Overview

Ethiopia is the second most populous country in Africa with an estimated population of more than 100 million people. Ethiopia’s economy has been growing fast over the last 15 years, averaging 10.3 percent a year from 2006/07 to 2016/17. However, the country’s real gross domestic product (GDP) growth decelerated to 7.7 percent in 2017/18 mainly due to political instability.1 The government has a high development orientation, and ambitious development projects coupled with elevated public investment and credit. The country’s public debt was estimated to be 57.2 percent of GDP in the fiscal year to 7 July 2019.2

Although Ethiopia was considered one of the least urbanised countries on the continent, this has been rapidly changing. The rate of urbanization, which was 5.8 percent between 2007 and 2012 is estimated to be 5.1 percent in the period between 2012 and 2017;3 major cities such as Addis Ababa, Adama, and Hawassa have recorded growth rates of 4.5 percent, 8.3 percent, and 8.9 percent, respectively.4 These growth rates mean that the country will move from an urbanisation rate of 20.4 percent to 22 percent recorded in 2017 to a projected 38 percent by 2037.5 Ethiopia’s cities are characterised by little formal planning, and rapid rate of urbanisation continues to put substantial pressure on housing, public consumption and public investment explain the demand-side construction, and services, accounted for most of the growth in the last two decades. Private consumption and public investment explain the demand-side growth, with public investment assuming an increasingly important role. Some effort has been made to improve the role of the private sector in the economy in recent times through a national initiative led by the Prime Minister’s office aimed at improving the ease of doing business and opening up telecommunications to the private sector and the financial sector for foreign investors.

The construction sector, which accounted for 12.5 percent of the GDP in 2018, has continued to grow yet remains fairly developed. Ethiopia’s growing population and rapid rate of urbanisation continues to put substantial pressure on housing, especially among the poor. Lower income households face two main barriers to owning homes: lack of affordable and quality housing stock, and the difficulty of obtaining housing finance. The unmet housing demand is estimated at approximately 1.2 million.7 The government’s Integrated Housing Development Program (IHDP) makes the biggest contribution to the housing stock in the country, followed by houses privately built by individuals. The real estate sector is in its infancy and contributes little.

Access to finance

Ethiopia’s financial sector has been tightly controlled by the state and excluded from foreign investment. No capital market exists and bonds are not widely traded. Government bonds are occasionally issued to finance government expenditure on mega projects or to absorb liquidity in the banking system. The National Bank of Ethiopia (NBE) is responsible for regulating banking and credit. Credit interest rates are charged on NBE directives of priority items/sectors. The NBE also sets the minimum lending, and a strict waiting list system to allocate foreign currency funds based on NBE directives of priority items/sectors. The NBE also sets the minimum interest rate for deposits (7 percent in 2018) but does not limit rates banks can charge for loans.
Banks and microfinance institutions are the main types of financial institutions in the country, and the main source of financing, particularly for the construction sector. The penetration of these institutions has over the last two decades increased, but still more than 80 percent of the population depend on informal sources of credit. There are 19 banks (18 commercial and one development bank) in Ethiopia serving a population of more than 100 million people. As at June 2018, there were a total of 4,757 bank branches. One study on Ethiopia’s banking sector noted that “as of 2018, [the sector had]—collected Br 730 billion in deposits (from around 33 million savers); provided Br 733 billion (33 percent of GDP) of total credit; handled close to US$10 billion in annual foreign exchange trading; employed 90,000 workers; delivered attractive returns to roughly 1.15 million shareholders; and contributed Br 13 billion in yearly taxes to the government (equivalent to roughly one-fifth of annual income tax receipts in recent years).”

The state-owned Commercial Bank of Ethiopia (CBE) dominates the banking sector partly because of preferential treatment from the government, such as its exclusive access to mortgage funding through the IHDP, and its long years of operation. CBE controls 66 percent of loans, 62 percent of deposits, 50 percent of capital, and just under 50 percent of profits in the sector. However, the share of private banks is increasing and they are becoming more competitive. In 2018, the share of the CBE in total profit declined to just 50 percent for the first time.

Yet the fledgling banking sector’s capacity to meet the needs of the private sector is still limited. Compared to banks in other African countries, Ethiopian banks are: “(1) much smaller in size; (2) very limited in their services; (3) heavily focused on lending instead of other income sources; (4) less burdened by non-performing loans; (5) carrying lower overhead costs; and (6) slightly more profitable – in ROE [Return on Equity] terms – than their peers.”

The banking sector is expected to grow and its contribution to GDP to double by the next decade. As part of the ongoing reforms in the country, the government has passed a bill that allows people living in the diaspora to invest in the finance sector, buy shares, and set up lending businesses. At least eight banks are being established, including one that is expected to specialise in loans to housing and construction projects. The government has shown interest in pursuing greater liberalisation of the sector by issuing a permit for the first foreign-owned company to lease imported equipment under local currency contracts.

