Economic Issues in Housing Reconstruction

Published by:
Intertect
1789 Columbia Road, N.W.
Washington, DC 20009 USA

Available from:
Intertect
1789 Columbia Road, N.W.
Washington, DC 20009 USA

ECONOMIC ISSUES IN HOUSING RECONSTRUCTION

Frederick C. Cuny

Paul Thompson

1981

INTERTECT

ECONOMIC ISSUES IN HOUSING RECONSTRUCTION

1. ORIENTATION

It has been noted by certain disaster specialists that response to an emergency is a humanitarian concern while reconstruction and longer-term recovery activities are primarily economic in nature. This is especially true for housing programs. Thus, utmost care should be taken to carefully examine all the economic issues related to housing reconstruction or housing modification. A carefully conceived program can reduce the economic hardships on the disaster victim, while a program which has failed to consider the economic consequences of actions and how they relate to prices, inflation, etc., can have an adverse effect on the local as well as the national economy and significantly extend recovery time. For the project planner, the economic consequences of actions determine the overall feasibility of successfully completing a project as designed.

2. KEY ISSUES

There are four key economic issues which should be considered when planning a housing reconstruction program:

A. Determining Appropriate Strategies For Each Economic Group

It is important that a mix of strategies and programs be developed to serve different economic groups within the affected community. A common problem among relief programs is that an agency will establish only one program and try to make it fit the needs of all victims. Organizations should realize that different economic groups and classes have different post-disaster needs and capabilities. For example, loan programs are more appropriate for urban homeowners than rural landless farm workers. Subsidized materials may be more appropriate for rural farmers and villagers.

B. Inflation

Inflation is one of the most difficult aspects to deal with following a disaster. Program planners must be careful to ensure that their actions and projects do not contribute to inflation, and appropriate measures should be taken to recommend that local government authorities take suitable steps to control prices of reconstruction materials.

It should be remembered that a certain amount of inflation following a disaster is natural. Suppliers within an affected area may have incurred losses and should be allowed to raise prices a reasonable amount in order to recover themselves. A reasonable price increase, however, is not the same as profiteering, and actions should be taken to ensure that unreasonable price hikes are not encouraged or permitted.

Some strategies for controlling prices are:

(1) Working Through The Local Market System

Relief agencies can serve as an intermediary between disaster victims and the market by placing large orders for relief materials (with a reasonable markup allowed) with the provision that the supplier sell at a fixed price. A variation of this approach is to guarantee a certain level of sales at a fixed price so that unreasonable price hikes are not encouraged or permitted.

(2) Establishing Alternative Distribution Systems

If the local suppliers refuse to lower prices of key items, relief agencies can purchase these items outside the community and offer them to disaster victims at the normal or a lower, subsidized price. In many cases, this competition with the normal market will bring prices back into line.

It is often proposed that large quantities of free materials be strategically "dumped" as a means of controlling prices. There is little evidence that this approach has worked. As a general rule, subsidized materials are more likely to serve as a price control measure than free goods and, by working through the markets, more influence can be exercised.

(3) Price Controls

Price controls are a much-debated method for controlling inflation. Usually, governments or agencies are wary of instituting price controls for fear that they will create a black market for the items on the control list. There is little evidence, one way or the other, to support or refute these claims. It has been noted, however, that price controls are not effective unless they cover not only the controlled items but the transportation costs as well.

(4) Centralized Purchasing

One of the factors which often sets off inflation following a disaster is competitive purchasing by relief agencies. Suppliers often play one agency against the other in order to raise the prices. One means of combatting this practice is to establish a price coordination committee among the relief agencies to set uniform prices that the agencies will pay in order to obtain the materials. Because relief agencies can represent a substantial portion of the demand for materials, suppliers can often be persuaded to reduce prices accordingly. This type of approach, however, will only be successful if all agencies agree to the prices established by the coordinating body.

C. The Use Of Local Markets/Suppliers

Many relief agencies find dealing in a post-disaster marketplace to be a particularly fustrating endeavor. Not only are there language and cultural barriers, but in the post-disaster situation, it may be difficult to make contact with the right suppliers for the right materials. Thus, many agencies feel that in the interest of speed, it is easier to purchase their materials outside the affected area.

