system highlights criteria for classifying and reporting problem loans as well as possible corrective action. One reason for coming up with a systematic credit review process is to promptly identify deterioration in asset quality. DFIs’ credit policies clearly highlight how the institutions will manage credit issues and assign responsibility accordingly. DFIs have to balance a trade-off between the two potentially conflicting objectives of fulfilling their policy mandate and being financially sustainable.

5.3.3 Alternative Approaches to Financing Real Estate

The study established that it is vital that DFIs develop a comprehensive understanding of the full spectrum of risks associated with real estate financing business. The risk assessment and risk management systems of DFIs have in-built ability to deliver early warning signals to keep their balance sheets safe from potential adverse effects while offering better pricing methods. Having adequate safeguards put in place, they are encouraged to facilitate real estate growth through enhanced outreach of financing services and innovative products. DFIs ensure that their internal policy framework guiding real estate financing practices undergo broad scrutiny and due diligence and that it is adequately risk-aligned and resilient to cyclical developments to support soundness of the economy. The findings are in agreement with the observations made by Ewert, Schenk and Szczensy (2000) that high-risk firms may offer valuable collateral and probably accept high premiums. These findings prescribe the minimum level which DFIs should observe to ensure prudent conduct in the operations of credit granting activities. Similar with the banking institutions, DFIs are free to adopt more stringent standards in their risk management policies.
In relation to the findings, credit risk continues to remain the largest source of risk for DFIs in Kenya. This is due to the fact that a DFI’s financing portfolio is basically the largest asset and the major source of revenue. Most of Shelter Afrique’s clients were of the opinion that DFIs practice of client inclusiveness is likely to translate into repeat business. Hence, development finance institutions like Shelter Afrique play a key role in the developing low-income project financing by providing debt capital and working to structure mortgages in a way that is affordable to clients.

As established from the study, banks have realized that while the demand for real estate financing is tremendous, there is no substitute for prudent lending policies. Some of the banks have withdrawn from the real estate market after being saddled with an unduly high amount of nonperforming loans. Further, there have been several problems in the real estate financing with several warnings raised for cautious lending and recovery. This contrasts the existing literature Chodechai (2004), who reveals that DFIs are better substitutes for financing of real estate. Their culture of client inclusiveness is able to drive capacity building, insight to business model and better understanding of the DFI.

The study also revealed that use of insurance and bank guarantees is an effective way of mitigating credit risks. The study showed that absence of proper management of such risk has consequentially resulted into significant losses for a number of DFIs. The consequence of such losses not only disrupts the intermediation function of the DFIs affected, but also imposes large financial burdens on the government in recapitalizing such DFIs. It is anticipated that as the size of the DFI’s balance sheet increases over time, the potential financial burden escalates proportionately. Effective credit risk mitigation is therefore vital to ensure that a DFI’s credit activities are conducted in a prudent manner and the risk of potential DFI failures minimized.

The ability of DFIs to identify, measure, monitor and control the risks they face as well as to determine that they hold adequate capital against those risks is a critical component in assessing whether and in what form to grant credit, DFIs consider the risks against the expected return, with regards to price and non-price terms. They can use collateral and
guarantees to help mitigate risks though transactions should be ultimately entered based on the intrinsic strength of the borrower’s repayment capacity. However, given their policy mandate to contribute to socio-economic development, DFIs also include key development impact measures in their lending criteria and put in place a proper system to identify social and environmental risks associated with their financing activities. From this perspective, DFIs in Kenya exhibit mixed behaviors. On the one hand, they seem to be financially prudent when granting a loan, with most of them requiring that the borrower contributes a certain amount, say, at least 25% of the total project cost with equity and provide collateral in the form of cash and physical assets to cover at least 35% of the loan value.

5.4 Conclusion

5.4.1 Adequacy of DFIs’ Lending Policy

DFIs in Kenya are required to be self-sustaining, and must increasingly raise funds independent of government guarantees. However, they still have to keep an eye to their credit ratings and adopt prudent lending policies to cope with risk management practices. Ultimately DFIs end up prioritizing their financing activities at the expense of high risk segments of the market which may remain neglected. However, some DFIs attempt to solve this by introducing special-purpose grant and soft loan windows to aid in reaching clients in a way that does not compromise their basic functions and sustainability. The primary role of DFIs in the market economy is to crowd in private financial flows by availing a package of services that not only fill the fiscal gap between capital for public good finance availed by the state on one side and commercial projects on the other, but also pursue to limit the gap in the finance system.