Microfinance institutions play an important role in construction financing. According to the World Bank, the country had 37 microfinance institutions, with nearly 1,800 branches, 4.7 million borrowers and 16 million accounts as of March 2018. Although the microfinance institutions are intended to serve the financial needs of the poor, 80 percent of the poor depend on informal lenders, suggesting that MFIs can achieve greater outreach. Still, MFIs are better than banks in financing housing and construction projects, with at least 82–540 housing construction loans in the country, versus 6,728 loans by private banks, and total exposure of Br 2.8 billion (US$95 million). MFI loans are smaller and for shorter terms compared to banks. Loans offered by MFIs are cheaper with an interest rate of 14.3 percent a year compared to 17 percent charged by private banks, and they charge lower fees, mainly because they are partly financed through loans from government and non-government organisations with the prime intention of enhancing financial inclusion of the poor. However, the total amount devoted to loans for the construction sector is less than 10 percent and even less for housing. Access to finance for housing projects is limited and informal loan arrangements with friends and family is still the norm. A new housing mortgage bank under establishment could meet the high demand for affordable loans for house construction.

Mortgages
Since Construction and Business Bank stopped mortgage services in 1980s and was swallowed by the giant Commercial Bank of Ethiopia in 2016, no bank specialises in mortgages or loans to the construction sector. In a country where no more than 16 percent of the population receives a formal salary, collateral requirements leave only a few households eligible for mortgage loans. The World Bank estimates that mortgages represent only 1.87 percent of GDP of the country, small even by African standards. The government works with the state-owned CBE to provide mortgages to IHDP beneficiaries, to be paid over 15 years at 9.5 percent a year. As a result, CBE dominates the existing small mortgage market, issuing up to 69 percent of total mortgages through the IHDP. Private banks’ capacity to offer mortgages is constrained by lack of long-term funds, risks of non-performing loans due to low levels of income of urban residents and the high price of houses, lack of house supply, financial illiteracy, and growing out of the market by CBE. Thus, their mortgages are restricted to their own employees or well paid employees of large international organisations. Bank employees receive preferential treatment lower interest rates (7.7 percent versus up to 18 percent for regular customers) no or a lower down payment and longer amortisation periods (25 years versus 10–15 years for regular customers).

Furthermore, to resolve their shortage of hard currencies, most banks have launched a diaspora mortgage where diaspora members are expected to pay loans in US dollars, pounds or Euro. Thus, most bank mortgages are for their own employees or other well paid employees of non-governmental organisations and intergovernmental organisations. Overall, the Ethiopian mortgage market primarily serves upper and upper middle-income salaried households. Due to the requirement of salaried income or collateral, the percentage of non-performing loans is considered low.

Affordability
Affordability is a major issue in the housing market in Ethiopia. Most household incomes are too low to afford formal housing solutions – public or private. The problem of the generally low income of urban residents is exacerbated by costly construction material and unreasonably high land prices.

Opportunities to buy newly built IHDP housing are allocated by lottery. The size of the apartments built by IHDP varies from time to time and amongst the various programs. In the latest round of the lottery the average size of apartments varies between “a studio apartment (32m²) and a one, two or three-bedroom apartment (51, 75, or 100m², respectively).” The cost of construction for IHDP houses is Br 9.18 billion, excluding costs of finishing and infrastructure connection. If land costs, administration and compensation costs for people who occupied the land prior to the IHDP, as well as the cost of infrastructure is included, the average production cost per unit increases to Br 16.725 (against the approximately Br 10.000 winning households pay) which suggests a 40 percent subsidy. The downpayment required to be saved in the event of winning a lottery and the monthly contributions registrants need to pay exceeds a household’s annual consumption many times over.

Unlike traditional subsidised social housing lottery, winners are free to rent out their apartment at market rates but not allowed to sell them before five years from the date of taking ownership of the house. Thus, once they have won the lottery many people rent out the houses at a better price and generate revenue to pay the mortgage. Due to this and other reasons, therefore, only 46 percent of lottery winners move into their apartments. The increase in interest in this public housing scheme should not be considered as affordability of the scheme but rather be seen in the context of the expensive nature of other options. As

Availability of data on housing finance
Agencies compiling and reporting data on housing finance include: National Bank of Ethiopia (NBE), the Central Statistics Authority, and the Ministry of Urban Development and Construction. Although Ethiopia’s statistical capacity is higher than the Sub-Saharan average, data on the housing sector is severely lacking. The NBE neither disaggregates data by sector nor compiles important housing sector data such as the total value and number of mortgages. The most recent population and house census was conducted 11 years ago. Furthermore, most of the available data is inconsistent and not available to the public. Secondary data collection is difficult as the websites of the Ministry of Urban Development and Construction are down, while the website of the Central Statistics Agency and National Bank of Ethiopia are not updated regularly and slow to respond.
things stand, only the upper income groups, and members of the Ethiopian diaspora can afford formally constructed housing in Ethiopia. Due to limited opportunities of accessing land formally, squatting settlement is one affordable way of owning houses at less than market prices. This comes with a risk of demolition by administrators. Informal houses are, however, the dominant types of housing in the country.