While this practice is justified in extreme cases, or where local suppliers are not available, it often compounds recovery problems for the local community. As a general practice, it is better to work within the local market system rather than with suppliers from outside the community. This has the advantage of stimulating recovery of the market system and keeps money within the community, creating spin-off benefits which are badly needed following a disaster. In reconstruction programs, the time saved by going outside the normal market system is usually of little consequence in the overall recovery picture, and the economic advantages of dealing within the market system generally far outweigh any advantages of speed.

D. Whether To Sell, Subsidize Or Donate Building Materials

One of the questions which always arises during reconstruction, especially in housing, is whether materials should be sold, subsidized, or given free to disaster victims. For humanitarian reasons many agencies feel constrained to give away the materials at no charge and, indeed, many materials are supplied to agencies with the constraint that they will not be sold. Experience indicates however, that it is far better to either sell or subsidize building materials than to give them away. There are five reasons for this:

(1) By subsidizing or selling the materials, the money returned can be reinvested, and more people can be served.

(2) Sales at reasonable prices can serve as a stabilizing factor in the materials market.

(3) A sales program will enable each family to acquire the amount of materials that it needs without affecting material availability to other families.

(4) Development officials point out that sales or subsidy programs are more in keeping with the development goals pursued by most countries. (Sales have more "dignity" and are less likely to create dependency relationships than distribution of free materials. It is also a means for measuring the relative value that the disaster victims place on the material being offered).

There are, of course, some people who will not be able to purchase the materials, even at a greatly subsidized price, and allowances should be made to provide opportunities for persons to earn either the materials or the cash in order to purchase them.

(5) The availability of cash. A key issue in any housing program is the amount of cash the victims will have to contribute to their share of the reconstruction effort. Agencies have consistently underestimated the amount of cash on hand which can be devoted to a housing reconstruction program. The availability of cash, however, is often related to seasonal factors such as the agricultural harvest. In determining the victims' cost participation in any housing program, project officials should remember that it may be unreasonable to expect a high level of participation in a housing reconstruction program soon after a disaster, as it may take several months to reestablish jobs, agriculture or herds, and to recover economically to a point where sufficient reserves are available. This may take several months to several years. Burdening a victim with a housing loan, even on easy terms, immediately following a disaster may be compounding problems for the victim, not alleviating them.

3. KEY CONCEPTS

Five key concepts to remember when considering the economic consequences and impact of a housing reconstruction program are:

A. Disasters are interruptions of the normal economic processes and the process of development. While disasters may destroy physical structures and facilities, they do not destroy the processes and systems.

B. Relief programs should utilize and build upon these normal markets and economic systems to the greatest degree possible. The normal marketing systems play a large part in any community's ability to develop and to cope with a disaster. By ignoring or bypassing these systems, relief programs may adversely affect community development.

C. The normal market systems may need to be stimulated by the relief program in order to recover. By working through the system, a greater degree of benefit can be attained.

D. Relief efforts should avoid upsetting longstanding economic arrangements. Often societies have their own unique financial or economic systems which have evolved to help families or communities in times of stress. These methods should be identified and efforts should be made to ensure that programs are either compatible with or do not disrupt these traditional systems.

E. Agencies should diversify economic approaches. Relief officials must be sure to develop a variety of approaches to providing housing and financial assistance to disaster victims. It should be remembered that within each society there ia a wide range of housing types and styles, and that persons within the same economic group will have different aspirations and financial capabilities. Thus, it is important to try and develop a "mix" of program approaches and financial mechanisms to assist the victims.

4. FINANCIAL STRATEGIES AND APPROACHES

The allocation of resources, especially money, is one of the most difficult choices that a program planner will face. It is impossible to describe all the choices that exist, but there are some basic financial concepts that it is helpful to know:

A. Funding Concepts

Funding concepts are used to extend the capabilities or resources of an agency, for example:

(1) Linking To Other Programs

The methods usually used are cost-sharing, pooling of resources, or contributing matching funds.

(2) Recoverable Funding

In recoverable funding, all or a portion of the funds distributed are returned to the program, usually for reinvestment in the program. The most common examples are the use of revolving loans and sales or subsidy schemes. Recoverable funding increases the number of people who can be served and extends the "service" of the cash originally committed.

(3) Maximization Of Buying Power

This refers to the practice of selectively spending money so that either the program's or the beneficiaries' financial power is extended. For example, if loans are determined to be a feasible option for certain economic groups, an agency can use its money to guarantee loans from local financial institutions to clients who normally would not be eligible, rather than using the agency's money to make the loan. In this manner, an amount of perhaps $100,000 could be used to guarantee up to $1,000,000 or more in loans, thus increasing tenfold the buying power or the money the agency has on hand.

