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Private Sector Investment in Informal Settlements: Partnerships for Innovations and for Creating Investment Opportunities

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Executive Summary

Recognizing the key role played by the private sector in all areas of development, engaging the business community is critical to the realization of the sustainable development goals (SDG). Even though approx. 60% of urban populations in Africa live in informal settlements, the economic importance of this large market remains untapped, yet it presents lucrative business opportunities. Companies and investors lack the enabling environment needed to develop business cases for modern solutions and affordable innovations for informal urban areas. Achieving settlements upgrading at scale requires diverse partnerships and the mobilization of innovation. Private sector engagement needs to consider individual and collective interests; leaving no one behind. Innovations must be inclusive, context-appropriate and affordable.

There is a huge opportunity for private sector investment in informal settlements based on the existing demand and purchasing power: A conservative estimates put the purchasing power of households in informal urban areas in Kenya at USD 6.1 billion, 7% of GDP, demonstrating the significance of this is an untapped potential. In the next decade the demand and purchasing power in informal settlements will grow. At the same time, there is a broad range of innovations and solutions developed by the private sector for housing and infrastructure and the proof of concept for bankable projects is there. There are many different business initiatives in informal settlements and successful concepts, that can be scaled.

Inclusive and enforced governance and legislation are key for an enabling environment for investment into the informal sectors. Governments should focus on facilitating those investments through a strategic private sector engagement supported by an enabling policy environment. Private sector must identify its niche and target a specific sector solution for the populations in informal settlements.

Complementary approaches and solutions should be explored as there is no one solution to fit all. For example, participatory approaches can mobilize and organize communities towards public private people partnerships (PPPP's) and to uncover local contributions. Community managed revolving funds can provide business models, and with technical support and seed capital to communities they can be a starting point for private sector and governments to engage at scale with public and private finance.

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1. Introduction / Background

Today, one billion people live in informal settlements. This population is set to increase by another 2 billion by 2050, with the largest proportion of people residing in Sub-Saharan Africa and Asia. The challenges of rapid urbanization that cities are facing globally are expressed in the growing proliferation of informal settlements in urban areas. Provision of affordable and environmentally sustainable housing and basic services for the urban poor remains a key challenge for many countries. In Sub-Saharan Africa urban poor living in informal settlements constitute 62% of the total urban population. Despite the progress in improving informal settlements – represented by a decrease from 39% to 30% of the urban population living in informal settlements between 2000 and 2014 – absolute numbers continue to grow, and the challenge remains critical.

For having been excluded from the urban fabric for decades, residents of informal settlements, particularly women and children, bear a disproportionate burden of poverty. Marginalized from formal development processes, these communities lack access to housing, water, sanitation, waste management and other basic services. Without security of tenure and the capacity, skills, financing and productive assets required to make out a living, they earn low incomes and lack employment opportunities. These factors have conspired to perpetuate the cycle of poverty as these poor urban households are compelled to resort to negative coping mechanisms and risky survival strategies, particularly during crises like the COVID-19 pandemic.

The magnitude of the challenge has been recognized globally and included as part of the international development agenda. Target 11.1 of Sustainable Development Goal 11 commits states and their development partners to ensuring access for all to adequate, safe and affordable housing and basic services and upgrade informal settlements by 2030. This global goal guides countries towards sustainable urbanization that involves improving living conditions in informal settlements by improving access to affordable housing and upgrading slums. Similarly, the New Urban Agenda's (NUA) principle of "Leaving No One Behind" and commitment to "Sustainable Urban Development for Social Inclusion and Ending Poverty" binds member states to paying special attention to urban poverty and the needs of people living in informal settlements.

The key issues are the lack of urban planning, overcrowding, lack of appropriate housing and infrastructure, including lack of socioeconomic services, and lack of vital basic services, including water, sanitation, and waste management. Other issues are environmental degradation, health deprivation, traffic congestion and lack of access to education, health services, employment and business opportunities. The key challenges to ensure a sustainable urbanization that includes all people, including those 62% living in informal settlements, are policy development and financing for affordable housing, water, sanitation, waste management, transport and social infrastructure. Making 'business easy' in informal settlements requires new approaches to the formalization of the economic development in informal urban areas.