**Housing supply**

An estimated 1.2 million housing backlog exists in the country with a projected demand of 635,800 housing units during 2015-2025, far exceeding the estimated annual supply of housing of about 165,000 units nationwide between 2007/2008 and 2013/2014. A study conducted in 27 cities in 2014 showed that the IHDPS supplied the most houses (52 percent) followed informal house building (31 percent), individual self-built housing (2.5 percent) real estate (0.3 percent) and municipalities (0.3 percent). With the country’s socialist background, cooperatives’ houses, which generally tend to be better quality, used to play a bigger role in house delivery, but their role has diminished recently and has been replaced by the government’s IHDPS.

The IHDPS condominium scheme is currently the dominant government-initiated housing programme in urban Ethiopia. The IHDPS arrangement allows residents who lived a certain period in a town and do not already own a house to make one application per household, and start monthly savings contributions towards a dedicated account to be used to cover the mortgage down payment if they win the lottery. More than 383,000 condominium units have been constructed and distributed under IHDPS between 2004 and 2018. Most of these units have been constructed in Addis Ababa (314,000) with the rest being constructed in other major cities (69,000). Of these units, over 245,000 have been transferred to beneficiaries, the number of IHDPS households is estimated at 182,000 in Addis Ababa and 62,300 in other cities.

Most of the existing housing stock is low quality. “Approximately 72 percent of households in large cities live in dwellings constructed out of ‘Wood and Mud’ (chikka), while about a quarter of households live in housing constructed out of ‘Cement or Stone’. A high proportion of households living in informal houses do not have access to basic social services.

Rental houses also meet a substantial demand. Most of the inner cities in most urban centres are houses owned by the government and rented to residents at a comparatively low fee. Although these houses were constructed during the past socialist regime and are old, their number is significant. The government is building 1,700 rental houses in Addis Ababa alone while similar initiatives are either being considered or already under way in other regions. Recently, the government has increased the price of rental houses for businesses by up to 1,500 percent in Addis Ababa. The government justified this move as a way of creating a competitive environment between businesses that rent government houses versus those who work from houses rented by private owners. Private sector real estate developers have so far played a limited role in the housing sector (less than 0.3 percent).

**Property markets**

Ethiopia’s rank on the Ease of Doing business index improved to 159 in 2019 (from 167 in 2018). It registered the best score (ranked 60) in enforcing contracts and scored worst in protecting minority investors (178). The Prime Minister’s Office has a dedicated initiative for improving the ease doing business. Property values have been increasing. While inflation plays a big part in the increase, higher consumption power among the emerging middle class, speculation, and irrepressible corruption play their own role. As cities expand, land that is not normally part of the cities is used for housing construction. Speculation on the land to be included into the city dramatically increases the value of the land, which in turn increase the value of property built on it.

**Policy and regulation**

Government policies have focused largely on ownership of houses through the IHDPS with substantial subsidies benefiting the lucky few. The IHDPS is too expensive for people living in smaller towns. As a result, there is a decline in demand for the IHDPS houses in some cities. The targeting error is high, and intended beneficiaries are not getting the houses. Questions also arise about the loss of social capital as people move to neighborhoods where they are unlikely to know any of their neighbours due to lottery system for distribution of the houses. Although the government prefers demolition and rebuilding high-rise houses, upgrading existing houses could be a way of maintaining the social network of people while viably providing affordable housing.

Public ownership of land has constrained the development housing market in the country. First, due to the absence of a dedicated land administration agency and insufficient staff, the country lacks a proper land administration mechanism. This absence of clear land title deeds and security creates difficulties for financing housing construction. Second, the private sector cannot obtain the required amount of land to construct houses. Third, land distribution has become a source of corruption. The price of urban land is high due to speculation, and lack of clarity on how to distribute and manage it. As a result, land for house construction is scarce. Although the Ministry of Urban Development and Construction is the main agency responsible for housing at the federal level, the role of different agencies at local and regional levels is unclear and overlapping.

**Opportunities**

The rapidly growing demand for houses is an opportunity to invest in the sector. The demand for housing in Addis Ababa and regional cities where the emerging middle class lives and migrates to is particularly a potential market for investors. The reforms being undertaken to liberalise the financial sector, coupled with reforms to improve the ease of doing business in the country are expected to

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Source: https://www.cgidd.com/C-GIDD, 2019
advance the climate for investment in the housing sector. The government has committed to reducing the housing shortage and recently showed interest in enhancing the role of the private sector in supplying houses. The promised specialised housing bank could be a game changer for access to credit for housing construction. However, the political situation is still volatile and continues to affect the investment climate.