5.4.2 Nature of Development Constraints

For DFIs to succeed within the rapidly changing global and regional environment they must meet a number of challenges for their effective management. Empirical evidence justifies that once DFIs are provided with strong governance structures and the right incentives they can play an effective role in expanding financial access and therefore contributing to both economic and social development. This normally entails focused and clear mandates accompanied by robust corporate governance standards, appropriate lending and risk management technologies, proper performance assessment criteria, financial sustainability,
and the recruitment and retention of qualified staff. DFIs must also actively participate in all the projects they fund as the will resolve any constraints early in the project life. DFIs should ensure that the project team, that is, the professional team and the contractor are well experienced in the market and that there is no room for errors in the rolling out of the project. In addition, advisory services should be offered to the developers, as a guide or reference point as the move along with the project. DFIs should involve the government more in the rolling out of the project to create a sense of inclusivity and therefore attract more cooperation from the government on areas they are supposed to collaborate.

### 5.4.3 Alternative Approaches to Financing Real Estate

In Kenya, DFIs tend to play a very significant role in addressing issues to do with market failures in the credit markets. Moreover experience with DFIs in the past has led to skepticism of the ability of development finance more specifically where Kenyan banks were and are still used for non-commercial, quasi-fiscal purposes hence posing a risk to financial sector stability. Development finance is unable to compensate for deficiencies in national and regional policy gaps and also institutional capacities, which in turn make DFIs an ineffective mechanism for unfunded public sector mandates. The primary function of DFIs requires use of sound banking principles to ensure that inadequate capital is acquired at an affordable cost and allocated efficiently, consistent with both risk and return. Cost effective intermediation is key for DFIs customers, who basically cannot afford high interest rates, and most often cannot access commercial bank services.

### 5.5 Recommendations

#### 5.5.1 Recommendations for Improvement

##### 5.5.1.1 Adequacy of DFIs’ Lending Policy

Development Financial Institutions in Kenya should not be permanently enshrined institutional structures but rather they need to work towards successful transformation of both developmental financing and funding through their lending policies. DFI’s should be able to set limits to safeguard liquidity or alternatively they may choose to comply with limits set by financial regulators and if not actively regulated, be at par with international standards.
Lending Limits are usually set with regards to demand in the market to ensure that the policy become more accommodative to both experienced developers and non-experienced ones. DFI s may not be profit maximizers, however, their profit generation capacity is arguably a key determinant of their long term success or failure.

5.5.1.2 Nature of Development Constraints
In order to mitigate constraints, DFI s require sound governance and financial management, an ability to balance cost effective intermediation and risk management with outreach through smart partnerships, capacity building and knowledge management and flexibility. Good corporate governance structure should be embedded in their operations as a means of enhancing their performance and the ability to handle complex transactions. This should be vividly demonstrated through the appointment of qualified and experienced professionals and also reinforced with effective checks and balances through a successful audit function. Additionally, DFI s’ accountability need to be enhanced by a legal framework in which such financial institutions should be obliged to disclose appropriate financial performance activities to the relevant authorities and the larger public. DFI s should enhance their partnerships with various government institutions so as to be able to take charge of a constraint that is on the government front. DFI s should assess the experience of project teams to allow experienced professionals to guide the process. DFI s should ensure that close monitoring and evaluation is enhanced at all times to capture any constraints early.

5.5.1.3 Alternative Approaches to Financing Real Estate
In order for DFI s to mitigate credit risk and do repeat business with their clients in a more innovative way, they need to take into account the fact that banking institutions are increasingly enhancing their capacity and capability and it is expected that they may even diversify into new areas, not forgetting those, currently served by the DFI s like real estate. DFI s therefore need to review and analyze their areas of comparative advantage and complement each other rather than compete with the banking institutions. This will go a long way in ensuring that DFI s remain relevant in the market in this turbulent environment. As a measure of enhancing their competitive edge they need to investment in new technology, which is the key to increasing their capacity, efficiency and effectiveness in order to provide specialized financial services, processes and procedures should be better managed through
greater use of information and communication technology, adopt alternative security methods like insurance and bank guarantees rather than the normal securitization methods of charging land, invest (Equity stake) more in alternative technology companies to ensure delivery of construction products that are fit to be used in the market.

5.5.2 Recommendation for Further Research

The study established that DFIs play an important role in real estate development with regards to financing of projects in Kenya. It highlighted the fact that DFIs are better geared towards financing of projects as compared to commercial banks. However, financing of real estate is a new concept and there is need to investigate new sources, products and also mechanisms of financing real estate. Therefore, the researcher recommends future studies to investigate other financing options and their suitability in this industry.
REFERENCES


APPENDIX- QUESTIONNAIRE

THE ROLE OF DEVELOPMENT FINANCIAL INSTITUTIONS IN REAL ESTATE IN KENYA: A CASE OF SHELTER AFRIQUE

This questionnaire is part of a research study for Masters of Business Administration (MBA) at the United States International University- Africa. The purpose of the study is to investigate the role of development financial institutions in real estate in Kenya. Your response will be treated with strict confidentiality by the researcher, and no respondents will be identified individually.