The United Nations Human Settlements Programme (UN-Habitat) together with the European Commission (EC), and the Organization of African, Caribbean and Pacific States (OACPS) entered a tripartite partnership to address the challenge of informal settlements in these states with the launch of the Participatory Slum Upgrading Programme (PSUP) in

2008. With funding from the European Commission (EC) the PSUP has been implementing upgrading projects with co-financing contributions from participating ACP partner governments. The PSUP implements strategies, policies and projects to address the widespread and chronic urban poverty in informal settlements, in contribution to the SGD 11 “By 2030, ensure access for all to adequate, safe and affordable housing and basic services and upgrade slums”. One of the Programme’s strategic objective is to strengthen global partnerships for participatory upgrading and prevention, and this involves partnerships with the private sector.

The Private Sector Partnership Initiative of the PSUP was launched in June 2020 at the Private Sector Partnership Forum. The Forum was organized in recognition of the critical roles played by the private sector in innovating and piloting novel solutions to development challenges, and the public sector in scaling up successful innovations. The PSUP commissioned Market Studies, whose findings were shared at the forum highlighting the important contributions made by micro-, small- and medium-sized enterprises in economic growth, job creation and the provision of essential goods and services. These studies demonstrated the potential for partnership between national governments and municipalities with private sector companies, specifically investors and innovators with low-cost innovative solutions to urban development challenges.

2. Methodology for Private Sector Engagement

1. Conduct market studies to analyse the investment opportunities in informal settlements focusing on the sector of priority (water, sanitation, energy, waste management, affordable housing etc.)
2. Facilitate the matchmaking of governments and investors with investable innovative private sector solutions
3. Launch a city-specific or national Call for Partnerships / Call for Investments - Companies should be selected based on the relevance of their innovative solutions to informal settlements development and their capacity to improve living conditions. The selection criteria that can be applied are:
 - i. Applicability in the country and applicability in informal settlements
 - ii. An innovative solution or product must already be existing and available for deployment in informal settlements
 - iii. A Company offers a solution or product that is innovative and responding to the needs of the urban poor
 - iv. Affordability for the Municipality and the target community: the company needs to have developed a financing model that makes the product solution affordable to the urban poor
 - v. The innovative solution or product must be scalable to target a wider population at a citywide scale
 - vi. The innovative solution or product is sustainable – socially, economically, environmentally, financially
 - vii. Priority should be given to solutions that are strengthening the urban poor’s capacity to develop businesses, manage services and maintain equipment, services, infrastructure

4. Organize a national forum for private sector investment and partnerships inviting a wide range of key stakeholders including city governments, decision-makers, innovators, financing partners and investors to identify opportunities for investments and partnerships.
5. Demonstrate business potential and explore opportunities to develop and deploy low-cost innovative solutions in informal settlements | Develop a pipeline of bankable and investment-ready projects for implementation in informal settlements fostering partnerships between local governments and the private sector.

3. Deploying Innovative Private Sector Solutions to Challenges in Informal Settlements: Private Sector Partnerships for Creating Investment Opportunities

The challenges of rapid urbanization affect all urban sectors that concern informal settlements, with the main ones being financing, housing, water, sanitation, waste management and energy.

3.1 Financing Challenge

Many countries have struggled to attract enough development finance and investment to meet the access challenges in key sectors due to legal, political, institutional and financial barriers that have remained unresolved for decades.

In sub-Saharan Africa, the informal economy is the backbone of development, employing nearly 86% of the labour force. Sadly, the financing needed by small-scale industries (manufacturing and services) to grow, innovate, improve efficiency and create employment opportunities remains a significant challenge. While 31.5% of small-scale industries worldwide benefit from loans and lines of credit, only 20.7% of those in sub-Saharan Africa receive those types of financial services.

3.2 Affordable Housing Challenge

Provision of durable, affordable and environmentally sustainable housing for lowest-income households remains a key challenge for many countries. The players in this industry are too few and there is minimal interest of private sector housing developers to provide low-income housing. The sector is driven by the much higher profitability and demand of the middle-and high-income housing market, leading to a huge shortfall in supply of affordable, low-income formal housing for the urban poor. The cost of production and the opportunity cost to the developer's aren't attractive enough to serve the lower market segments. Provision of low-cost housing to lower income groups is also hugely affected by the cost of land and inadequate infrastructure investments by governments. The motivating factors for developers venturing into the lower market segment are few, while appropriate housing models and solutions are limited.

