FINMARK TRUST

MAKING FINANCIAL MARKETS WORK FOR THE POOR

ACCESS TO HOUSING FINANCE IN AFRICA: EXPLORING THE ISSUES

No. 9

ETHIOPIA

Overview of the housing finance sector in Ethiopia, commissioned by the FinMark Trust with support from

Habitat for Humanity®

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BACKGROUND TO THE SERIES

Since 2002, the FinMark Trust has been pursuing its mission, "Making Financial Markets Work for the Poor", first in the Southern African Customs Union (SACU) countries and now throughout Africa. An independent trust with core funding from the UK Department for International Development (DFID), FinMark Trust aims to promote and support policy and institutional development towards the objective of increasing access to financial services by the un- and under-banked in Africa.

A key product developed by the FinMark Trust is FinScope™, a national-level survey of individual usage of financial services, now being undertaken in eleven African countries.[1] FinScope™ will provide baseline data to stimulate policy change and support innovation by commercial providers seeking to deliver products and services sustainably to consumers who are currently outside the formal financial system. FinMark Trust will use the data of FinScope™ to promote and support change processes across the continent.[2]

FinMark Trust's Housing Finance theme area[3] conducts research and engages with sector stakeholders in the promotion of innovative housing finance mechanisms to enhance access to housing finance for the poor. Broadly, the housing finance theme's activities can be separated into the following categories:

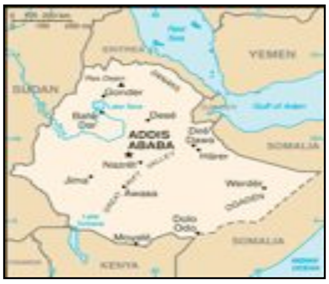
- Understanding the housing asset
- Exploring housing finance innovation
- Understanding issues relating to housing finance in Africa

This report is the ninth of a series of studies which will explore access to housing finance in various African countries (earlier reports consider housing finance sectors in Zambia, Botswana, Kenya, Uganda, Namibia, Rwanda, Mozambique and Malawi). It is meant as an input into a larger debate about how to enhance access to housing poor by low and moderate income earners throughout Africa. Comments and contributions can be sent to the FinMark Trust's Housing Finance Theme Champion, Kecia Rust on Kecia@iafrica.com.

The FinMark Trust hopes that its research into access to housing finance in Africa will begin to shed some light on the key issues facing the poor as they seek to mobilise the finance necessary to access adequate and affordable housing.

Country Profile: Ethiopia[4]

- **Population:** 83.1 million (UN, 2007)
- **Capital:** Addis Ababa / **Area:** 1.13 sq km (437 794 sq miles)
- **Major languages:** Amharic, Oromo, Tigrinya, Somali
- **Major religion:** Christianity, Islam
- **Monetary unit:** 1 Birr = 100 cents / 1 Euro = 15.24 Birr; 1 US$ = 9.75 Birr
- **GNI per capita:** US $160 (World Bank, 2006)
- **Main exports:** tobacco 53%, tea, sugar, cotton, coffee, peanuts, wood products, apparel



[1] FinScope™ is a nationally representative study of consumers' perceptions on financial services and issues, which creates insight to how consumers source their income and manage their financial lives. The sample covers the entire adult population, rich and poor, urban and rural, in order to create a segmentation, or continuum, of the entire market and to lend perspective to the various market segments. FinScope™ explores consumers' usage of informal as well as formal products and builds a picture of the role that the informal sector can play in the financial markets of developing countries. Since FinScope™ is a perceptual study, it also encompasses attitudes, behaviours, quality of life factors and consumption patterns. See www.finscope.co.za

[2] By 2012 it is intended that some 20 countries in Africa will have the survey. Repeat studies will take place on 2-3 year cycles, enabling trends within countries to be monitored and providing the basis for cross-country comparison especially around access to finance. FinScope™ data will provide financial service providers and regional integration initiatives with comparable, standard and reliable data about demand for financial services across borders. (FinScope™ Africa Brochure)

[3] To go to the housing finance theme page, go to www.finmark.org.za, click on "themes" and then click on "housing finance". The theme has been renamed the Centre for Affordable Housing Finance in Africa, a division of the FinMark Trust.

[4] From FinScope™ website, drawing on the World Bank Fact Book and CIA.

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- Ato Zewdu, Head, Branch Operations, Construction and Business Bank (CBB), Addis Ababa, Ethiopia.

Exploring housing finance in ETHIOPIA

This study into housing finance in Ethiopia has been commissioned by FinMark Trust of South Africa, and partly funded by Habitat for Humanity. It is one in a series of studies covering East and Southern Africa with the aim of documenting the current status quo on housing finance and making recommendations on how interested organisations can intervene to improve the flow of finance, particularly targeting lower income households. This report was commissioned as a short desk-research study. However there was limited published material on the housing and more particularly the housing finance sector in Ethiopia, meaning the content was enriched with additional face-to-face interviews with some stakeholders.

Ethiopia's growing population and rapid rate of urbanization is placing substantial pressure on housing, especially amongst the lower income population. The challenges for lower income households to acquire their own home are twofold; lack of affordable, good quality housing stock and the difficulty of obtaining housing finance. During Ethiopia's military dictatorship land and housing were nationalised. Financial markets did not exist. Emerging from this past and establishing a market economy has taken time. Meanwhile the rents of existing state-owned housing have been very low and the stock has been allowed to deteriorate. To address this, the Government has launched an ambitious subsidised housing programme to replace the older state-owned housing by modern multi-storey flats. While the speed of production of these units is remarkable, and they contribute to the development of SMEs and employment generally, there are questions as to whether the programme addresses the needs of the poor.

In the field of housing finance, only one bank has a mortgage book of any size. Its interest rates are far below the rate of inflation, but it was capitalised by substantial World Bank (IDA) loan, so does not require to raise funds from savings or the market – both of which are very difficult in current market conditions. There is a rapidly growing micro-finance industry in Ethiopia. At present, it does not explicitly serve housing, but there is a likelihood that its loans are used for small scale, incremental housing construction.

Comments, challenges and perspectives to this report are welcome. These should be directed to the FinMark Trust's Housing Finance Theme Champion, Kecia Rust, by email to Kecia@iafrica.com, or on +27-83-785-4964.

Key findings from the study

- Housing finance penetration among the middle and low income categories is insufficient to meet their housing needs. Affordability is a key issue and generally, low incomes coupled by un-affordable housing products on the market has limited the ability to access finance. There is a need for greater innovation both in the supply of more affordable housing as well as finance products.
- Government subsidised housing and land supply often fails to benefit the intended beneficiaries, and is instead taken advantage of by more privileged groups. There is a need to reconsider the targeting mechanisms for these programs to ensure that they benefit the people intended.
- Creation of an efficient and accurate system of land registration and cadastre is required for housing finance systems such as mortgage, to work. This is because these finance systems heavily rely on the proper functioning of land registrations systems, where title is clear and secure.
- The land registration system, including the permit and lease system, also imposes considerable curbs on holding and transacting in land. The rationale and effect of these curbs should be re-visited, especially because of the effect they have on supply of land for housing, the expansion of the mortgage market and the incentive to develop and improve housing by land owners.

- The financial markets in Ethiopia are undeveloped. This among others limits the development of a large mortgage industry in the country. There is a need to nurture capital market formation for greater financing options in the long run.
- Government activity and regulations in the housing finance sector have often been stifling to private sector activity. Restrictions to the entry of foreign retail financial service providers has limited the number of players and constrained supply. Interest rate controls have also discouraged greater lending. Heavy government borrowing from the private sector has also discouraged private sector lenders from lending to the general public. To encourage a more diverse and better supply of housing finance products, there is a need to create a conducive environment for their establishment and growth of private players. Government's role should thus only be retained for carefully thought out prioritised and strategic interventions. Land price controls which have likewise had a negative effect on mortgage funding need also be revisited.
- The growth of microfinance lending in recent years is encouraging, especially given that there is some limited evidence that lending has been channelled to house building. Deliberate efforts to stimulate greater housing microfinance lending should be made, by the government, through conducive financial and land regulatory regimes, and by the non-government and private sector, by exploring suitable products. .
- There needs to be an effort to train more people skilled in professions directly linked to land such as land surveyors, economists and valuers.
- Upgrading of existing settlements especially Kebele housing should be prioritised given the poor living conditions of this large number of people.

Acronyms and Abbreviations

AARH	Agency for the administration of rented houses
ORMAP	Office for the Revision of the Master Plan of Addis Ababa
BNLS	Botswana, Namibia, Lesotho and Swaziland
CBB	Construction and Business Bank
CBE	Commercial Bank of Ethiopia
DfID	Department for International Development (UK)
HDPO	Housing Development Project Office
HSB	Housings and Savings Bank
IHDP	Integrated housing development program
NBE	National Bank of Ethiopia
NEERI	Nominal Exchange Rate Index
NUPI	National Urban Planning Institute
REERI	Real Effective Exchange Rate Index
SACU	South African Custom Union
UN-ECA	United Nations Economic Commission for Africa

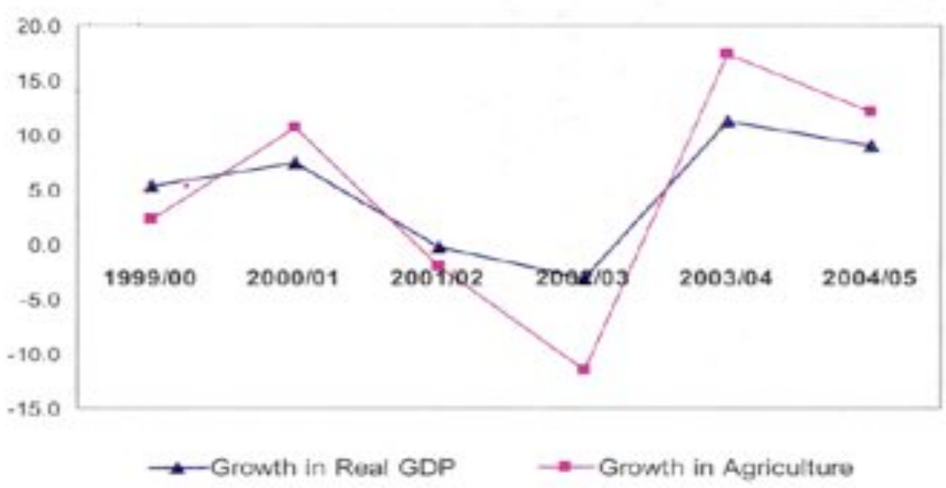
Overview of Ethiopia's macro-economy

Soon after it emerged from a turbulent military dictatorship after nearly two decades, Ethiopia began the 1990s by taking measures to reverse the socio-economic crisis of the 1980s wrought by the policies of the former Derg (Military) regime. The main focus of the reform programmes was to change the previous state-led command economy, as structured by the Military regime, to one of a market-oriented economy. In addition, the role of the government was also changed to that of a facilitator of economic growth by creating a conducive legal, institutional and policy environment to enhance private sector development.

Since the beginning of the 1990s, the Government of Ethiopia (GoE) has taken a number of measures to encourage the private sector to actively participate in economic growth. Accordingly, prices and markets for goods have been liberalized; the labour market has been deregulated; the exchange rate has been partially market-based; restrictions on imports have been somewhat eased; and tariffs on selected commodities have been reduced. Most of the formerly state-owned enterprises have been sold off to domestic and foreign private investors, which process continues slowly as they decrease. (Ethiopian Government, Press, Information and Documentation General Directorate, 2002/03).

GDP Growth

Fig 1: Growth in GDP and Agriculture



Source: Ministry of Finance and Economic Development

Between 2004/05 and 2005/06, the Ethiopian economy was characterized by relatively high real GDP growth and monetary stability. In 2003/4, GDP grew by 11.1 per cent, followed by 8.9 per cent in 2004/05 and by 9.6 per cent in 2005/06. This sustained growth placed Ethiopia among the top performing economies in sub-Saharan Africa. In 2005/06, the main contributors to the improved GDP performance included agriculture with a 12 per cent increase in output; while industry and services grew by 6.6 per cent and 5.8 per cent respectively.

Table 1: Sectoral Contribution to GDP and Growth

Items		Year					
		1999/00	2000/01	2001/02	2002/03	2003/04	2004/05
GDP at Constant Basic Prices		59,575	63,973	63,756	61,654	68,472	74,506
Sector	Agriculture & Allied Activities	28,595	31,626	30,950	27,361	32,100	35,948
	Industry	7,457	7,817	8,213	8,665	9,254	9,865
	Services	24,197	25,122	24,997	26,096	27,614	29,221
Growth in Real GDP		5.4	7.4	-0.3	-3.3	11.1	8.8
Real GDP per capita		951.9	993.1	961.9	904.4	976.8	1034.0
Share in GDP (in %)	Agriculture & Allied Activities	44	45	49	44	47	48
	Industry	13	12	13	14	14	13
	Services	41	39	39	42	40	39
Growth in Real GDP per capita		2.3	4.3	-3.1	-6.0	8	5.9
Agriculture & Allied Activities	Absolute Growth	2.2	10.6	-2.1	-11.6	17.3	12.0
	Contribution to GDP growth	1.0	4.8	-1.0	-5.1	8.1	5.8
	Contribution in %	17.8	64.8	306.1	156.1	73.4	65.6
Industry	Absolute Growth	1.8	4.8	5.1	5.5	6.8	6.6
	Contribution to GDP growth	0.2	0.6	0.7	0.8	0.9	0.9
	Contribution in %	4.2	8.0	-192.5	-23.5	8.3	9.9
Services	Absolute Growth	9.5	3.8	-0.5	4.4	5.8	5.8
	Contribution to GDP growth	3.9	1.5	-0.2	1.9	2.3	2.3
	Contribution in %	71.5	20.3	57.6	-56.4	21.2	25.9

Source: Ministry of Finance and Economic Development (MoFED)

The Ethiopian economy grew by 10 per cent in 2006/07 – the fastest of any non-oil producer in sub-Saharan Africa that year. A contributory factor was a significant foreign investment inflow, particularly from China and India. Returnees from the United States and Europe have also been investing in hotels, bars, shops and restaurants and the real estate markets. For some years now, there has also been a significant expansion of the construction sector in Addis Ababa and the major regional capital cities. High-rise buildings are being developed by the fast-expanding services sector including restaurants, supermarkets, shops and offices.