SECTION 1: Respondent’s Details
1. Sex  Male ☐  Female ☐
2. Age  25-35 ☐  36-45 ☐  45 and Above ☐
3. Years company has been in the industry …………………………………
4. Position in the company: Owner ☐  Director ☐  Manager ☐  Employee ☐

SECTION 2: Adequacy of Lending Policy
5. (a) How many times have you taken up a loan with Shelter Afrique? (Tick the appropriate box)
   Once ☐  Twice ☐  2-5 Times ☐  5-10 Times ☐  More than 10 times ☐

   (b).Were you comfortable with the lending policy that directed the terms of your loan?
   1. Yes ☐  2. No ☐

   (c).If No in (b) above, what were you uncomfortable with?
   ————————————————————————————————————————————
   ————————————————————————————————————————————
   ————————————————————————————————————————————

   (d) Do you think that the Shelter Afrique lending policy is adequate enough for the Kenyan Market?
   1. Yes ☐
   2. No ☐
(e) If No in (d) above, what changes do you think could be made on the lending policy to improve Shelter Afrique’s efficiency and be able to accommodate more players under its portfolio?

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6. Does the Shelter Afrique’s Lending Policy assist in achieving the listed outcomes?

<table>
<thead>
<tr>
<th></th>
<th>Strongly agree</th>
<th>Agree</th>
<th>Neutral</th>
<th>Disagree</th>
<th>Strongly disagree</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Reduces the response time</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>(b) The lending policy fosters negotiations</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>(c) The lending policy guides the minimum and maximum amounts</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>(d) The lending policy guides the relationship with the client</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>(e) The lending policy indicates the level of assistance by the lender</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>(f) The lending policy guides the credit analysis process</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>(g) The lending policy guides the pricing decision</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>(h) The lending policy eases Credit Referencing</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
</tbody>
</table>

SECTION 3: What kind of constraints do you experience in delivering Real Estate projects/ Mortgages?

8 (a) Have you ever experienced a constraint during the delivery of your objective as a company?

1. Yes
2. No

□

□
(b) If Yes is (a) above, what constraints were these?

9. (a) How well would you say you are able to mitigate these constraints?
1. Not well  
2. Just an Idea  
3. Moderately  
4. Well  
5. Very Well  

(b) How would you rate the importance of Shelter Afrique in assisting mitigate this constraints?
1. Not Important  
2. Necessary  
3. Very Important  

(c) What can Shelter Afrique do to assist mitigate this constraints?
10. Do you think the following factors enhance efficiency in delivery of projects?

<table>
<thead>
<tr>
<th>(a) Increase of Loan tenure</th>
<th>Strongly agree</th>
<th>Agree</th>
<th>Neutral</th>
<th>Disagree</th>
<th>Strongly disagree</th>
</tr>
</thead>
<tbody>
<tr>
<td>(b) Increase of Grace Period</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(c) Involvement in the vetting of professional team</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>(d) Involvement in the tendering process</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>(e) Involvement in the selection of Marketing Team</td>
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<td></td>
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<tr>
<td>(f) Constant Monitoring and Evaluation</td>
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<td></td>
<td></td>
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<tr>
<td>(g) Use of Independent Project Managers</td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>(h) Any other - state and rate</td>
<td></td>
<td></td>
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<td></td>
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</table>

SECTION 4: Will alternative approaches be able to address the current issues in the industry?

13. How relevant are the contemporary methods used to mitigate credit risk? (please tick one)

- Very relevant
- Quite relevant
- Not Relevant
- I don’t Know

14. What do you think can be done to motivate you to be a repeat client of Shelter Afrique in relation to alternative approaches used by the institution?

15. How willing would you be to be involved in an activity/exercise that would help define the alternative approach used by Shelter Afrique in Mitigating Credit Risk?

- Very Willing
- Quite willing
- Not willing
- I don’t know
16. Do you think that the activities (No.15 above) would motivate you to be a repeat client of Shelter Afrique?

YES □ NO □

(b) Explain
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17. How well do you think having the following activities would influence you to be a repeat client of Shelter Afrique, as an alternative approach to credit Risk Mitigation?

<table>
<thead>
<tr>
<th>Activity</th>
<th>Strongly agree</th>
<th>Agree</th>
<th>Neutral</th>
<th>Disagree</th>
<th>Strongly disagree</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Use of Insurance</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>(b) Use of Bank Guarantees</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>(c) Use of positive and Negative covenants</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>(d) Use of other properties as legal charge</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>(e) Use of assignment of receivables</td>
<td>5</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
</tbody>
</table>

*** Thank you for your time and cooperation ***