3.3 Water, Sanitation and Waste Management Challenge

It is estimated that 2.2 billion people lack access to clean and safe drinking water, 4.2 billion lack access to adequate sanitation, and 3 billion lack basic handwashing facilities. Whereas 1.8 billion people have gained access to basic drinking water services since 2000, there remain vast inequalities in the accessibility, availability and quality of these services. Inadequate water and sanitation services significantly contribute to the mortality burden, with poor sanitation estimated to claim 1.6 million lives annually and to contribute to numerous grave health conditions, that have a big negative impact of economic productivity of countries.

3.4 Clean Energy Challenge

It is estimated that 1 billion people lack access to electricity and approximately 3 billion people cook using polluting open fires or simple stoves fuelled by kerosene, coal and biomass in the form of wood, animal dung and crop waste. Household air pollution is one of the leading causes of disease and premature death in the developing world, causing an estimated 3.8 million premature deaths annually and acute respiratory infections, particularly in sub-Saharan Africa, where advances in the use of clean fuels and fuel-efficient stoves have not kept pace with population growth. With 12 million Africans joining the labour force each year, more income and employment opportunities need to be created, and this means finding innovative ways of accelerating access to loans or lines of credit for households and businesses.

3.5 Deploying Innovative Private Sector Solutions

The creation, development and diffusion of knowledge, technologies and innovations are powerful drivers of inclusive and sustainable socio-economic and urban development. As knowledge and skill diffusion are considered key to the reduction of inequality, investment in innovation capability is imperative if the SDG are to be realized. For lagging behind other continents in knowledge and skill diffusion, Sub-Saharan African continues to experience inefficiencies and productivity challenges in various sectors, significantly slowing down its economic growth and perpetuating income inequalities.

The COVID-19 pandemic has caused significant socioeconomic disruptions worldwide and is expected to have particularly devastating impacts in developing countries. Due to weak national health systems and economies, developing countries are expected to lose in excess of USD 220 billion, exacerbating the vulnerabilities of their predominantly poor populations. This is particularly so for populations living in densely populated informal neighbourhoods with insufficient access to water, sanitation, waste management and employment. Whilst the pandemic presents a significant challenge to economic growth, the new normal also offers numerous opportunities for innovation, investment and policy reform in key sectors that have lagged behind the sustainable development agenda.

There are numerous opportunities for Private Sector Partnerships and investments that are strategic and sector- and project-specific. For this reason, the Participatory Slum Upgrading Programme (PSUP) of UN-Habitat has taken steps towards addressing this opportunity and duly matching private sector innovations and solutions with the needs in informal urban settlements. The Private Sector Partnership Initiative of the PSUP was

launched in June 2020 during the Private Sector Partnership Forum. The Forum was organized in recognition of the critical roles played by the private sector in innovating and piloting novel solutions to development challenges, and the public sector in scaling up successful innovations. The event brought together over 300 participants from national governments, municipalities, financing partners, the private sector, 78 Speakers and Presenters, 34 Innovations across 7 sectors and communities from informal settlements.

The interest generated by the forum demonstrated the huge demand for sustainable solutions and investment and business opportunities in the informal settlements. It explored innovative solutions to affordable housing, water, sanitation, waste management, health, education, energy and financing challenges, and ways to mobilize expertise, solutions, investment, finance and governance to deliver in innovative ways. The forum explored how to scale up interventions and establish People Public Private Partnerships (PPPPs) for bringing in innovation and local ownership – in the initial phase focusing on Africa.