Government Expenditure

The present government, since coming to power in the early 1990s, has given priority to pro-poor programmes, both at the national and sub-national levels. Comparisons with other African countries for which data are available show that Ethiopia is on the top list when it comes to pro-poor expenditures. This trend has been gaining momentum since 1999/2000. The 2004/05 budget featured a substantial absolute increase in pro-poor spending, at 18.3 per cent of Gross Domestic Product (GDP). Further increases are revealed as indicated in the Macro Economic Fiscal Framework (MEFF) (2005/06 to 2007/08) which foresees poverty-targeted spending rising from 61 per cent in the fiscal year 2004/05 to 71 per cent by the fiscal year 2007/08.

The government budget in the fiscal year 2004/2005 was $2.52 billion. This was 20 per cent higher than the previous year. During the same period, recurrent expenditure reached $1.34 billion and showed a 9 per cent increase over the last fiscal year. Yet, its share of the total expenditure stood at 53 per cent compared to 58 per cent the previous year. Capital expenditure in that year was budgeted at $1.2 billion, a 37.3 per cent increase over the previous year.

Fig 2: Trends in General Government Expenditure by Component

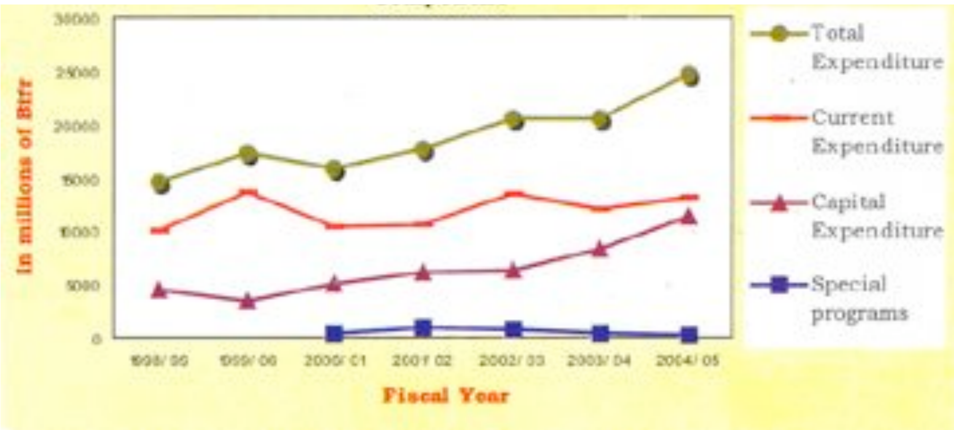


Table 2: Summary of General Government Expenditure 2003 – 2005

Particulars	2003/04 [A] Pre. Act	2004/05 [B] Revised Budget	[C] Pre.Act	Percentage Change [C/A]	Performance Rate [C/B]
Total Expenditure	**20,504.00**	**28,712.00**	**24,617.00**	**20.1**	**85.7**
1.Recurrent Expenditure	**11,961.00**	**14,531.00**	**13,036.00**	**9.0**	**89.7**
General Services	5,048.00	5,554.00	5,767.00	14.2	103.8
Economic Services	1,35600	1,618.00	1,468.00	8.3	90.7
Social Services	3,253.00	3,908.00	3,775.00	16.0	96.6
Interest and charges	1,080.00	1,567.00	1,011.00	-6.4	64.5
External Assistance	699	901	721	3.1	80.0
Social Safety Net	0	0	0		
Others	525	983	294	-44.0	29.9
2.Capital Expenditure	**8,271.00**	**13,414.00**	**11,357.00**	**37.3**	**84.7**
Economic Development	4,773.50	8,265.90	7,585.30	58.9	91.8
Social development	2,232.50	4,609.00	3,319.90	48.7	72.0
General services	1265.3	538.9	451.8	-64.3	83.8
Compensation Payments	0	0	0		
External Assistance2	1047.2			-100.0	
3. Special programs	**272.0**	**767.0**	**224.0**	**-17.6**	**29.2**

Annual Price Developments/ Inflation

Until comparatively recently, Ethiopia had one of the lowest rates of inflation country in sub-Saharan Africa. This was due to several reasons: a strong currency, prudent monetary and fiscal policies (1960s-1973); and a ration-based economy and general price control under the Military regime (1974-1992). Implementation of economic reform and stabilization programmes (1992-2004) also helped this process.

The country's track record in low-inflation started to unravel in 2002/03 when prices rose at a significant pace, reaching 15.1 per cent per year by the end of the year. However, the rate slowed down the following year to 7.7 per cent.

Table 3: Percentage change in Annual Average Inflation Rates — 2002 – 2005

Category	2002/03	2003/04	2004/05
Items	A	B	C
General	15.1	8.6	6.8
Food	24.8	11.8	7.7
Non-food	0.5	2.8	5.2

Source: Central Statistical Agency (CSA) and National Bank of Ethiopia (NBE)

In 2005/06 there was a further steep rise with respect to consumer prices when the general inflation rate exhibited a significant rise to 12.3 per cent. In 2007/2008, according to the Central Statistical Agency, the rate rose to a record 30 per cent, threatening the Ethiopian economy. The increase was mainly led by food price inflation. According to the World Bank, at the time of writing, the rate had reached 50 per cent—quite unprecedented in Ethiopia's recent economic history.

Exchange Rate

In recent years, there has been a steady depreciation of the Ethiopian Birr against major currencies, typically the U.S. Dollar and the Euro. For example, the real effective exchange rate (REER) depreciated by 3.29 per cent and 4.85 per cent in 2002/03 and 2003/04 respectively. The depreciation of the REER between 2002/03-2003/04 could be explained by the gain in competitiveness stemming from Nominal Effective Exchange Rate (NEER) depreciation, which more than offset the relative rise of domestic inflation. This resulted in the improvement of the external competitiveness of the country – one indicator of which was a significant increase in total exports.

Table 4: Trends in the Real and Nominal Effective Exchange Rate

Year	REERI	NEERI
1999/00	93.6	95.5
2000/01	87.9	98.7
2001/02	85.3	103.1
2002/03	97.4	96.5
2003/04	99.0	92.0
2004/05	94.2	85.2

Source: National Bank of Ethiopia, Addis Ababa, 2004/05
Note: An increase in REERI and NEERI indicates appreciation and vice-versa. (REERI=Real Effective Exchange Rate Index / NEERI=Nominal Exchange Rate Index)

During the last ten years the Birr has been falling steadily, albeit at a slow rate, against the US Dollar. For example, the auction average marginal exchange rate of Birr to the US Dollar rose from a high of Birr 5.77 in the 1993/1994 fiscal years to Birr 8.62 in 2003/2004 fiscal year. In 2007/08, this figure reached a low of 9.75 Birr against the U.S. Dollar.

External Debt

Ethiopia is classified as a heavily indebted country. At the end of the 2004/05 fiscal year, the country's external debt stood at $6,021 million. Of this, about 81 per cent was owed to multilateral creditors, 13 per cent to bilateral creditors and the remaining 6 per cent to commercial lenders.

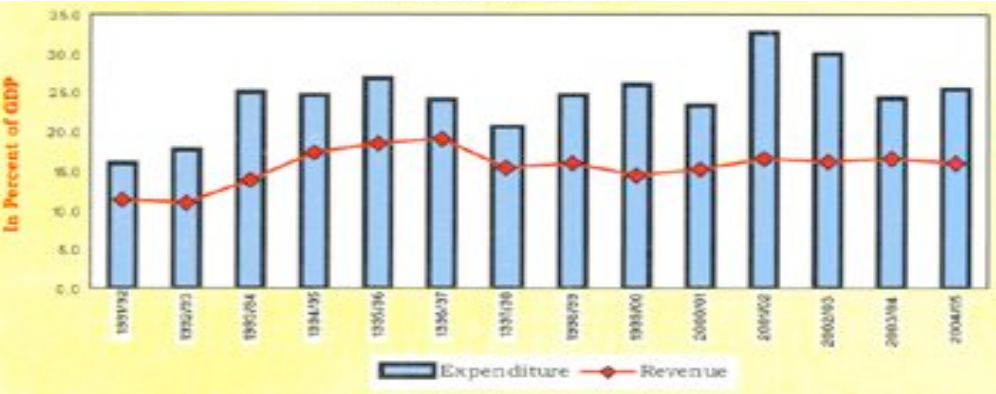
According to data from the National Bank of Ethiopia (NBE), the ratio of external debt service to receipts from export of goods and non-factor services has steadily declined between 2002/03-2004/05. It was 9.9 per cent in 2004/05. Similarly, total debt to GDPI ratio dropped from 73.5 per cent in 2003/04 to 53.8 per cent in 2004/05. At the same time, the ratio of external debt to exports of goods declined to 3.2 per cent in 2004/05 from 5.9 per cent in 2002/03.

Balance of Payments

The balance of payments situation for the country has been sharply deteriorating over the past 2-3 years. In 2004/2005 there was a deficit of $101.4 million in contrast to a surplus of $226.7 and $306.5 million in 2002/02 and 2003/04 respectively. One important factor that exacerbated the situation was said to be a recorded deficit in the merchandise trade. In 2004/05, the merchandise trade deficit widened to $2815.9 million (25.2 per cent of GDP) from $1373.3 million (20.7 per cent of GDP) in 2002/03 and $1987.5 million (24.7 per cent of GDP) in 2003/04. This dramatic deterioration was caused by a surge in imports which was not accompanied by a comparable increase in exports. The widening of the merchandise trade deficit led to considerable deficit in the current account – which more than doubled in 2004/05 and reaching $1,013.6 million (11.4 per cent of GDP) against a deficit of $501.7 million (6.2 per cent of GDP) in 2003/04.

In recent years remittances from citizens working abroad have been increasing steadily and were reported to be $53 million or about $1 per capita and accounted for approximately 0.8per cent of GDP (2000). In 2007/08, they were reported to have reached the 1 billion $mark and thus have become a significant source of foreign exchange earnings. Foreign aid receipts amounted to about $16 per capita and accounted for approximately 17per cent of the gross national income (GNI).

Fig 3: Trends in General Government Expenditure and Revenue (per cent of GDP)



Deficit Financing

Deficit financing has become a major feature of Ethiopian government expenditure. Because of a 20.1 per cent increase in the government's budgetary expenditure (well above the 10.9 per cent increase in revenue and grants) a record deficit was registered in 2004/05. A significant portion about 74 per cent of the deficit was financed from domestic borrowing, followed by external and non-bank borrowing. Figure 3 illustrates the trends.

Table 5: Balance of Payments

Particulars	2002/03	2003/04	2004/05	Percentage change	
	A	B	C	C/B	C/A
Trade Balance	**-1373.29**	**-1985.68**	**-2815.91**	**41.81**	**105.5**
Exports	482.71	600.45	817.91	36.22	69.44
Imports	1856.00	2586.13	3633.25	40.49	95.76
Net Services	**121.91**	**246.17**	**241.57**	**-1.87**	**98.15**
Travel	39.09	100.62	114.06	13.35	191.78
Transportation	83.30	57.30	70.73	23.43	-15.09
Government (n.i.e.)	117.08	173.81	176.88	1.77	51.08
Investment income	-46.51	-63.58	-35.79	-43.71	-23.06
Interest Cash(net)	-34.98	-38.94	-14.03	-63.97	-59.89
Arrears	-7.32	-11.07	12.48	-212.75	-270.46
Relief Dividend	-0.50	0.00	0.00		-100.00
Other Services	-27.15	-27.87	-26.51	-4.85	-2.36
	-11.53	-24.64	-21.76	-11.70	88.67
	-71.04	-21.99	-84.32	283.43	18.69
Private Transfers	**494.89**	**671.32**	**810.95**	**20.80**	**63.87**
Current Account Balance(excl. public transfers)	**-765.49**	**-1068.19**	**-1763.39**	**65.08**	**133.10**
Public transfers	**599.80**	**566.53**	**749.77**	**32.35**	**25.00**
Current Account Balance (incl. public transfers)	**-156.69**	**-501.66**	**-1013.61**	**102.05**	**546.88**
Non-monetary Capital	**400.04**	**512.44**	**585.09**	**14.18**	**46.26**
Long-term (net)	336.81	388.36	440.61	13.45	30.82
Disbursements	561.13	510.67	570.83	11.78	1.73
Repayments	224.32	122.30	130.22	6.47	-41.95
Cash	136.51	68.69	72.92	6.16	-46.58
Arrears	0.33	0.00	0.00		-100.00
Relief	87.48	53.61	57.29	6.86	-34.51
Direct Investment(Net)	123.31	150.00	150.00	0.00	21.64
Short-term(net)	-60.09	-25.92	-5.52	-78.70	-90.81
Net Errors& Omissions	**63.17**	**215.93**	**327.1**	**51.51**	**417.91**

Overall Balance	**306.51**	**226.71**	**-101.37**	**-144.71**	**-133.07**
Financing	**-306.51**	**-226.71**	**101.37**	**-144.71**	**-133.07**
Reserves(- = increase)	**- 376.52**	**-308.19**	**17.57**	**-105.70**	**-104.67**
NEB net foreign asset	**-290.11**	**-333.58**	**-52.80**	**-84.17**	**-81.80**
CBE net foreign asset	**-84.26**	**25.39**	**70.37**	**177.17**	**-183.51**
Arrears	**0.83**	**0.00**	**0.00**		**-100.00**
Principal	0.33	0.00	0.00		-100.00
Interest	0.50	0.00	0.00		-100.00
Debt Relief	**69.18**	**81.48**	**83.81**	**2.86**	**21.15**
Principal	42.07	53.61	57.29	**6.86**	**36.17**
Interest	27.19	27.87	26.51	-4.85	-2.50

Changes in Reserve Position

Between 2002 – 2004 fiscal period, Ethiopia increased its reserves. However, in 2004/05 there was a sudden deterioration and as a result net reserves fell by $17.6 million. This was mainly caused by a decline of the commercial banks' reserves of $70.4. This can be partially explained by their effort to finance import demands from their own reserves. In 2005, the National Bank of Ethiopia built up its reserve by an additional $52 million and this positively contributed to the gross reserve of the country which as of July 7, 2005 was sufficient to cover 3.6 months of imports of goods and non-factor services of the coming year.

Capital Expenditure

Ethiopia has seen continued economic expansion as manifested in a significant increase in investment in various sectors. For example, in the last quarter of 2005/06 a total of 1,357 investment projects were approved. This was an increase of 26 per cent over the same period in 2004/05 when 1,076 projects were approved by the Government. The projected capital outlays of the approved projects amounted to $1,203 million, $2,393 million and $1,130 million in the third and second quarter of the year 2005/06 as well as the third quarter of the year 2004/05, respectively. It was also projected that 98,581 permanent and temporary jobs would be created once these projects became operational.