(4) Multiple Objective Planning

In multiple objective planning, expenditures are targeted so that more than one objective is reached with each disbursement. The objective is to place money in the community in such a way that the majority of the funds will stay in the community or at least pass through several hands before leaving. A sample scenario: a work project is established to repair a road damaged by the disaster. The workers are paid in cash and/or coupons redeemable in local markets. The workers spend the money to buy subsidized building materials distributed through the market system, which in turn increases the amount of material available to the victims and stimulates recovery of the material supplier.

B. Financial Balance

A second set of concepts describes some guiding principles for financial balance in a program:

(1) Loan-to-Grant Ratio

In establishing a mixed approach for funding housing programs, the financial capabilities of each sector of the community should be reviewed. For the purposes of program planning, it has been estimated by INTERTECT that the loan-to-grant ratio for simple housing programs is approximately 80% to 20%. For more comprehensive programs, a suggested balance of funding is 40% subsidies, 50% loans, and 10% grants.

(2) Balance Between Family And Community Assistance

When planning a housing program, it should be remembered that funds should not only be dedicated to assisting families, but a portion of the total budget should go into community assistance. As a rule of thumb, INTERTECT has estimated that approximately 1/4 to 1/3 of project funds should be used for labor-intensive community projects. The use of labor-intensive projects where people are paid in cash will provide additional money to disaster victims at the lowest economic level, so that they will be able to more fully participate in housing reconstruction activities.

5. PEOPLE AND ORGANIZATIONS

In disaster assistance, there are three sets of organizations that form the post-disaster economy. They are financial institutions, material suppliers, and the labor market.

A. Financial Institutions

Financial institutions can be classified as either formal or informal. Formal institutions are further divided into internal organizations (or those which exist within the country) and external organizations (those which are based outside but provide assistance in a disaster). Internal financial institutions include:

(1) National housing banks

(2) Private banks within the country

(3) Savings and loan associations

(4) Credit unions

(5) Cooperatives

(6) Insurance companies

External formal groups include:

(1) Aid organizations

(2) Voluntary agencies

(3) The development or relief agencies of foreign governments

(4) The World Bank

(5) Regional development banks (e.g., Inter-American Development Bank)

Informal organizations often supply the bulk of funds for low-income families following disasters. Informal organizations can include the family, the extended family, or a patron. Countries that have a high proportion of first-generation immigrants living in Europe or the United States may expect to receive substantial sums from relatives abroad following a disaster and these funds can be a major resource for reconstruction activities.

For the most part, internal formal financial institutions are limited in the amount of funds which they can supply to individuals or families following a disaster. Priority will go to previous borrowers and to institutions in the business and commercial sector. At the lower end of the scale, the savings and loans associations, credit unions and co-ops normally only lend to their own members. Foreign institutions may extend funds to the next tier of people who are not served by the internal institutions, or provide funds to the internal institutions, or provide funds to internal groups to extend their range of services to include those who would not otherwise be eligible.

B. Material Suppliers

Suppliers of reconstruction and recovery materials comprise the next segment of the post-disaster economy. A unique aspect of disasters in the LDC's is that large quantities of materials are often supplied from outside the country. Examples of external suppliers are voluntary agencies, commercial companies and foreign government assistance agencies. These external suppliers compete with the local market, often causing inflation and distribution and supply problems. It is this sector of the economy where inflation and distribution problems are usually amplified. Yet this sector receives the least amount of attention in most aid programs.

C. Labor

The labor market is an important sector to be considered in a post-disaster economy. In housing, the key group is the building tradesmen, especially carpenters and masons. Following most disasters, there is a tremendous demand for their services and the amount of money they receive in wages may increase substantially. For example, in Guatemala prior to the 1976 earthquake, skilled masons earned an average wage equivalent to three U.S. dollars per day. Following the earthquake the same worker could expect to receive a salary of between $8 and $12 per day, especially if he went to the capital city where his services were in great demand. For relief programs, the cost of labor is a factor which should be considered carefully in project planning, and measures should be taken where possible not to contribute to the inflationary spiral of increased wage demands. In rural areas, increasing wage scales offered by the commercial sector may deplete the labor force on hand for small-scale or rural housing programs, and agencies may be faced with having to use second-class tradesmen or to rely extensively on volunteer or self-help labor.