The key recommendations made during this engagement have informed the strategic thinking behind the private sector partnership initiative to:

- Facilitate matchmaking governments and investors with investable innovative private sector solutions
- Demonstrate business potential and explore opportunities to develop and deploy low-cost innovative solutions in informal settlements
- Develop a pipeline and project platform of bankable and investment-ready projects for implementation in informal settlements fostering partnerships between local governments with the private sector

Market Studies facilitated by UN-Habitat to identify investment opportunities in informal settlements were presented at the forum. They brought to light the important contributions made by micro-, small- and medium-sized enterprises in economic growth, job creation and provision of essential goods and services and the potential for partnership between national governments and municipalities with private sector companies - specifically investors, international financing partners and innovators with low-cost innovative solutions. The market studies were conducted in four countries, in Kenya, Nigeria, Cameroon and Senegal, and identified entry-points for private sector investment and business cases for informal settlements. The opportunities are manifold, addressing housing, water, sanitation, waste management, transportation, energy, health services, education and economic infrastructure. Partnerships between the private sector, investors, the government and communities can provide an enabling environment for investment into the informal sectors. The key challenges to doing business include the legal and regulatory limitations, status of informality, levels of savings and the costs of doing business. Most importantly, the opportunities for investment require analysis per sector. Market studies can serve as an important tool to identify the barriers to private sector investment.

The key findings from the forum, the engagement with partners and from the market studies are:

- There is evidence that there is purchasing power in informal settlements – which is increasing. For example, it is estimated that the purchasing power of informal

households in Kenya is 6.1 billion USD, 7% of GDP – this is an untapped potential. In the next decade the demand and purchasing power in informal settlements will grow further - 40% of this purchasing power goes to infrastructure and housing services and there is a big opportunity for investment in informal settlements.

- There is a demonstrated business potential for bankable projects in informal settlements: There is a broad range of innovations and solutions developed by the private sector already for affordable housing, infrastructure and services applicable in informal settlements, that can be replicated – and together with other initiatives and actors they can become a strong package to transform neighbourhoods, whole districts and cities.
- Governments should focus on facilitating investments and private sector engagement with an enabling policy environment. What investors are looking for is a transparent economy, and a political system that is not easily impacted by external factors and instability. The government should provide a stable platform to ensure that companies are not subject to unexpected volatility which would help attract investors.
- Private sector must identify its niche and target a specific sector, while expanding subcontracting opportunities to micro enterprises and through PPPs.
- Achieving informal settlements upgrading at scale requires diverse partnerships and the mobilization of innovation and finance at scale. Blended finance is needed to reach scale and to introduce new business models and innovations.
- Participatory approaches are key to mobilizing and organizing communities towards PPPs and to uncover local solutions and contributions. Partnerships between formal and informal sectors are an important first step for formalization of the informal market.
- Community Managed Funds provide a reasonable business model, technical support and seed capital to communities which can be leveraged and are a starting point for private sector and governments to engage and scale with public and private finance.
- The COVID-19 pandemic has highlighted the huge impact of unequal access to basic services on rates of infection in underserved and overcrowded informal urban areas. The crisis is a challenge and an opportunity to provide sustainable basic water and sanitation services and infrastructure in informal settlements and to facilitate finance for deploying low-cost innovations at scale, that will have a crisis mitigation effect now and in the future.

4. Partnership with Mr. Green Africa for Waste Management | Case Study

The project is part of the PSUP's Private Sector Partnerships Initiative under the component for innovation project partnerships. Through strategic financing and project partnerships with the private sector, the social and economic impact of business models shall be upscaled in informal settlements, and UN-Habitat's participatory community-based methods, training and tools shall provide an enabling environment for the replication and sustainable growth of the innovative private sector methods and solutions. The partnership will be multi-lateral and provide an enabling environment for investment into the informal waste sector involving the city government of Kisumu.

Together with the private sector partner, Mr. Green Africa, UN-Habitat will implement the project 'Turning Waste into Jobs' which will support community-based waste management

in low-income areas and informal settlements through Fair Trade Plastic Recycling. The private sector partner has been selected based on criteria defined in the Call for Partnerships, to which the company responded with an expression of interest. Mr Green Africa recycles and sells ethically sourced materials with a social and environmental impact. It engages over 2,000 previously marginalized waste collectors and sells over 2,000 metric tons sourced recycled materials for local and international markets. The business seeks to formalize the plastics supply chain and create jobs, as well as relieve growing cities from plastic pollution build on the principles of circular economy. The collected plastics are processed and sold as post-consumer recycled plastics to plastics manufacturers for use by large fast-moving consumer goods companies.