Commercial and residential construction accounted for 41 per cent of the total investment in 2005/06. Investments in the services sector, agriculture, and hunting and forestry sectors accounted for 24 per cent, 13 per cent and 12 per cent respectively. On the other hand, in terms of their investment capital share, manufacturing; real estate; and construction sectors accounted for 43 per cent, 18 per cent and 15 per cent of the total investment capital. No data were available to indicate the proportion of investment that went into housing due to the fact that there is no separate tracking of residential construction in Ethiopia.

Financial Sector

Finance Sector Regulatory Framework

The National Bank of Ethiopia (NBE) is responsible for regulating the banking and insurance business in Ethiopia. In light of the rapid growth of the financial sector in the 1990s, the Government issued the Monetary and Banking Proclamation No. 83/1994 to enhance the autonomy of the NBE as the nation's central bank and gave the bank added powers to supervise banks and insurance companies. In addition, Proclamation No. 84/1994 was issued to streamline the licensing and supervision of banks and insurance companies by the central bank. It also sets out guidelines for the establishment of private financial institutions. These Proclamations were meant to facilitate the growth of the banking and insurance industries, monitor the quantity and quality of their assets and liabilities, and control the expansion and development of their networks.

In addition to its regulatory power over the formal banking and insurance industries, the National Bank of Ethiopia also has the authority to license and supervise microfinance institutions operating in the country. The regulations stipulate that to be licensed by the NBE, microfinance institutions must have a minimum paid-up capital of Birr 200,000 ($21,000 in 2008).

Financial Markets

Due to the socialist legacies of the previous Military dictatorship spanning nearly two decades (1974-1991), Ethiopia has very little experience in financial markets. To date, there is no established capital market in Ethiopia and no effective stock exchange where company shares and bonds are listed and traded. Instead, treasury bills continue to be the only active primary securities. Long-term securities such as bonds are not widely used and traded. However, government bonds are occasionally issued to finance government expenditure and/or to absorb excess liquidity in the banking system.

Treasury Bills

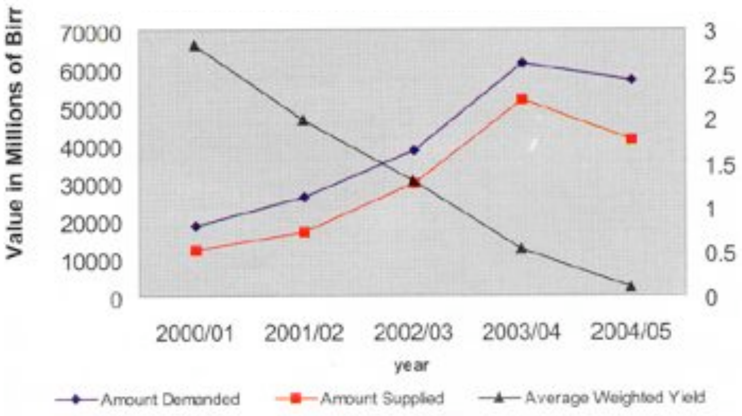
Data from 2004 – 2005 indicate that the total face value of T-bills floated at the bi-weekly T-bills auction market run by the NBE was $4,232 million. Commercial banks are the major institutional investors in T-bills which are risk and tax free. Of the total bills supplied, banks bought T-bills worth $3,875 million (or 92.0 per cent). At the end of the 2004/05 fiscal year, outstanding bills stood at $656 million of which banks held 78.1 per cent. The details are provided in Table 7 and Figure 5.

Table 6: Treasury Bills Auction Result (2002/03-2004/05) (*in $million*)

Particulars	2002/03 A	2003/04 B	2004/05 C	Percentage Change C/A	C/B
Number of Bidders	293.0	293.0	242.0	-17.4	-17.4
Amount Demanded	3,947	6,271	5,836	47.9	-6.9
28-day	919	2,439	3,143	242.1	28.9
91-day	2,140	2,883	1,768	-17.4	-38.7
182-day	887	950	925	4.2	-2.6
Amount supplied	3,043	5,297	4,232	39.1	-20.1
28-day	728	2,349	2,289	214.3	-2.6
91-day	1,766	2,364	1,339	-24.2	-43.3
182-day	549	584	605	10.2	3.5
Amount Sold	3,043	5,296	4,212	38.4	-20.5
Banks	2,756	4,915	3,875	40.6	-21.2
Non-banks	287	381	337	17.5	-11.6
Average weighted price for US$1 for successful Bids					
28-day	10.2	10.2	10.26	-0.001	0.019
91-day	10.3	10.3	10.24	0.340	0.089
182-day	10.2	10.2	10.28	1.095	0.364
Average weighted Yield on successful Bids (per cent)					
28-day	0.197	0.391	0.146.	-25.9	-62.7
91-day	1.440	0.425	0.086	-94.0	-79.9
182-day	2.246	0.785	0.054	-97.6	-93.1
Outstanding Bills at the end of the Period	933	1,280	656	-29.7	-48.8
Banks	830	1,171	512	-38.3	-56.3
Non-Banks	103	109	144	39.2	31.2

Source: National Bank of Ethiopia, staff computation

Fig 4: Treasury Bills Auction Result (2000/01 - 2004/05)



Government Bonds

In 2000, the governments auctioned bonds which matured and were redeemed in 2002. Later, government bonds were issued to the Commercial Bank of Ethiopia outside any formal auction. At the end of fiscal year 2004/05, the outstanding bond holding by banks amounted to $258 million while the non-bank public held $36 million. The Government is not transparent on the use of these bonds but it is safe to assume that they are probably being used to finance short-term government deficits. It appears also that banks have no problem purchasing these bonds because of their excess liquidity.

Inter-bank Money Market

Ethiopia introduced an inter-bank money market in September 1998. Since then, only 13 transactions have been effected in the market with an average inter-bank interest rate of 7.8 per cent. Only one transaction was conducted in the inter-bank money market in 2004/05; thus pointing to a sluggish inter-bank money market in the country. Persistent excess reserves in the banking system (particularly in the government-owned banks), and lack of collateral in the case of private banks, have mainly contributed to the low level of activity in the inter-bank money market in Ethiopia.

Table 7: Inter-bank Money Market Transactions – June 2003--2006/07

No	Borrower	Lender	Amount Borrowed (US$ 000s)	Internal Rate (%)	Date of Trans-action	Maturity Period
1	Nib Int. Bank	Awash Int. Bank	717,949	11	16/11/00	Overnight
2	Wegagen .Bank	Commercl. Bank of Eth.	1,025,641	8	3/01/01	5 Years
3	Nib Int. Bank	”	1,025,641	8	31/03/01	3 months
4	Wegagen Bank	”	1,025,641	8	22/03/01	1Year
5	Nib Int. Bank	”	369,230	8	31/05/01	6 months
6	Nib Int. Bank	”	369,231	8	30/06/01	6 months
7	Nib Int. Bank	”	82,051	8	30/11/01	6 months
8	Nib Int. Bank	Bank of Abyssinia	2,97	7	31/12/02	3.5months
9	Nib Int. Bank	Bank of Abyssinia	195	7	31/01/03	3.5months
10	Nib Int. Bank	Bank of Abyssinia	2,051,283	7	28/02/03	3.5months
11	Nib Int. Bank	Bank of Abyssinia	2,974,359	7	31/03/03	5.2months
12	Nib Int. Bank	Commercial Bank of Eth	2,564,102	7.5	07/07/03	5.2months
13	Nib Int. Bank	Bank of Abyssinia	2,051,283	7.5	26/3/05	Over draft
14	Nib Int. Bank	Bank of Abyssinia	2,051,283	7.5	26/3/05	Over draft
	Total/Average	-	22	7.8		

The Banking Sector

Traditionally, the banking and insurance sectors in Ethiopia have been dominated by the Government. This was particularly true under the Derg/Military Regime when the entire banking and insurance sectors were nationalized and placed under state control.

Following the change of regime in 1991, banking and insurance were opened up to private sector participation. However, by law they are restricted to Ethiopian nationals, and the country remains closed to foreign banks and insurance companies. This has generated a non-competitive financial market structure, and the economy has been insulated from the possible benefits of financial sector liberalization that has taken place in many other African countries.

Despite the restrictions to entry of foreign firms, the domestic banking sector has shown a steady expansion. Banks and insurance companies owned by Ethiopian nationals have been growing over the years. At the time of writing there were eleven banks with a total of 504 branches.

As of 2007/08, there were three state-owned banks, namely the Commercial Bank of Ethiopia, the Construction and Business Bank (CBB) and the Development Bank of Ethiopia (DBE). The largest government-owned bank is the Commercial Bank of Ethiopia with 196 branches and accounting for 47 per cent of the total capital and 39 percent of branches in the banking system. In 2007/08, the 8 private banks held 32 per cent of the total bank capital and had almost half the bank branches in the country. As noted later in this report, the Construction and Business Bank is the major bank providing mortgages to residential and commercial development.

Table 8: Capital and Branch Network of the Banking System at December 31, 2007
(Branch in Number and Capital in Million U.S $)

Banks	Branch Network 2007/08 Quarter I			Quarter II				Capital 2007/08	
	Regions	Total	per cent Share	Regions	Addis Ababa	Total	per cent Share	Quarter I	Quarter II
Public Banks									
Commercial Bank of Ethiopia	147	196	38.9	148	49	197	37.7	433	470
Construction & Business Bank	15	27	5.4	15	12	27	5.2	26	25
Development Bank of Ethiopia	31	32	6.3	31	1	32	6.1	191	192
Total Public Banks	193	255	50.6	194	62	256	49.0	650	687
Private Banks									
Awas International Bank	20	45	8.9	21	26	47	9.0	45	52
Dashen Bank	20	44	8.7	21	24	45	8.6	63	56
Abyssinia Bank	13	30	6.0	14	19	33	6.3	43	44
Wegagen Bank	22	39	7.7	22	17	39	7.5	41	45
United Bank	11	31	6.2	11	21	32	6.1	37	42
Nib International Bank	9	31	6.2	11	24	35	6.7	44	49
Cooperative Bank of Oromiya	15	17	3.4	17	2	19	3.6	13	14
Lion International Bank	7	12	2.4	11	5	16	3.1	14	15
Total Private Banks	**117**	**249**	**49.4**	**128**	**138**	**266**	**51.0**	**300**	**317**
Grand Total Banks	**310**	**504**	**100.0**	**322**	**200**	**522**	**100.0**	**950**	**1004**

Source: National Bank of Ethiopia Quarterly Bulletin, Second Quarter 2007/8

Table 9: Distribution and Share of the Banking Business in Ethiopia, 2006/07

Banks	Branches	per cent Share
Government Banks		
1. Commercial Bank of Ethiopia (CBE)	196	38.9
2. Development Bank of Ethiopia (DBE)	32	6.3
3. Construction and Business Bank (CBB)	27	5.4
Total Government Banks	225	50.6
Private Banks		
Awash International Bank (AIB)	45	8.9
Dashen Bank (DB)	44	8.7

Abyssinia Bank (AB)	30	6.0
Wegagen Bank (WB)	39	7.7
United Bank (UB)	31	6.2
Nib International Bank (NIB)	31	6.2
7. Cooperative Bank of Oromia (CBO)	17	3.4
8. Lion International Bank (LIB)	12	2.4
Total Private Banks	249	49.4
Grand Total Banks	**504**	**100**

Source: National Bank of Ethiopia, Quarterly Bulletin, 2007/08

In 2007/2008 there were 10 insurance companies, with 164 branches. The state-owned Ethiopian Insurance Corporation (EIC) had 36 branches (or 22 per cent) while the rest, i.e. 148 branches, were owned by the private sector. It can be observed that the private sector has made considerable progress in sharing the insurance market despite the fact that it was only allowed to enter the business a little more than 15 years ago.

Table 10: Branch Network and Capital of Insurance Companies 2007/08
(Branch in Number and Capital in millions U.S. $))

No.	Insurance Companies	Branch				Capital	
		Quarter I 2007/08	Quarter II 2007/08			2007/08	2007/08
		Total	A.A	Regions	Total	Quarter I	Quarter II
	Ethiopian Insurance	36	11	26	37	25	22
	Awash Insurance	18	11	8	19	47	45
	Africa Insurance	9	6	7	13	51	51
	National Insurance	12	7	5	12	11	13
	United Insurance	18	13	6	19	49	40
	Global Insurance	6	3	3	6	19	19
	Nile Insurance	18	10	9	19	67	41
	Nyala Insurance	16	8	8	16	58.	50
	Nib Insurance	15	10	5	15	31.	34
	Lion Insurance	0	5	3	8	15	14
TOTAL		**148**	**84**	**80**	**164**	**373**	**329**

Source: National Bank of Ethiopia Quarterly Bulletin, 2007/08

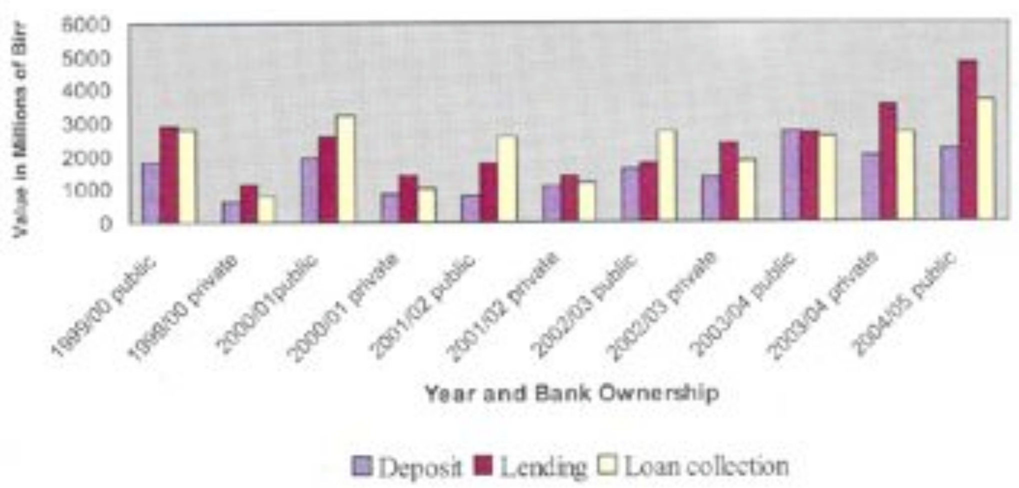
Credit Growth

In 2004/05, total loans granted by the banking system were Birr 9,433 million ($978 million), growth rates of 130 per cent and 51.9 per cent over the fiscal years 2002/03 and 2003/04 respectively. More than 73.0 per cent of the total loans were extended to the private sector while the rest went to government or quasi-government agencies (see Figure 3).

This increase in credit continued into 2004/05. During this period credit to the government sector increased by 12.9 per cent, while credit to the non-government sector went up 56.1 per cent. Out of the total loan that was given out in 2004/05, about 86 per cent was extended to the private sector. The main economic sectors to benefit from this credit included trade, agriculture, housing and construction. (NBE, 2005/06).