6. ROLES FOR RELIEF AGENCIES

Appropriate economic roles for relief agencies in housing reconstruction are:

A. To Assist In Controlling Prices

This can be done by:

(1) Bringing relief agencies together and working out common economic strategies for dealing with rising prices.

(2) Monitoring local markets and encouraging programs to take countermeasures (such as distribution of subsidized materials) in communities where inflation is beginning to get out of hand.

(3) Encouraging the government and foreign voluntary agencies to seek creative methods for working through the local markets where possible to control prices.

B. To Develop Financial Schemes For Providing Economic Assistance To Those Not Covered By Other Sources Of Financial Aid

Approaches include direct methods such as encouraging the host government to develop loan and grant mechanisms to serve these people, encouraging voluntary agencies to develop such programs, or establishing "operational" programs to help balance the overall financial assistance being offered in the affected community. Indirect roles include such activities as guaranteeing loans to persons not otherwise qualified for assistance from existing institutions.

C. To Monitor Economic Trends

An important function often neglected in disasters is the assessment of the economy and identification of weak sectors. Often a foreign aid agency can identify these sectors and respond to the needs more quickly than the local government. An appropriate role for relief agencies is to monitor the situation and either develop programs to meet the needs in a specific sector or direct the resources of other aid agencies to those communities.

D. To Encourage The Establishment Of Uniform Economic Approaches Among All Assisting Agencies

After a major disaster, numerous organizations can be expected to initiate a wide variety of assistance programs. Often, agencies working in adjacent communities will be offering two different types of financial packages. For example, one agency may be distributing free building materials, while in the next community, the agency is providing the same type of materials at a subsidized price. These differing schemes often cause resentment and bitterness and usually serve to prolong rather than shorten recovery. It has been found that uniform distribution is a more important consideration than whether the materials are given away or sold.

7. LESSONS LEARNED

A. A wide range of economic approaches confuses those receiving help and can lead to bitterness. Uniform reconstruction policies relating to the financing arrangements can help to resolve this problem.

B. Post-disaster inflation can be controlled if the signs of spiraling inflation are recognized early and adequate measures are established quickly. Informal measures and strategic intervention can be effective if carefully planned.

C. A mix of economic programs will best serve the disaster victims.

D. Financing mechanisms should be based on a reasonable expectation of rising costs in the housing sector.

E. There is usually more money in an affected community or available to disaster victims than is generally recognized by relief agencies.

F. The availability of excess cash to devote to housing reconstruction may be dependent upon seasonal factors (such as the harvest season) or other priorities of the disaster victim (for example, restoration of economic endeavors). Thus, housing reconstruction programs should be timed to coincide with a period when the potential homeowner will have accumulated enough excess capital to devote to his housing needs or the housing finance scheme may have to delay repayment until this capital has been acquired.

8. FURTHER REFERENCES

Gersony, R., Jackson, T., Froman, J., "A Contrastive Analysis of Alternative Reconstruction Models After the February 1976 Guatemalan Earthquake", Guatemala: A.I.D. Disaster Relief Program Reports on Post-Earthquake Distribution of Building Materials, Agency for International Development, Washington, D.C., 1977.

Taylor, Alan L., "The U.S.A.I.D./Guatemala Lamina and Housing Materials Distribution Program: Ex-Post Evaluation Report", Guatemala: A.I.D. Disaster Relief Program Reports on Post-Earthquake Distribution of Building Materials, Agency for International Development, Washington, D.C., 1977.

INTERTECT, The OXFAM/World Neighbors Housing Reconstruction Program: Guatemala 1976-77, INTERTECT, Dallas, Texas, 1977, pp. 53-62.

Thompson, Paul, Thompson, Charlotte, Evaluation of the Activities of the OXFAM/World Neighbors Post-Disaster Housing Program, Guatemala: February, 1976 - March 1977, INTERTECT, Dallas, Texas, 1977.

Department of Economic and Social Affairs, Financing Rural Housing: Selected Policies and Techniques for Developing Countries, United Nations, New York, 1974.

Economic Commission for Africa, "Methods of Cost Assessment in Low-Cost Housing", United Nations Economic and Social Council, New York, June 1969.

"Some Socioeconomic Implications of International Relief: The Disaster Boom Economy in North-Central Peru" (author unknown; draft for publication consideration by Human Organization, 1979).

Office of International Affairs, Housing Finance Institutions Abroad: A Directory, U.S. Department of Housing & Urban Development, Washington, D.C., September 1979.