The project shall support the Integrated Solid Waste Management Plan in Kisumu, Kenya, and establish an enabling framework for Public Private People Partnerships (PPPPs) for the sector in informal settlements, achieving a formalization of the waste sector in informal settlements. The project shall also create formal jobs. The partnership is designed as a quick-win project on how to manage a waste centre by the community as a pilot and to test a model for a financially sustainable Waste Recovery Centre, starting with plastic waste. UN-Habitat will partner with a non-profit organization experienced in the area of community mobilization and participation, participatory methods, capacity building in the use of community managed funds and together with the private sector partner the following partnership work will be carried out:

- Support to the City of Kisumu Integrated Solid Waste Management Plan
- Create a community-based waste management system and establish a model for a Public Private People Partnership (PPPP) in informal settlements through Fair Trade Plastic Recycling
- Support to the city and the county development plan for waste management in informal settlements
- Mobilizing community-based stakeholders and existing cooperatives and support them through organization and training in community-based waste centre management
- Establish a financially viable waste centre that is managed by the community
- Create 400-500 Formal Jobs in one year

The goal is to establish a model for public private people-centred partnership for the waste sector between the local government, communities and the private sector implementing an innovative business case that supports the improvement of living conditions in a selected informal settlement. The project will provide job creation and improved waste management. While the private sector partner will implement their innovative business model the non-profit partner will bring additional value in skills transfer and experience in sustainable job creation in the waste sector.

Mr Green Africa will deliver technical expertise and own investment to enter the market in Kisumu to set up community centre logistics and together with UN-Habitat support a community-based organization with training and skills transfer in waste management and waste centre organization. UN-Habitat and its non-profit local partner will work with community organizations, carry out participatory planning, support them in community organization, the set-up of a project steering committee and establishment of a community managed fund. Mr. Green Africa serves as a sustainable off-take partner to the

centre and buys the plastics at fair prices and supports the financial viability and sustainability of the centre. The City of Kisumu signs a district performance contract and formalizes the partnership to a PPPP. The Waste Centre surplus income will be paid directly into the community managed fund that will serve to improve quality of life of centre members from the local community and their families.

Partnership Model

- Innovation Project Partnership to create Business Opportunity and a Business Case in Low-Income Communities and Informal Settlements
- Formalization of a Public Private People Partnership (PPPP) through the project

Financing the Partnership

- Direct investment from the business partner to the implementation of their innovative solution in with their business plan to expand to a new market. No funds shall be provided to the private sector partner by the city or the UN, but partners operate on an agreed upon project budget toward the achievement of the partnership objectives
- Co-finance from the involved government institutions is possible to support the community-based management
- UN-Habitat through the PSUP (EC funds) finances project level activities, i.e. capacity building/training, technical assistance, local community organization and implementation management on community level

5. Conclusion

Based on experience, we recognise the importance of engaging with local communities in identifying sustainable solutions to the challenges bedeviling them, as they are the best resources in terms of articulating their most pressing needs and the most workable solutions. Achieving lasting change requires partnerships between local communities and solutions providers, particularly the private sector, and financing partners to unlock their development potential.

The innovative financing solutions that PSUP is working to deploy can be replicated in Arab countries to stimulate innovation in critical sectors to accelerate delivery of affordable solutions and catalyse investment. The community-managed funds are a tool that enabled us to leverage public financing for community-driven programming in response to chronic deprivations. While the problem of informal settlements is incomparable to that of Sub-Saharan Africa, the solutions that PSUP has deployed and tested in this region can inform the development of context-appropriate solutions in the Arab region.

PSUP has established that challenge-driven solutions are effective solutions to market failures, particularly those related to the failure of markets in the informal settlements to

attract investment and private sector participation in response to chronic deprivations. The recommendations for the Arab region are:

- Increase the competitiveness and sustainability of private-sector-led solutions
- Facilitate access to the capital needed to commercialize promising early stage innovations and bring existing innovations to scale
- Facilitate matchmaking governments and investors with investable innovative private sector solutions
- Develop a pipeline and project platform of bankable and investment-ready projects for implementation in informal settlements fostering partnerships between local governments with the private sector

6. References

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