In 2005, international trade was the major beneficiary of bank credit (31.1 per cent) followed by domestic trade (20.2 percent). Agriculture and industry each took up 16.5 and 11.5 per cent respectively. The loans disbursed by private banks constituted 49.4 per cent of total lending in 2004/05 while the balance of about 50 per cent was provided by the government sector.

Fig. 5: Developments in Deposit Mobilization, Lending and Loan Collection Activities of Banks (1999/00-2004/5



Source: NBE 2004/2005

Table 11: Loans and Advances by Lender Banks -2003/04-2004/05 (in U.S. $ million)

Name of Bank	2003/04			2004/05					
	Disbursed	Collected	O/S	Disbursed	Collected	O/S	percentage change		
	B	C	D	E	F	G	E/B	F/C	G/D
Government Banks (3)	274	273	2590	490	375	2,204	78.4	37.6	-14.9
Private Banks (9)	363	264	651	478	358	781	31.8	35.5	19.9
Total	637	537	3,241	968	337	2,985	51.9	36.5	-7.9

Source: NBE, 2004/05

Outstanding Loans

Outstanding loans of the banking system stood at $298 million at the end of 2004/05. This represented a 7.9 per cent decline compared to the balance at the close in 2003/04 fiscal year. In the period 2003 – 2005, gross outstanding claims on central government declined by 47.5 per cent while that of public enterprises, private sector and co-operatives increased by 42.6, 17.5 and 110.6 per cent respectively. 79.9 per cent of the value of total outstanding loans was owed to public banks in 2003/2004: this proportion declined to 73.8 per cent in 2004/05. This trend clearly indicates that private banks are increasing their share and becoming more competitive in the banking business.

Licensing and Supervision of Microfinance Institutions (MFIs)

In recent years, micro-finance institutions (MFIs) have become increasingly important players. In 2004/05, there were 25 microfinance institutions of various sizes operating in the country. During the same year, their total assets were valued at $195 million. By the end of the year, MFIs had mobilized deposits and advanced loans amounting to $152 million.

By 2006/07, the number of micro-finance institutions has grown to 28 spread around the country, and their accumulated savings and total assets had grown to $3,639 million.

The National Bank of Ethiopia (NBE) is the authority which licenses and supervises microfinance institutions operating in Ethiopia. It has set regulations which have to be followed by all MFIs. To operate legally, microfinance institutions must be licensed with a required minimum paid-up capital. At the beginning, this amount was set fairly low in order to attract investors to the micro-banking sector.

Most microfinance institutions were started by non-governmental organizations. However, there has been a change in the law to the effect that microfinance institutions must now have at least five shareholders. As a result, mixed ownership of public and nongovernmental organizations as well as private shareholders has emerged.

Since micro-finance institutions are viewed as effective mechanisms for poverty reduction, the loan policy of MFIs lays down that preference should be given to poor rural farmers and microeconomic activities of rural and urban communities with small cash requirements. In the past, the minimum annual interest rate paid on savings and time deposits in microfinance institutions was set by law at 7 per cent against an inflation rate of 17-20 per cent and a central bank rate of around 4-5 per cent (2007/08). In addition, the law allowed discretion for individual microfinance institutions to set their own interest rates on loans, up to a maximum of 15.5 per cent per year. However, this was also later changed. Currently interest rates on loans and advances can be determined by each institution's board of directors. Along with the change in the determination of the interest rate, the cap allowable to a borrower has also been lifted due to the increasing number of clients who needed more money from MFIs, but could not access credit from commercial banks.

Employment and Household Incomes

Employment

Ethiopia is experiencing high population growth with a corresponding increase in the country's labour force. The national labour force was estimated to be around 32.2 million people in 2005, up from an estimated 12.9 million people in 1984. The total labour force is expected to double in the next 25 years, and this will place a huge strain on the labour market even under the most optimistic growth scenario. More than 80 per cent of the labour force is employed in subsistence agriculture[5]. According to a 1996 International Labour Organisation report, the informal sector accounts for 61 per cent of total employment, 70 per cent of which is comprised of women.

Unemployment

In 2005, the unemployment rate in urban areas was estimated to be 20.6 per cent while it was 2.6 per cent in rural areas. As was indicated elsewhere in this report, the economically active population of the country stood at 32,158,392 in 2005 (42 per cent of the total population).

Household Income

Ethiopia is one of the poorest countries in the world. According to the World Bank, per capita household consumption (in constant 1995 US dollars) was $87 in 2001. In 2005 this was estimated to be just above US$100 (2005 est.). The richest 10 per cent of the population accounted for approximately 33.7 per cent of household consumption and the poorest 10 per cent approximately 3.0 per cent.

As noted above, the Government of Ethiopia launched a major anti-poverty initiative commonly referred to as the Plan for Accelerated and Sustainable Development to End Poverty (PASDEP) in 2006. The policy document uses measures of total and per capita consumption to estimate income/consumption for households. According to the plan, urban per capita consumption for 2004/2005 was estimated at $196 million per year. Based on an estimated 4.3 persons per household, this would be $842 per urban household per year.

One of the important consequences of poverty is poor housing and sanitation and bad health that derives from it. The 2004 report by Ethiopia's Ministry of Finance and Economic Development on the Millennium Development Goals (MOFED, 2004) discusses the need to set priorities for investment in sectors which can most strongly achieve the goals. It states that "some preliminary estimates have shown that expenditure on education, water and sanitation development and natural resources tend to be associated strongly with [a reduction in] the state of

[5] (Central Statistical Authority)

poverty." The Ethiopian government's expressed seriousness about "an accelerated and sustained development to end poverty" implies that it cares about improving the housing and sanitation conditions of the poor. If this political will is genuine, it is the foundation for all that follows.

Land policy and issues

Land has remained a controversial subject in Ethiopia; and policies have changed sharply with successive regimes. Under the old imperial regime (i.e. pre-1974), land was treated as private property subject to sale, inheritance and mortgage without any restrictions.

This was radically changed by the Military Government (1974-1991), which made land 'state' property not subject to sale, transfer, or inheritance by individuals. In effect, this meant that citizens only had a 'use' right over the land.

Under the present government, land is also state property. Formally, citizens have only the right to use the land. The only difference now is that individuals can get land through lease payments and retain the right to use the land for the period as determined in the lease contract. As was discussed earlier, the government charges subsidized lease rates for poor and low-income home builders. This means (at least theoretically) that property values are based solely on the improvements (the building/house) excluding the land.

The Federal Constitution of Ethiopia refers to land are as follows:

The right to ownership of rural and urban land, as well as of all natural resources, is exclusively vested in the State and in the Public. Land is a common property of the Nations, Nationalities and Peoples of Ethiopia and shall not be subject to sale or to other means of exchange.[6]

It goes on to say:
Ethiopian peasants have the right to obtain land without payment and to protection against eviction….the government shall ensure the right of private investors to use of land on the basis of payment...Every Ethiopian shall have the full right to the immovable property he builds and to the permanent improvements he brings about…by his labour or capital. This right shall include the right to alienate, to bequeath….or claim compensation for it…..[7]

There are two aspects of land policy which have implications for housing finance: the mechanics of land transfer and leasing, and the valuation of land.

Mechanics of land transfer and leasing[8]

There are two parallel systems in operation.

Rent/Permit

Most urban land is owned by the local government which rents it to individuals with a permit to occupy. The occupier must apply to have the rental agreement renewed annually, and although this is a formality, the paperwork swamps the administration. Since the rents are very low, and not related to any market value, the income scarcely compensates for the administrative burden. At best it is a source of employment, but in truth it is a huge waste of resources. Even though tenure under this system is only secured on an annual basis (i.e. lasts no more than a year), in practice permits are not revoked and the system is perceived as being secure. Thus there is a *de facto*

[6] The Constitution of the Federal Democratic Republic of Ethiopia, (1994), Article 40, 3.
[7] *Ibid.*, Article 40, 4, 6, 7, and 8.
[8] This section relies heavily on material from Olga Kaganova (2005)

security even though *de jure* it does not exist. Due to the low rents charged, there is a reluctance to move to the more market orientated system of leases.

Leases

In theory the rent/permit system has been replaced by land leases. The leasehold system was introduced in 1996 with the intention of making land tenure more secure and less vulnerable to speculation and exploitation. At the same time it was expected that the lease fees would pay for the cost of developing the land. While these objectives are being met in general terms, some states are reducing the costs to make the land more affordable and thereby negating one of the objectives of the system. Others are hoarding it themselves in order, as they see it, to reduce speculation (Berrisford, 2004, 3).

This new system is being introduced on a city by city basis. However, even in cities where it is in operation, less than 10 per cent of the properties have been brought into the leasing system. Land leases are auctioned by the states in which they are located. However since comparatively few parcels of land are auctioned annually, there is huge competition to get them and prices are very high. Where land leases are bought and the buyer cannot pay the whole amount (which is normal), the state accepts deferred payment provided that the buyer pays interest on the unpaid balance. Without the sophisticated software to manage a system such as this, its administrative and financial complexities have been substantial. As a result there are many disputes concerning the payments. Furthermore, since prices are very high, and land is effectively sold on a cash basis, poor people have no prospects of obtaining land through this system. Leases are normally for a period of between 60 and 99 years.

Leases are given on the condition that an approved structure is built on the land within three years. If this condition is not met, the lease can be revoked and the land reverts to the state without compensation being paid to the leaseholder even if there is a part-finished building on the land. This is to prevent speculation.

No more than 10 and no less than 2 years before the lease expires the leaseholder must apply to have the lease renewed at the end of the term. However, if the lease is not renewed, the leaseholder receives no compensation for improvements on the land. It is little comfort to the leaseholder that he may remove the building from the land at the end of the lease as the salvage value will be of minimal value compared to the completed building – unless it is a prefabricated structure which can be rebuilt elsewhere.

The administrative process for land transfer and grant of rights over the land is cumbersome. City Administrations are in charge for recording transactions, certifying property rights, and maintaining records and files, but are not well suited to the process. Each transaction requires “no objections” from several departments.

The overall system of governance of land management has substantial structural shortcomings. On one hand, it excessively over regulates what land holders can and can’t do, and makes it top-down. As a result, flexibility in land use regimes, which is desperately needed for economic development, is eliminated, at least on paper – with all negative implications for productive land use and re-use. What is also important, this stiff over-regulation is established at the federal and regional levels, while local governments do not have direct control over numerous land management parameters that are local by their nature (such as starting prices on auctions, types of land uses recognized in land planning documents, parameter of lease contracts, etc). Lack of key information needed for land management is a major obstacle for a further efficiency increase. There are no street addresses, and cities generally do not have current land use maps or inventories of vacant land. Moreover, there is some general confusion in cities about what can and can’t be expected from an on-going federal cadastre project, and when.

Transactions are taxed at rates of between 4 and 7 per cent.

Valuation of land

Improvements can be privately owned, while land is owned by the government and is given to private tenants either with “rent” rights or for lease. As a result, tenants and the government have to maintain two parallel systems of documenting property rights: one for improvements, one for land.

The single cause of all the problems is the absence of a market mechanism to allocate land and real estate efficiently and equitably. The solution therefore lies in creating this market mechanism, not in fixing some of the most obvious outcome failures while postponing the reforms which would allow the market mechanism to function. This sort of reform is difficult because the act of creating this market requires simultaneous action on a number of different fronts, and because in such a distorted system short term actions may be seen to benefit speculators rather than those who have borne the costs of the current system. Such a distribution of benefits, in turn, can lead to distrust of the overall reform program, and a consequent loss in momentum for reform. Hence, it is difficult to implement the transition to a more market-based system. However, perhaps equally important is that the proposed methods of reform not attempt to buy support through the development of large scale and expensive programs. In the end such programs often substitute for and ultimately delay the development of activities that would be undertaken by the private sector.

Another factor which will inhibit any reforms of this type is the lack of skills in land economics, land valuation and land survey. The previous absolute control by the government of land, and the politicised position regarding land pricing, have effectively removed the professions related to land valuation from the Ethiopian system. As it is banks do not accept the land values paid at auctions. They maintain that they are artificially high (due to the high scarcity prices paid, especially in Addis Ababa). Because the price of land is a product of the amount which is released annually by the state, banks fear that land values could fall just as fast as they have risen if government were to release much larger quantities. Thus there are no market-based benchmarks for land values.

Lack of cadastral information

There is a dire lack of appropriate skills and equipment in the field of cadastral surveys and mapping. Some towns have taken the initiative to implement a cadastral system. For example Bahir Dar has covered 40 per cent of its area with a new cadastre, and this alone has led to the trebling of their land-based revenue.

Housing policy and issues

State of Housing in Ethiopia

The Government has acknowledged that housing conditions are poor. For example, nearly 70 per cent of the urban population of Ethiopia live in unhygienic, congested and inhuman conditions (ORAMP, 2001/2002; CSA Census 1994; www.cyberlaw.harvard). Apart from the poor physical condition of housing, lack of basic facilities like water, electricity, sanitation, roads had also contributed to the deteriorating urban environment in Ethiopia. The following are some indicators of housing conditions in the country:

- 70.2 per cent of the dwelling units in the country have one room only;
- The majority of the dwelling units are below standard and lack adequate living space. The average number of rooms per dwelling unit is 2.3;
- A considerable proportion of dwelling units are shared by more than one household;
- Out of the total housing stock, only 4.4 per cent have piped water inside the housing units; 48 per cent within the compound; 45.3 per cent outside of the compound; and 1.6 per cent get water from unprotected sources such as wells or springs;
- Out of the 75.1 per cent of the total housing units that have toilet facilities, only 8 per cent have private toilets; 32 per cent use common toilet facilities; and 23.89 per cent use open spaces for this facility;
- As to the type of lighting, 95.5 per cent of the houses have access to electricity of which 45.3 per cent have private meters and 50.5 per cent have shared electric meters.

Apart from the poor quality, acute shortage characterizes the housing situation in Ethiopia. In Addis Ababa alone, there was a backlog of approximately 233, 000 housing units in 2002. It is estimated that the housing deficit will rise to 456,000 housing units by 2010 and to 550,000 units by 2015 (Abraham, 2007; Curran, 2007; PADCO, 1997).

The situation in Addis Ababa reflects that of the country as a whole. It is characterized by substandard physical substance and lack of infrastructure facilities. For example, according to existing data (CSA, 1994), the average living space is 4.3 m^2 per person as compared to the African average of 6.5 m^2 per person; and over half of the housing stock is constructed out of temporary materials and which deteriorates over time.

The Ethiopian Statistical Agency has reported that inflation for March 2008 rose to 29.6%, food price inflation even being higher (39.4%). Some reports indicated the inflation rate in January 2008 to be in the range of 36%. The World Bank's reported figure was a 50 per cent inflation rate during the same period.

The housing market has been badly affected by this inflation. The effect has been felt in two ways. First, inflation has led to sharp increases in the price of construction materials, such as cement and steel, and this may dampen the housing market. Secondly there have been steep rises in house rents in Addis Ababa and regional cities; and this has made housing unaffordable to many. In addition, houses being developed by the private sector have been unaffordable to many middle-income households.

Addis Ababa: a case study

To get a fuller picture of the housing in Ethiopia, it is useful to look at the case of Addis Ababa, which has benefited from several studies on the subject. Accurate and reliable data on existing housing stock in Addis Ababa is hard to come by and data inconsistencies are quite common.

One estimate is that the current existing housing stock (i.e. 2007) in Addis Ababa is in the range of 370,000 to 380,000 and the number of households is just over 400,000 (Abraham, 2007; Curran, 2007). On the other hand, the 1994 census which indicated 5.5 persons per housing unit and a population of 3.5 million, would suggest there to be nearly 636,000 housing units. Another source gives the total housing stock in Addis Ababa at 656,000 housing units. Out of these, 15 per cent were said to be pre-1974 owned; 30 per cent were government-owned administered and managed by the government's Agency for the Administration of Rental Houses (AARH) and Kebele administrations; 51 per cent were houses which were deemed to be either 'illegal' built on non-regulated areas; and a little more than 3 per cent were said to be legally leased (Bertaud, 2004). This figure can be taken as authoritative because the Government's Housing Agency, which is responsible for managing all public houses in Addis Ababa, is involved in the data collection process. In addition, this was also supported by other studies on housing in Ethiopia (Muluketa, 2007). A fourth estimate, (Mathema 2004) using other sources would seem to concur with Arnaud and Muluketa. The following Tables and commentary are taken from that source:

Existing housing stock [9]

Table 12. Housing Stock of Addis Ababa

	Housing type	# units	Percentage	Source
1	Formal sector housing	298,000	46.5	Structure Plan (2001)
2	*Kebele* rental housing	150,000	23.4	World Bank (2004) – GOE official estimate
3	Illegal housing (organized)	132,000	20.6	Estimated from percentage (30%) of illegal housing given in Structure Plan
4	Slums (disorganized illegal)	60,000	9.4	
	TOTAL	**640,000**	**100**	

Source: Mathema (2004)

Formal housing is developed by a variety of different agencies. The Table below breaks it down numerically; below we describe each type in some detail.

[9] This section draws heavily on Mathema (2004)

Table 13. Source of Formal Housing Stock

	Housing construction by	Percentage of total "formal" housing stock	# housing units
1	Private real estate developers[1]	1.3	3,874
2	Government housing[1]	33.9	101,216
	of which, RHA housing[2]	(5.3)	(16,000)
3	Government low-cost housing[3]	0.2	700
4	Housing cooperatives[1]	52.5	156,450
5	Individuals[1]	12.0	35,760
	Total	100	298,000

Sources:
1. "Assessment, Evaluation, and Concluding Remarks of the Addis Ababa Master Plan on Housing Sector" (1999).
2. Addis Ababa Housing Office (documents and discussions, 2004)
3. Based on numbers from the low-cost condominium housing pilot project in Gerji.
Notes: Percent may not add up to 100 due to rounding. Due to large variations and inconsistencies in the data from various sources, these numbers may require to be checked for accuracy.

The Kebeles

Kebele housing was a direct consequence of the Land Reform Bill of March 1975 passed during the Derg regime. This Bill outlawed private land ownership, in favour of collective use of land under local *Kebele* Councils. Housing was nationalized, and all "surplus" houses, i.e. all houses other than those being used as primary residences by the owners were acquired by the government. This placed all those units with rents less than 100 Birr per month under *kebele* administration, and those with higher rents under the control of the Rental Housing Authority. Rents for the poorest families were subsidized, often by as much as 50 percent, and were kept frozen over the years. The underlying principle was to subsidize housing for the poor, and promote home ownership. Instead, what happened was quite the opposite: rental housing—that typically serves as an adjustment between housing demand and supply—ceased to grow, land and housing markets got distorted, and the poor condition of *kebele* housing steadily declined.

Today, nearly three decades since the nationalization, these houses are inhabited by over 150,000 families. This translates into roughly 850,000 residents based on the average household size of 5.64 (World Bank Poverty Assessment, 2004). In fact, this figure might be significantly higher because low income families typically have larger families. Hence, *kebele* housing constitutes a significant portion of the "affordable" housing stock of the city.

A typical *kebele* house may be described as a single room, 3-4 metres wide and 4-5 metres long, accommodating anywhere between 5-10 people. The large majority is made of traditional *chika* construction – using mud and wood or straw. Sanitation and hygiene in these settlements is extremely poor: some households have access to communal toilets, others defecate in the open. Household chores—grinding, drying spices, laundry—are done in the street or in the small common open spaces outside the houses. The majority of households use communal kitchens to bake the *injera* bread. Drainage and garbage disposal systems are typically non-existent, except in neighbourhoods have benefited from past or on-going upgrading efforts. Many settlements have benefited from NGO programs that have installed communal (in some cases, even individual) water points.

Rents from these houses are very low, ranging from 2-100 Birr per month. Based on discussions with the residents and officials, it is believed that most rents are between 5 and 10 Birr.[10] This rent is not even enough to cover the maintenance of the houses, let alone serve as a source of revenue for the city. Yet, despite the inherent subsidy, most of the people are not paying their rents. This is partly due to the inefficient collection systems in place, but also because of the common perception among residents that housing is a "social" good, and the poor must not be required to pay for it.

The *kebele* councils, for fear of heightening compensation liabilities, do not permit the residents to make substantial renovations to the houses. "Allowable" changes include only basic maintenance of the structure, or upgrading the building material; the floor plan of the original house must be adhered to. Occasionally exceptions are made.

[10] To put this in context, a similar unit rented from a private owner would fetch a rent of 100-150 Birr per month. The same applies to registered commercial property owned by the *kebele*.

Similarly, new construction is not permitted on an empty lot or abandoned house, except for building *communal* toilets and kitchens. The implication is that even if a plot has additional space to build an additional room, or add a *personal* toilet or a kitchen, this is not permitted by law.

Interviews with some CBOs working on housing and/or maintenance revealed that even though they had generated sufficient funds (from community contributions and NGO/donor support), they had been unable to carry out any substantial improvements to the houses, due to the legal constraints. This is despite the fact that the money to rebuild would come from the community funds, not the government, and that the house would still, by all legal standards, belong to the government.

Occupants, on their part, do not engage in improvements of their homes based due to lack of incentive or resources, but mostly for fear that rents would be increased if the houses were improved.

Housing development in Addis Ababa

According to the Planning Commissioner, Office for the Revision of Addis Ababa Master Plan (ORAAMP), housing is a "high priority" for the City, for several reasons:

- Of the roughly 150,000 *kebele* housing units in Addis today, 70-80 percent will cease to exist in 20 years' time due to their poor quality of construction.
- 97 percent of the *kebele* houses are row houses, or single-story structures, implying "low densities and underutilization of many of the city's prime locations suitable for private investment."
- Ethiopia's concept of legal titles to property so far has been limited to land.[11] There have never been titles for the housing unit per se: *de facto* ownership of a housing structure exists, but there is no formal title to the built property, which is one reason why banks and lending agencies have so far been unwilling to accept the "house" as collateral for a loan.

Given the gravity of the situation, the tendency is expectedly to opt for visible, quick-fix approaches to address the housing crisis. The "urban renewal" approach involves large scale demolition of existing areas and re-housing people into high- and medium-rise condominium units, as a means to achieve higher population densities, and make land available for private investment. To quote the Mayor of Addis Ababa from the *Fortune*, (Addis Ababa, Ethiopia, July 18, 2004):

> *"Old houses will be demolished and new houses will be built in selected pockets to embellish the appearance of the city. They will be replaced by apartments of three and four storeys that could fit the status of Addis Ababa."*

With this construction of housing, the government hopes to "not only to provide shelter to the low-income residents of the city, but also help generate employment to the tens of thousands of young people graduating from the vocational schools."[12] This programme is described in detail below.

Private developers

Private sector real estate developers have so far played a limited role in the housing sector. There are only four major developers active in the City, and all their projects target the upper-income households. In a recent development, Logo Plc., an Italian Ethiopian and English investment, began negotiations with AACA for the acquisition of land for the construction of 4,000 new apartments.[13]

The Bertaud et al (undated) report suggests that at present, developers cannot accumulate land for future use[14].

[11] There was a titling system in place prior to nationalization of land during the Derg regime.
[12] *Fortune*, Addis Ababa, Ethiopia, July 18, 2004.
[13] *Capital*, Addis Ababa, Ethiopia, July 18, 2004.
[14] p 15.

Large-scale developments are discouraged because the developer cannot be assured of future access to contiguous land parcels, nor guess the price or contingencies associated with these parcels. There are only about four formal developers currently developing land and building houses in Addis Ababa. The two developers interviewed are concentrating in the upper income range of the market only. These builders fully realize that their current niche is rather thin and they will have eventually to go further down-market. Nevertheless, they fulfil an important role by improving productivity in the construction industry, and creating a professional building skills. Their activity should be encouraged, while at the same time the government should be careful not to pass along to them hidden subsidies in the form of under-priced land or infrastructure.

Private Individual Developers

Scattered randomly in the low income *kebele* settlements are also some privately-owned houses. These are typically larger, with better structures, and easily distinguishable from the *kebele* houses, owned mostly by middle-income households. Most of these were previously *chika* structures; the families, over the years, have been able to leverage their savings to improve their houses. After the fall of the Derg regime, many of these private house owners built additional units (rooms) for rental purposes. Additional income from rent is quite substantial: a unit with space equivalent to a *kebele* house, and in the same locality can fetch rents up to 150 Birr per month, nearly 30 times the rent for a *kebele* house.[15] Similarly, a typical private house *within* a *kebele* settlement can easily be valued between 200,000 and 300,000 Birr. In contrast, a typical *kebele* house (a 1-room mud structure) has no defined market value other than its cost of construction, which ranges between 7,000 and 9,000 Birr.[16]

Government housing

This comprises housing for government employees and constitutes about 34 percent of the formal housing stock, which includes roughly 16,000 rental housing units managed by the Rental Housing Authority (RHA).[17] These are mostly units acquired by the government during nationalization, which had rents above 100 Birr per month.

Private Housing Co-operatives

Housing co-operatives are the primary mode of housing construction in Addis, constituting over half of the city's total formal sector housing stock. Co-operatives in Ethiopia, similar to many other countries, are formed by groups of people who come together as an entity to perform the function of a "developer". In the absence of an active private sector presence in real estate development, the cooperatives are clearly filling in the gap. They are recognized as legal entities by the government, and allocated land upon which to design and construct the development (residential for most part).

Infrastructure Development

The government must provide infrastructure under the law, but is generally not doing so in practice. The actual construction of infrastructure should for the most part be sub-contracted to private firms. Private developers would likely prefer to contract directly for infrastructure development, and then turn it over to the municipality for ongoing maintenance. This sort of arrangement would remove the risk of a municipal default, particularly regarding the

[15] Assuming an average *kebele* rent of 5 Birr per month.

[16] Estimated comparative costs of construction using subsidized labour and minimum finishing:

Building Material	Cost per sq.m
Chika	180
Hollow Block	600
Brick	1500
Masonry	2000

Source: Structure Plan: Housing Component (2001), ref. page 28.

[17] Proclamation 47/1975 by the Derg regime placed under *kebele* administration all those units with rents less than 100 Birr per month; those over 100 Birr per month were placed under the control of the RHA.

timing in the provision of infrastructure investment. The legal protection of private infrastructure ownership until it is turned over to the municipality (and its value is appropriately reflected in the land lease that is provided house buyers) should be formalized.

Projected Housing Demand

There is a nation-wide acute shortage of affordable housing in Ethiopia.

Taking the case of Addis Ababa once more, according to the Addis Ababa City Development Plan, “an estimated 60 percent of the city’s core is dilapidated, and about a quarter of all housing units have been built informally. The City is not able to provide adequate services to the extension areas thus discouraging house construction and contributing to the expansion of slums.” (ORAMP, 2002). Roughly 40,000 “titled” plots with completed houses are currently lying vacant because of their inability to get services extended to their plots.

Table 14. Projected Housing Need for Addis Ababa (2000-2010)

Projected Need	# Housing Units in year	
	2000	2010
New Housing	140,000	242,000[1]
Sharers/ overcrowded households	50,300	NA
Replacement / upgrading	51,130	NA
Total	241,430	242,000

Source: Structure Plan: Housing Component, 2001

Note: 1. Assuming an increase of the city’s population of 1.26 million, as indicated in the Structure Plan (using high variant). Ref: page 23 of Structure Plan: Housing Component

Another estimate suggests that there is currently a demand for between 350,000 – 450,000 housing units to be supplied in the next 10 years (Curran, 2007). Such supply will: i) address demands for housing by new households being formed, including in-migration (about 230,000 units); and ii) replace housing that is demolished or significantly below-standard and make up the backlog of housing deficit for the existing overcrowded population (about 220,000 units). This would require the production of about 70,000 housing units per year (Abraham, 2007; Curran, 2007; PADCO, 1997).

Whichever analysis is accepted, it can be observed that the Addis Ababa City’s housing market is under considerable stress. There is a substantial imbalance in the demand for and the supply of housing: the supply of housing has not kept pace with the rapidly growing population and rate of urbanization.

Shortage of houses is especially acute for low-income households that account for over 80 percent of the city’s population. Hence, demand is extremely high for those less complex houses that come largely from lower and middle-income households. Demand for high quality buildings mostly from higher income groups of the society who represent less than 10 percent of the city population seems less acute compared to the former (Curran, 2007).

Policy Response

Objectives

Until very recently, the Government of Ethiopia did not have an explicit housing policy. The Federal Ministry of Works and Urban Development is the lead agency entrusted with the responsibility for the provision of housing. Recently, the Ministry has prepared a policy proposal on housing development which will serve as a guide for cities and regional governments in meeting the soaring housing demand in the country (MWUD, 2006).

The policy envisages two approaches to tackle the housing problem, namely direct government intervention; and promotion of private real estate development.

Housing is not included in government’s annual budget in the category of key social and economic development. In addition, appropriations for the housing industry are not indicated. However, the Government has set out projections for the number of houses and finance needed between 2006/2007-2009/2010 fiscal year; and this can serve as proxy to show the resources that the Government plans to earmark for the housing sector.

According to Government's projections, the total number of houses planned to be built between 2006/2007-2009/2010 is 396,000 units; out of which 192,000 units will be built in Addis Ababa and the rest in Dire Dawa and the regional states. The total amount of money needed to complete construction is about $1.6 billion. Out of the total amount, 85 per cent was be spent for construction and the remaining 15 per cent for infrastructure development.

Funding

According to Government plans, the sources of finance for this ambitious housing project are the following:

- Bank borrowing by regions;
- Bank borrowing by housing development enterprises to be established by regions;
- Regional Governments raising funds by selling bonds; and
- Private savings by beneficiaries (MWUD, 2002).

The Government's two housing strategies cited earlier will benefit from the above financing schemes. For example, funds raised by regional governments through bond sales will be used to finance highly subsidized, low-cost housing for the poor and the very poor. It is also envisaged in the urban development policy that some of the capital raised by regions will be used to augment the capital base of housing development enterprises for providing housing to moderate income earners (MWUD, 2006).

Housing Programmes

The Government sees its role as the main provider of low-cost housing to poor and low-income households at highly subsidized rates. The Government aims to achieve this objective through the use of two strategies:

Government Housing Projects

The Government has taken the decision that low income housing development should primarily be undertaken by the public sector. This is a subsidized initiative to make houses affordable to the target group.

The programme was pioneered by the Addis Ababa City Government with support from GTZ in 1996. Addis Ababa has established the Housing Development Project Office (HDPO) as a semi-autonomous agency to supply housing at low and affordable cost. This is an ambitious plan to redevelop the *kebele* housing, by the construction of 4 storey walk-up blocks of flats for sale as condominium units. The aim was multi-faceted:

- to speed up supply of low-cost housing for the poor
- to densify and "renew" prime urban land
- to boost the building/construction industry, and pump cash into the economy by generating employment opportunities for the poor.
- to redevelop the existing run-down *kebele housing and* the residents into the new flats, thereby freeing up the land area for the construction of more new housing. Other kebele residents would be moved into this housing.

The government initially set a target of building 20,000-30,000 new condominium units in Addis annually to meet the housing shortage. The target is to build 192,000 units by the end of 2010. The national government is contributing funds to support this large scale housing sector undertaking.

Condominium units constructed by HDPO are supplied to poor and low-income residents of the city. Most of these are picked from the City Government's registry of house seekers or are residents who might have lost their residential units due to the roads expansion and upgrading projects underway in the city. As per the guidelines issued by the City Government, eligible households and individuals must pay 20 per cent of the cost of the houses up front as down payment. Mortgage facilities are worked out with the government-owned Commercial Bank of Ethiopia to pay the balance in the long term.

This strategy has now been extended nationally. As the research was underway, the Government has officially announced ambitious plans to build more condominium housing units (i.e. estimated between 250,000-300,000) in the coming 5-7 years. It is primarily being undertaken by regional governments and city administrations with the support of the Federal Ministry of Works and Urban Development. According to this plan, regional and city governments will set aside special funds from their annual budgets and construct low cost housing units. As much as possible, these units will be built on existing plots in central parts of cities and towns thus helping stave off additional transport costs for potential occupants, most of whom are likely to be poor and low-income households. The primary target groups are urban residents who are being displaced as a consequence of new real estate development in central parts of the city. The houses are supplied below cost thanks to the land lease payment that the City Government receives from private real estate developers, which is being used to offset the cost for the poor.

Most of these projects utilize low-cost designs, and are to be multi-storied. The features of the programme are:

- The government arranges bridging finance from bank borrowing to cities
- Construction is undertaken by micro, small and medium-scale private construction firms
- Use low-cost materials and methods
- To utilize labour intensive technologies thus creating employment opportunities for skilled and semi-skilled workers

The houses so constructed are for sale and not for renting. Cities transfer the houses to low and middle-income residents who do not have their own houses, especially those relocated from their houses due to developments taking place in their localities. (If they already live in rented government houses, they are required to hand over the house). About 20% of the units are allocated to women-headed households.

Terms of Repayment of households buying condominium houses are:

- 20% advance payment
- Repayment Period 15-20 years
- Interest rate 7.5%
- Grace period 1 year

In addition, small and micro-enterprises (SMEs) are established in major urban centres to supply materials for these projects. The Government promotes SMEs by providing working capital in the form of loans and technical assistance. While job creation is the idea behind SMEs the Government is also hoping that such enterprises will have significant impact on the economy. The capacity of local contractors and engineers is also expected to grow as a result of such entrepreneurships.

The Government's plan to provide affordable housing to low- and middle-income through the condominium project has not been without problems, and the programme is increasingly coming under scrutiny because of doubts as to whether this scheme will provide sufficient affordable housing for the low and very low income groups. Among the concerns are:

- Lately, there have been sharp rises in prices of construction materials such as iron, cement, wood and other building materials. While this has not put a dent on the construction industry in the short-to medium term, its long term consequences and particularly its effect on the supply and demand for housing have yet to be seen. Costs rose from an estimated $87/m2 to about $144/m2; and continue to rise rendering it impossible for access to affordable housing by the poor.
- Although unit prices were set at the original estimate ($87/m2), many units are occupied by higher income households who can afford to pay full price ($3,590-$6,154 or more) "at one go" or a "larger down payment". This means that moderate-income families are benefiting from the scheme intended for poor and low-income households. The Government has not officially admitted the problem but they are aware that this is primarily

caused by escalating costs of construction, which has rendered housing unaffordable for the poor;

- Many people have found it very difficult to adapt their living patterns to multi-storey living. Whether for this reason, or the opportunity for windfall profits, many families move out and sub-let their dwellings to higher income families. The gap between the amount paid by the official allottee and the rent he can charge can be as much as five times.
- Even with low-interest loans, the down payment and monthly payments are not affordable to 80 per cent of the population. Curran puts is as follows:

  About 80% of Addis Ababa's central city areas have been described as "slums", with a high proportion of substandard housing, insufficient infrastructure, and over-crowded conditions. Since it appears that the median income in Addis Ababa is currently less than 550 birr per household (perhaps in the 500– 525 birr per month range)[18], and that over 60 - 70% of the population work in the informal sector or are unemployed, most of these households:
  - *do not have capital to afford a down payment on market rate housing or even partially subsidized housing (such as the condominiums currently being built for sale as part of the Low Cost Housing Scheme);*
  - *cannot afford monthly payments that would adequately cover the real cost of even very basic standard quality housing*
  - *may be able to contribute significantly to self-help housing schemes on free, serviced plots on the periphery of town.*
  - *often depend on the livelihood and social network of their current central city neighbourhoods, and would suffer significant loss in livelihood security by being forced to move to a new settlement in the periphery.*
  - *currently live on land that would have relatively high income potential for commercial redevelopment, given the free play of market forces*
  - *do not have legal ownership or secure tenure in their current housing, and thus cannot "sell" their property (or be compensated for it) at its fair market value, even though they may have lived in their home for one or more generations. (Curran, 2007, 7)*

Apart from the sustainability and affordability issue in the long-run, it is important to note that the social and cultural implications of such an ambitious housing scheme remain to be determined. Concerns have been expressed regarding both the social and financial implications of the solution.[19]

The private sector

The Government is aware of the potential contribution of the private sector towards easing the housing problem and aims to encourage its participation in the housing industry. As a result, private real estate developers have increasingly been involved in the construction of standard housing units, mainly for the middle and high income groups. To make housing affordable, the Federal government has been helping private developers through incentives, for example, giving free land to real estate developers to build rental housing for low-income families (with rents less than 100 Birr per month) and also facilitating the supply of essential infrastructure, like water, roads, telephone and electricity services, etc. Currently, mortgage facilities are potentially available for houses to be developed by private sector real estate developers.

Housing Construction Co-operatives

The Government sees one of its roles as the principal provider of land for housing construction by co-operatives at subsidized prices. In addition, the Government will also provide basic facilities, such as water, electricity, sewerage, telephone, etc. services to reduce cost and make the houses affordable to the target group. Low and moderate income earners have been the main beneficiaries of housing cooperatives.

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[18] This is an optimistic estimate. Based on the PADCO (1997) study, it appears that about 50% of households in Addis Ababa earned less than 340 birr per month at that time.

[19] Mathema (2004), 29 – 32.

Between 1986 and 1992, about 2,667 cooperatives with a total membership of 69,775 home builders were set up in 26 urban areas. Addis Ababa alone accounted for 85 per cent of the total membership. In terms of output, between 1975 and 1992, a total of 40,539 housing units (2,252 units annually) were built by cooperatives (PADCO, 1998).

Possible new directions

Kebele upgrading

One alternative to the construction of multi-storey flats is to upgrade the existing kebele housing. This would require selling off the units to the existing occupants: in view of the dilapidated condition, the price would only be nominal. The sale of units would have to be conditional on either the land being subdivided and titles issued, or being sold to cooperatives. In both cases there should be a commitment by the residents to maintain the common areas and the infrastructure. Thereafter, the residents could progressively improve their units, possibly with loans from micro-finance institutions. Public assistance would be targeted to those kebeles that were willing to contribute something and agree to manage the goods provided. Such a policy would trigger a massive increase in housing standards comparatively quickly, without the major social and physical disruption that the condominium housing project is causing, and at a much lower cost.

Housing finance

The mortgage market in Ethiopia is not well developed. The absence of such a market has impeded the emergence of either savings institutions or long-term financing facilities in the country. At present, only government-owned banks, viz. the Commercial Bank of Ethiopia (CBE) and the Construction and Business Bank (CBB), provide housing finance for residential consumers. Because of the risk factor and shortage of capital for investment in the housing sector, the contribution of the emerging and fast expanding private banking system in providing long-term housing finance is insignificant. The absence of a developed formal network of housing finance institutions has meant that the housing financing sector has negligible impact on the development of the broader banking system.

Penetration by the formal banking institutions into the urban housing finance market has been by and large minimal over the past four decades. Study conducted in the mid-1990's, for example, indicated that only 10 percent of households used the public sector housing bank as the primary source of funding for residential construction, and only 6 percent used the same source to purchase their plot of land (PADCO, 1997).

Housing finance in Ethiopia: a background

In Imperial Ethiopia (i.e. pre-1974), urban land and housing was largely in private hands primarily owned and controlled by a small landed class of aristocrats. More than 60 per cent of the housing was rental units. Since most urban land was owned by the upper class and there was limited investment in the housing sector, there was a severe shortage of affordable residential housing for low and middle-income households (Abraham, 2007).

During the Marxist-Leninist Derg—1974-1991, the Housing and Savings Bank[20] was the only state bank lending money for housing construction, repair and extension. Just before the downfall of the Derg, this bank was providing long-term mortgage lending to private individuals and housing co-operatives at interest rates of 7 and 4.5 per cent respectively (PADCO, 1996)[21]. These rates were subsidised: the central bank rate at the time was running at between 9-10 per cent. The Government was in favour of subsidized housing in the country; hence, the mortgage lending rate was kept below the central bank rate. During this period, because of the socialist policies of the

[20] This is currently named the Construction and Business Bank (CBB).
[21] Currently, this state bank is known as the Construction and Business Bank (CBB), and, until recently, has been the only bank in Ethiopia specializing in the provision of finance for the housing sector.

regime, economic growth was slow and inflation was relatively low at between 4-5 per cent. The State was the main player in the economy and private initiative in many sectors, including private mortgage lending, was very much discouraged.

Following the onset of the financial reform program in early 1990s, the Housing and Saving Bank became the Construction and Business Bank in September 1994. The Construction and Business Bank is now established as a universal bank in line with the dictates of Regulation No. 203/1994 issued by the council of ministers. It caters for banking services, mainly financing loans for construction, repair, modification and acquisition of residential and non-residential buildings, for construction sector activities and for the development of hotels and tourism. It also provides business loans to meet the working capital requirements of commercial and industrial activities. The bank also has the mandate to offer foreign banking services.

The government that came to power in 1991 did not support the policy of highly subsidized residential housing supply pursued by its predecessor. As a result, it introduced a market-oriented system to housing development and launched a major effort to respond to housing demand and supply according to the dictates of the market. Land was declared state property and a new policy of holding land through a lease system was put in place. The lease period varied from 99 years for owner occupied housing to 50 years for commercial and other uses. The new market orientation removed most subsidies and liberalized mortgage interest rates to approximate market rates (Abraham, 2007).

However, the Government's financial reforms did not result in expanding residential housing finance in the country. Historically, the Construction and Business Bank (CBB) was the only bank giving mortgage loans to home builders. Up until 1995, the CBB gave mortgage loans amounting to $42 million for the construction of 26,912 residential houses. These were subsidized loans at below market interest rates. Of the total units built, 14,881houses (55.3 per cent) were built by borrowers whose monthly income was below $52. This meant the bank played a pioneer role in supporting the financial needs of the middle income group of society for housing construction.

The narrowness of the mortgage market dominated by the CBB was a major factor that has not helped the expansion of mortgage finance in Ethiopia.

In recent years, some other banks have started to enter the mortgage market. For example, big banks like the Commercial Bank of Ethiopia and the Development Bank of Ethiopia, which were not active before, have increasingly become important lenders to the commercial construction sector at interest rates ranging between 9-10 per cent for a maximum of 10 years. There are also signs that private banks are beginning to show interest in providing mortgage loans to the commercial construction industry. The Commercial Bank of Ethiopia has also been made responsible for providing the loans for purchasers of the condominium housing units.

Housing Affordability

As indicated earlier, urban incomes in Ethiopia are generally low and this has serious implications on low housing affordability. For example, in Addis Ababa, studies conducted on household incomes brought out the following facts (CSA, 1998; PADCO, 1997):

- 50 per cent of the population was estimated to earn less than $35 per month in the mid 1990s;
- 74 per cent earned less $75;
- The largest number of households, over 110,000 families, earn about $41 per month; and
- Less than one-fourth of the city's households earn more than $92 per month.

The above data illustrate the difficulty of providing affordable housing by the majority of the population.

Fuller data on the distribution of incomes in Addis Ababa reinforce the difficulty of providing affordable housing.

Table 15: Estimated Household Income Distribution for Addis Ababa in Birr

Income Group	Income bracket	Per cent of Population in 1995-2001	Rough estimate of Income distribution in 2006 (%)	Midpoint of income group	Monthly payment affordable at 15%	Monthly payment affordable at 25%	Size of affordable home at 1400/m²
Extremely low income	0-200	16	14	100	15	25	-
Very low income	200-400	34	26	300	45	75	-
Low income	400-700	24	20	550	83	138	15
Low/moderate income	700-1100	10	15	900	135	225	24
Middle income	1100-1600	6	10	1,350	203	338	37
High Income	1600-2400	5	10	2,000	300	500	54
Very high income	2400 and up	5	5	12,000	1,800	3,000	325

Source Curran, 2007, Table 4, p109

It is not clear what definitions were used for the income group categories in the Table above, but it can be observed that the 'middle income' group consists of only 10 per cent of the households. The 4 categories of the low income group constitute 75 per cent of all households. The 'high income' and 'very high income group' constitute only 15 per cent of the total population. Based on this projection (2007), it appears that the median household income is around $53 per month given the income distribution as depicted in Figure 6. The bulk of the data in this projection point to very low income figures that cannot guarantee access to affordable housing in the short- to medium-term time perspective.

Curran, commenting on the above table, writes
The last two columns of the above table illustrate that for the three lowest income groups (all those under 700 birr per month) – comprising at least 60% of the population - it is not possible to afford the construction price of a very small, modestly-constructed home, even with a no-down payment loan at 5% over 20 years. Only the top-third of the population could afford the actual cost of a modest home or better. The exception to this is that a low-income household might be able to self-construct a small home on a serviced plot. For most of the low income households, rental is really the only option, and even that will only be affordable if there is significant subsidy of the actual cost of housing. However, responsible renters might be given the hope of attaining a title to their home after a certain period of time, to increase their sense of personal investment and care for their home and the site.

This situation is further exacerbated by the fast increasing costs of construction. Although the Government is aware of the problem, resource constraints have tied its hands from taking action to assist the groups affected by price and interest hikes in the construction industry.

As things stand now, it is only the upper income groups, and members of the Ethiopian diaspora who can afford newly constructed formal housing in Ethiopia. The diaspora have become major sources of remittances from abroad and continue to build residential and commercial units in Addis Ababa and the major regional cities[22]. Official government estimates put the amount of remittances at $1 billion in 2007/08.

Table 15 also illustrates something about housing affordability for Addis Ababa's residents; particularly their ability to repay mortgage loans. As can be observed, using the midpoint of each income group, an affordable monthly payment for housing has been calculated, using both 15 per cent and 25 per cent of monthly income as the criteria for affordability. At 25 per cent of household income, which is obviously a high proportion for very low income households, no household in the first three income groups could afford a commercially-constructed home of 25m² – the minimum allowable size which is determined by the government.

[22] The recent global economic crisis has affected the flow of remittances to the country. Nevertheless, foreign remittances continue to be major sources of financing residential and commercial construction.

Current Situation

Ethiopians have four methods of financing their housing. First, a significant number of Ethiopians build their houses through formally registered housing co-operatives that obtain loans from the Construction and Business Bank (CBB). As is indicated elsewhere in this report, these used to be the most common forms of subsidized housing ownership particularly during the socialist Military regime (Derg); and there were 69,775 home builders registered under such schemes until 1992, although their significance has dwindled among the population as a whole. But they still remain popular among poor and lower middle-income households.

Second, paradoxically, many of the higher income group home builders choose not to borrow, preferring to finance housing out of personal savings as a means of avoiding debt and the complexities of the mortgage system. But more importantly building incrementally, and financing construction from savings and current income, is the normal method used in the construction of informal housing.

Thirdly, financing for housing is leveraged through "*edirs*" and community savings schemes.[23] According to GTZ officials, there is close to 400 million Birr (US$50 million) currently saved in credit unions which can be mobilized towards housing and infrastructure improvements;[24]

Lastly, housing is financed through mortgage loans. This covers residential and commercial construction. However, it needs to be pointed out that mortgage delivery is limited given the fact that there is effectively only one mortgage bank, the Construction and Business Bank.

Constraints

The real estate market in Ethiopia is underdeveloped. Factors limiting the growth of the sector are the fact that there is only a single government-owned bank, i.e. the CBB, operating in the real estate, particularly housing, for a long time and private banks have not been lured into the market due to risk factors in short-term financing, less profitability and lack of experience. Government banks, like the Commercial Bank and the Development Bank of Ethiopia have begun to be involved but only in the commercial construction sector. All this has meant that the real estate market and mortgage financing in Ethiopia have a long way to go before they reach the standard of many sub-Saharan countries.

Borrowing is also limited due to stringent collateral requirements and other impeding requirements. Given the weakness of the formal financial sector and the high expenditure that housing requires, many urban households have had to enter into the informal financial network to build or upgrade their dwellings units. Personal savings, family borrowings and an active network of informal sector organization such as traditional rotating savings associations (other wise known as *ekubs*) currently fill the financial gap for homebuilders.

As a result of the government policy concerning land values, and the fact that a free market does not really exist, it is exceedingly difficult to establish a 'real' market price to determine the value of a residential unit. This increases the risk of mortgage lending.

Mortgage lenders

As noted above, one bank effectively has a monopoly for residential mortgage lending - the Construction and Business Bank.

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[23] Edirs are community associations that function like savings schemes (for funerals). They play a pivotal role in society, and are being increasingly seen as a resource from where community funds may be mobilized for physical improvement programs.
[24] Based on a meeting with GTZ representatives on July 26, 2004.

Table 16: Loans Extended by the Construction and Business Bank:1980/84 - 2000/04

Year	*Amount of Loan (US $ 000s)*
1980-84	*11,457*
1985-89	*23,919*
1990-94	*16,637*
1995-99	*12,731*
2000-04	*6,849*
Total	*71,593*
Annual loan expenditure	*3,580*

Currently the annual total is running at about $68 million, 19 times greater than the average between 1980 and 2004. In terms of housing, in 2005/06, CBB approved a total of $12.5 million. This represented a 179.41 per cent growth over the 2004/05 fiscal year. The Table below shows that the commercial sector is still the largest borrower. The breakdowns for residential and commercial construction are not provided for other years.

Table 17: Loan Approval Performance of the Construction and Business Bank 2003/04-2005/06 (in US $)

				Variation between 2005/06 and 2004/05	
Type of Loans	**2005/06**	**2004/05**	**2003/04**	Absolute	Per-centage
Building Construction	46,256,409	28,820,512	9,846,153	17,435,897	60
**Residential	12,512,820	6,974,359	5,435,897	5,538,461	80
**Commercial	33,743,589	21,846,153	4,410,256	11,897,436	54
Business Loans	7,179,487	2,769,230	615,384	4,410,257	162
Short term	1,846,153	882,051	266,667	964,102	114
Medium term	5,338,809	1,846,153	369,230	3,492,656	189
Overdrafts	5,435,897	584,615	410,256	4,852,282	829
Total	66,056,755	34,902,561	11,507,690	280,118,03	89

Source: CBB Annual Report –2005/06

Recently, government banks like the Commercial Bank and the Development Bank have joined the mortgage market but only in the commercial construction sector. The same is true of the emerging private bank sector. There is limited involvement in residential mortgage by public and private banks because of perceived high risk and shortage of experience.

The mortgage interest rate was revised recently. During 1997-2001, lending rates ranged from a low of 10.5 to a high of 15.0 per cent. Between the fiscal years 2001/2002 and 2002/2003 lending rates were considerably reduced to vary from a low of 7.5 per cent to a high of 13 per cent per year. The current (2008) mortgage interest in Ethiopia is 9.75 per cent for a maximum of 10 years and 10.75 per cent for a period exceeding 10 years. This rate is applicable for the purchase of existing real estate sale as well as for new construction. Existing real estate sale refers to the sale of existing assets, i.e. transfer of ownership of existing assets; while new construction refers to loans advanced for putting up new construction.

According to discussions with some real estate companies, comparatively few Ethiopians take out mortgage loans for residential construction.

Conclusions

The preceding discussion points to the challenges of accessing affordable housing for many households and individuals in Ethiopia. As was reiterated throughout this report, the escalating cost of construction has sharply raised the cost of housing. There are no feasibility studies on the cost of housing in Ethiopia; but, the current general estimate for a house with 3 rooms, falls within the range of $15,000-20,000. For a maximum 25-year mortgage period, the monthly payment for such a house will fall in the range between Birr 500-666 ($50-70) for a single household. This is beyond the reach of most poor and even moderate income households in Ethiopia. All this may mean that housing in Ethiopia within the short- to medium time-frame will continue to be an unaffordable commodity for many households.

In summary, the demand for housing finance has been reduced due to:

- poor and weak supply of plots of land for housing construction;
- increase in the cost of construction materials, partly caused by the high inflation rate in recent years;
- increase in the minimum own contribution required by the CBB from borrowers who desire to construct houses (from 5 percent to 20 percent); and
- the limited capital base of the CBB.

Future prospects for Sustainable Mortgage Finance.[25]

Mortgage and construction finance represents less than 1 percent of Ethiopia's GDP. This is a very low figure even by the standards of low-income countries.

This current situation arises for a number of reasons. First, is the relatively low overall level of financial savings available in the country. Ethiopia is in the early stages of restructuring its financial system and is doing so at a slow pace with considerable caution. A second problem is the apparent operational inefficiency of the government monopoly, the Construction and Business Bank (CBB), which is one of the larger public banks in the country.

The current law in Ethiopia enables commercial banks to extend credit collateralized by structures, i.e. construction and mortgage loans. In addition, the foreclosure law, allowing non-judicial foreclosures, works well, according to the banks. But the banks need a registered title to back the claim. While the law allows for this, timely availability of title and registration remains a problem.

As the financial system is restructured, the six domestic private commercial banks could also become a source of potential lending for real estate. They already offer several services to developers. For example, they accept foreign deposits, and act as a "proxy" for their depositors, providing site inspections of construction progress. They also release funds as construction milestones as they are met, usually within a day or two of these inspections. Finally, they make a limited amount of short-term construction advances between construction draws so that the construction process is not interrupted by inefficiency in the financial disbursement process. Their development, however, will follow and not lead decisions made with respect to the largest public banks which hold most deposits.

Many banks have started to encourage saving and credit discipline with "savings for housing" schemes. Under these programs a potential borrower who agrees to deposit a pre-specified amount for a period of, e.g. five years, is simultaneously generating a cash down payment and demonstrating his credit worthiness.

The structure and operation of the main mortgage lender, the Construction and Business Bank, may lack sustainability. It was a traditional state-owned Housing Bank: it received funds at preferential rates (one third of its funding derives from the World Bank at a long-term interest rate of 1.5 percent (IDA loan)), and passed on the subsidy to home borrowers.

The CBB continues to provide mortgage credit, but is not very dynamic, in part due to questions about its status. Negotiations for a mortgage lending line can reportedly drag on for years. Approval for a simple construction draw takes an average of six weeks from site inspection. At the current time the CBB is slated for "privatization," which possibly also contributes to its lack of dynamism.

About 80 percent of its loans are mortgages on existing real estate. They appear to be relatively well performing assets. Its internal studies show a high potential demand for mortgages, and thus mortgage lending will remain its focus. It also has approved business plans for construction lending to developers. About half of its mortgage portfolio of approximately 710 million birr is to individual homeowners. This consists of about 12,000 individual loans at 50,000 birr average balance.

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[25] For more on this see Bertaud et al (undated), 35

The two reforms are: first, the government can do a better and more transparent job of fulfilling a much more clearly defined public role. Such a clarification by itself would encourage a more active private sector involvement in real estate development. Second, it can refrain from competing with the private sector, and/or attempting to use a range of restrictions on how assets can be used so that transactions only take place if they are deemed to clearly fulfil a public role. The key to a well-functioning housing market is to foster a viable private real estate development process and to design public policies that complement and build on these private rights.

Constraints to growth in long-term housing finance

The implications of the controlled land value policy

The overall system of land pricing and allocation by government continues to be administrative (non-market) to a very large extent. In particular, a negligible fraction of all existing land holdings have originated through market procedures (auctions). Most newly-allocated land plots are given to applicants on a waiting list for housing construction at administratively established prices (usually the same price for the entire city) that are substantially lower than market prices of these plots (usually, from several to ten and more times lower). Similarly, heavily subsidized land is given to many industrial and social land users.

For commercial sales, Addis Ababa City Government has created a complex formula to price land for sale in the absence of market transactions. It reduces the price of land for high density development, and the sales of leases are based on developers' proposals[26].

There are several weaknesses in the system. A developer who realizes that there is no demand for the large house or apartments he/she has planned would not be able to build smaller apartments or smaller plots because (i) the size of apartment or houses are a condition of effectiveness of the title deed, and (ii) the price of land would have already been paid to government at a higher price than the new higher density would imply. The government is unlikely in this case to give a refund to the developer. The pricing system is not linked to the cost of developing land, which at the time of sale is not known. The current pricing system could result in large losses for the city, and large subsidies for some income groups.

In practice, land is not mortgagable, despite the fact that the federal land lease law (Proclamation # 272/2002) allows using the use of leased land as collateral. Banks (both private and governmental) do not accept land as collateral for a number of reasons, one of which is land price control by City Administrations. Loans can be secured by improvements (buildings) only, regardless of the land tenure form of tenure of the land underneath the buildings.

Single plots are auctioned. While this system does create a relatively market-based form of pricing, it militates against co-ordinated development. In addition, due to the problem of mortgaging land buyers must pay cash. Since many do not have the funds available, the state permits deferred payment which, in itself is a problem, as discussed below.

In short, the major issue in Ethiopia is not the type of land rights which are being used but whether these rights are fully tradable and the restrictions on property use are clear. When governments try to retain control on land development through, for example, conditions built into leaseholds which are designed to reduce speculation, they increase the risk of investment in real estate by decreasing the certainty of property rights. The direct and almost certain effect is to discourage and decrease the volume of investments.

Competition by CBB

The CBB was capitalised with a long-term soft loan from the IDA. It is practically impossible for private banks to compete on an equal footing with funds from local sources – for example deposits and savings accounts. Controlled interest rates are a further disincentive to enter the market. Banks prefer to invest their funds in Treasury Bills and Government Bands which are risk free and lack the risks and administrative challenges of mortgage lending.

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[26] This section relies heavily on: Bertaud et al (undated), 26.

The interest rate policy
The highly negative interest rates make it very difficult to attract savings, so the savings and loan concept which several banks are pursuing has little chance of succeeding at scale. Unless and until inflation is brought down and relatively attractive rates can be paid on savings and investment accounts, it could be difficult to attract funds required for mortgage lending at scale.

Undeveloped financial markets
Due to the lack of developed financial markets, there is little scope for raising long-term finance that way.

Micro Finance for housing

Micro-finance institutions offer a potential area for intervention as a source of finance for the poor and low-income. According to information obtained from the Association of Micro-finance Institutions in Ethiopia (AMFIE), some relatively big micro-finance institutions have started extending small loans for housing. The loans are mostly given to creditors who purchase new condominium houses built by the Integrated Housing Development Project Office (IHDPO) of the Addis Ababa City Government as part of the low-cost housing scheme. The loans cover usually the down-payment for the houses, which is about 20 per cent. The interest rate for such loans ranges between 12-15 per cent against a central bank rate of 4.5-5.0 percent.

Subsidies

Subsidies are aimed at making housing more affordable for the lower income groups. Unfortunately, targeting subsidies is difficult. Often instead of helping the poor, they can have the effect of delivering windfall profits to the few and distorting the market and discouraging competition. In Ethiopia, subsidies are used in both land and housing. This section describes how the subsidies are applied.

Land

In an attempt to meet the demand for housing, local governments buy land on the periphery of the city, subdivide it, install services, and allocate it to families on a waiting list. The standard plot size is 250 m^2. These plots are transferred to those on the waiting list at a nominal price – often not even enough to cover the compensation to the farmers, let alone the cost of roads, water etc.

Not surprisingly the waiting lists are growing, and the public sector cannot keep up with the demand. But the current practice imposes an unrecoverable financial burden on public budgets.

Authorities do not quite recognize that the above land allocation practices translate into large, not accounted, not sufficiently targeted, and not-equitable indirect subsidies to land recipients, and create substantial distortions for the real estate markets and the urban economy in general.

Not surprisingly, some of the sites obtained through waiting lists quickly find their way in the real estate market, thus creating windfall profits for ex-wait-listers. However, while this situation poses a problem in all cities, it is currently difficult to assess the magnitude of the problem.

Housing

Subsidies also affect the housing market. The government's main programme for lower income groups is the condominium housing which was pioneered in Addis Ababa, and is now being replicated in the larger cities throughout Ethiopia. The costs of the units being build in Addis Ababa by the City's Housing Development

Programme Office (HDPO) are structured as follows[27]:

Pricing the individual unit

The cost of Individual units is based on actual costs for the whole block on a square metre basis, multiplied by the actual area of the unit. In this way the costs of access balconies and stairs are included in the costs and attributed to the individual units. To be strictly accurate, the cost per square metre of the individual units differs because the small units have a higher ratio of bathroom and kitchen to habitable space. Since these rooms are more expensive per square metre than non-serviced areas, small units are thereby given a moderate degree of cross subsidy.

Other costs

Land, professional fees are then added in. This is done by taking the sum of these costs and dividing it by the total area of the units, thus giving a cost per square metre of occupiable accommodation. This is then multiplied by the area of each unit to give the cost per unit. It seems that the HDPO's overheads are not included in the costs, which is a form of subsidy.

Cross subsidies

The City Government of Addis Ababa Proclamation 19/2005, section 12.2 states:
"Construction cost may, where necessary, be computed and determined, by the City Cabinet, with a view to enabling purchasers with low income to be cross-subsidized by purchasers with better income."

Down payment

Most purchasers are required to make a deposit. An exception is made for the studio and one bedroom units which are intended for the poorest applicants. It is assumed they that will not have the means to accumulate sufficient capital. The City Government of Addis Ababa Proclamation 19/2005, section 9.1, determines the following minimum deposits required:

Studio	7.5%	1 BR	10.0%
2 BR	20%	3 BR and more	30%

Mortgage payments

The Commercial Bank of Ethiopia provides the long-term finance. Under the City Government of Addis Ababa Proclamation 19/2005, sections 9.2, 9.3 and 11.1 the terms are to be as follows:

Table 18: Addis Ababa: Integrated Housing Programme Repayment terms

Unit	Period of loan	Grace period	Interest rate
Studio	20 years	6 months	0%
1 BR	15 years	3 months	2%
2 BR or more	10 years	-	8.75%

However, provision is made is section 11.2 for the rate to be adjusted, and it is understood that the Bank currently charges 7.50%.

It will be noted that purchasers of Studio apartments receive very concessional rates, and one bedroom purchasers also enjoy an important concession in terms of the interest rate.

Maintenance costs and insurance

As yet there does not seem to be a procedure for calculating the maintenance costs for which condominium owners will be responsible. These will include

- Insurance of the building against fire and damage from natural causes such as wind and floods.
- The maintenance of public spaces, for example the public open space and landscaping between the buildings

[27] This material is taken from Martin (2008)

as well as stairways and access balconies, and the community facility buildings.
- The cost of routine repairs and maintenance such as unblocking drains, repairing leaks in water pipes etc, painting the steel staircases etc.
- The cost of future repairs to common elements such as roofs.

Summary and Recommendations

On average, urban residents in Ethiopia spend about 49 per cent of their income to fulfil their basics requirements. This figure can be as high as 70 percent and 79 per cent for some cities such as Mekele and Bahir Dar respectively (PADCO, 1998). This is one indication of the fact that the majority of the urban population in Ethiopia does not have adequate income to house itself without housing finance of some sort.

Private banks came to the banking scene thanks to the collapse of the Military Regime (Derg) and its replacement by the current government in 1991. In less than two decades, private banks have succeeded in controlling nearly 49 per cent of the market. Given the relatively short history of private banking in Ethiopia, this is a major feat by the private sector in increasing their share of the banking industry.

It has been observed in this report that labour-intensive sectors like the construction industry (e.g. those involved in housing) are experiencing difficulties accessing bank financing. On the other hand, micro-finance institutions (MFIs) are not in a position to offer an alternative because as they currently operate do not pose a realistic proposition given their limited loan ceiling and short loan duration.

The increase in the cost of construction materials such as cement, wood and sheet metal has created a bottleneck in the housing market in Ethiopia. The price of cement, wood and sheet metal has been escalating largely in response to the high demand. The recent effort by the Addis Ababa City Administration to produce large numbers of housing units has led to a sharp price rises in cement and other construction materials, suggesting that large scale housing production would be hamstrung by supply constraints in construction materials.

The real estate market in Ethiopia is underdeveloped. As a result, this has made it exceedingly difficult to establish a ‘real’ market price to determine the value of a mortgage. In other words, it is difficult to assume that the mortgaged object will be sold at a price that equals at least the outstanding debt.

As was pointed out earlier in the discussion, presently only the Construction and Business Bank (CBB) is directly involved in providing mortgage financing. However, it is also true that about 70 per cent of its lending seems to go for non-residential construction. Although the private sector has made considerable progress in increasing its share of the banking and financial sector in a relatively short period of time, the private banking industry as a whole remains reluctant to engage in housing because of less profitability, high risk, shortage and lack of experience.

The data presented in this report suggests that the housing market in Addis Ababa is under considerable stress. There is a substantial imbalance in the demand for and the supply of housing. Supply of housing has not kept pace with the rapidly growing population and rate of urbanization. On the other hand, demand has been growing quite rapidly, mainly driven by rapid urbanization, high population growth and household formation. However, it has to be considered that the market for the housing sector is highly segmented and far from uniform.

Key players and Possible Interventions : conventional financial institutions

Progress in the housing finance sector in Ethiopia can be achieved through the collective involvement of several players in the real estate market. The potential roles of some of these players are discussed below.

The Construction and Business Bank (CBB)

This is the nation's pioneer bank in the mortgage industry dating back to the early 1970's. Over the years, it has played an important role in extending housing loans that have been invested in the building of thousands of residences. Currently, the CBB has a serious limitation in capital to reach more customers/potential house builders. To enable the bank play an expanded role in the housing market the Government will need to invest more capital in it and increase its capacity to extend loans to potential home builders.

If the Government chooses not to proceed with privatisation, the bank can also serve as a clearing house for the government to provide low-cost housing to poor households at highly subsidized rates. However, given the current inflationary pressure on the economy largely spurred by heavy investment in public construction (mainly roads and big dams), this may not be sustainable in the long run.

Commercial Bank of Ethiopia

This is by far the nation's biggest and most powerful bank. It has vast resources at its disposal controlling the lion's share of the banking sector––nearly 50 per cent of the total bank capital and business coverage. In addition, it has huge reserves of liquidity which can be harnessed for the real estate market in the country. With such a huge potential, there is no doubt that the Commercial Bank of Ethiopia (CBE) can be an important player in the growth and expansion of the housing finance sector in Ethiopia. A change of policy by the government combined with innovative leadership by bank management is needed to enable the Commercial Bank of Ethiopia to be an active player in the mortgage finance market.

However, a policy change by the government is needed to involve the Commercial Bank of Ethiopia to engage in the mortgage business. This means that the current constraint that prevents CBE from engaging in mortgage housing finance must be lifted. As was discussed earlier, the recent change of policy to involve the Commercial Bank of Ethiopia in mortgage finance of condominium houses is a good start in the right direction. Not surprisingly, other lenders have not been attracted to this arrangement because of subsidized interest rates charged by CBE.

The Private Banking and Insurance Sector

In Ethiopia, the private banking and insurance sectors have made considerable progress in a relatively short period of time. In a span of less than 15 years, this sector has managed to control nearly 50 per cent of the banking and insurance industry. As was discussed earlier, its participation in the real estate market at present is very limited for several reasons, including, as was discussed earlier, lack of experience, less profitability and risks associated with long-term financing. This has to change in favour of an expanded role by the private sector.

There is a shortage of capital for investment in the housing sector as the only bank that specializes in the provision of housing finance is the Construction and Business Bank. Moreover, the commercial banks favour short-term loans. The low degree of penetration of formal housing finance institutions means that the housing financing sector has a minimal impact on the development of the broader financial system.

The lack of functioning mortgage markets in Ethiopia impedes the emergence of both savings institutions and long-term financing facilities. Risk bearing financing is provided in other countries by venture capital institutions, which are non-existent in Ethiopia. In the short to medium term, therefore, it is unlikely that such institutions, which are capable of mobilizing substantial resources to finance the housing sector, will be developed in Ethiopia.

At the same time, the Government should encourage the participation of private banks in the mortgage market.

Possibilities for addressing this situation include Government guaranteeing their loans, and the sale of the land after careful assessment of its market price. These will diminish the risk factor and thus encourage private banks to enter the mortgage industry.

Micro-finance Institutions

Currently, there is a burgeoning micro-finance industry throughout the country. This sector has about a million loan clients and its outstanding loan portfolio in 2003 stood at more than $513 million. It has also amassed savings of more than $515 million as of 2007. A sector with such huge potential can make a significant contribution to the growth and expansion of the housing finance sector in Ethiopia. As was discussed earlier, the sector currently advances small loans to poor and low-income home builders at interest rates (i.e. 10-12 per cent) far below the inflation rate estimated at about 30 per cent.

Land and property rights

A number of comparatively simple changes will improve the land market and management.

- Leaseholders should be given the comfort of compensation rights if leaseholds are not renewed.
- Cadastral systems should be introduced to identify and map land holdings.
- Professional skills in land management and valuation need to be developed.

These measures will assist in the development of a market in land which, in turn, will give banks increased confidence in using land as collateral.

On the subject of the real estate investment climate, given the situation of the Ethiopian economy, the GOE should seriously consider whether there really is any trade-off between: (i) increasing real estate investment by reinforcing property rights of lessees and (ii), trying to retain a complete control on what is built. In our view, there is no trade-off as the restrictions are so constraining as to discourage overall investments and not just certain types.

The Bertaud et al (undated) report cited above states that international experience indicates that rarely is such a trade off available. Indeed, the real trade off is not even between more land use control vs. more investments, but between increasing illegal land developments vs. increasing legal ones. In Ethiopia, as everywhere else, attempts at tighter control of land markets will result in increasing illegal developments not more orderly development.

The same report suggests that the Land Development Agency of the Municipality of Addis Ababa (LADAA) should modify its land pricing system, and base it on capitalization of notional rents. Prices should also be linked to permanent tangible site features, such as location, width and quality of adjacent roads commercial potential, etc.[28] However, it recommends that developers should be allowed to increase density as much as there is demand for it. This would create a better incentive to save land as it would automatically decrease the price of land per dwelling unit while keeping the price per square metre constant. By developing large areas of government controlled land and fragmenting it into small residential parcels, LADAA land development schemes should have a quick and very positive impact on the land market. If the pricing system could be simplified and the standards revised, LADAA land schemes should allow the vast majority of urban households to participate in the land market.

Financial Policies

Ethiopia should adopt a housing policy to facilitate the development of housing for all income groups in various forms of tenure. Subsidy policies for needy households should be part of the general social security system of the country. At present, the government's intent to provide housing to the poor and low-income has missed its target despite the good intentions of the government. For example, the condominium houses meant for the poor and low-income are being taken up by middle and upper income households and individuals.

Financial sector liberalization with particular reference to the banking sector is an issue that needs to be given urgent attention by the government. Before launching such a scheme, the mode and pace of such financial liberalization measure has to be a matter of serious policy discourse. In this connection, two critical factors with a

[28] For pricing and site design we recommend reading the World Bank report "Efficiency in Land Use and Infrastructure Design" available at Http://www.worldbank.org/urban/publicat/inu17.pdf

potential to constrain Ethiopia's financial development need to be pointed out. One is the closed nature of the Ethiopian financial sector in which there are no foreign banks. This has generated a non-competitive market structure and strong capital controls in place. The other is the dominant role of state-owned banks. Ethiopia's economic development will benefit from financial sector liberalization, especially from the entry of foreign banks and the partial privatization of state-owned banks.

Currently, conventional financial institutions, be they either government or private, do not seem to be able to service the needs of the urban poor as regards housing and neighbourhood development. So it appears that presently only MFIs have potential to effectively respond to their concerns. Efforts should therefore be undertaken to enhance financial institutions which have built their success on providing working capital loans to the urban poor and small enterprises to expand and diversify their products to loan financing for home improvement and progressive building. Efforts should also be directed at promoting small-scale landlords to produce cheap rental accommodation through a variety of innovative incentives, such as supplying land at low and highly subsidized prices.

As of December, 2003, there were 753,022 loan clients of MFIs. The outstanding loan portfolio during the same period was $610 million while the balance of client savings was $334 million. The overwhelming majority of active clients are rural and loans are predominantly agriculturally focused, aimed at food production and food security. When evaluated by sustainability and outreach, MFIs are efficient but unprofitable, because lending interest rates of all MFIs do not allow them to cover their operational costs. There is resistance to increasing rates on the grounds that the activities of the poor are not profitable enough to cover higher interest rates. Nevertheless, MFIs have mobilised a significant amount of savings from the poor that can be a potential source of investment in the supply of housing.

There is an encouraging level of political commitment to addressing the issue of inadequate housing in Ethiopia. Despite the good will however, the government lacks the mechanisms and resources for the implementation of a solution that casts it in the role of developer and deliverer of housing. Among other things, the cost is simply too great given the problems of affordability that low income households face. Hence, it becomes necessary that the government take on more of a facilitative role, focusing on the regulatory framework in which development is to take place and addressing the issue of land in a manner that ensures long-term tenure security, particularly for poorer households.

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