Country Report

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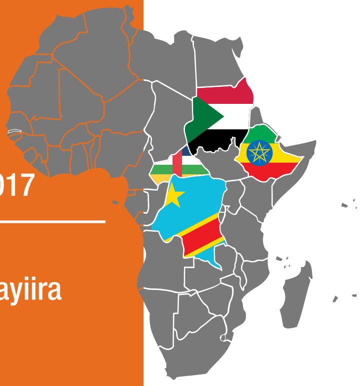

Centre for Affordable Housing Finance in Africa

ETHIOPIA

LANDSCAPE OF INVESTMENT

BACKGROUND

This country report forms part of The Centre for Affordable Housing Finance's Investor Programme which aims at addressing key information asymmetries on who, why and how investments are made in the African housing sector. With the intention of identifying and championing increased investment in affordable housing, the report includes insights and analysis into the depth and breadth of investment in Ethiopia's housing and housing finance sector. The overall goal of this project is to quantify the breadth of investment activity with respect to housing and housing finance across Africa, and to establish a mechanism to track this on an ongoing basis. This project has collected data and highlights gaps and opportunities in the investment landscape. With the aim of stimulating greater investment in affordable housing and connecting investors with potential investments, the report profiles investors and investment instruments with the greatest impact on the housing finance market in Ethiopia.

Growing financial sector experience and increasingly sophisticated financial instruments are driving Investor interest in African real estate. This includes new market opportunities related to a rising urban middle class, an increasingly localized construction material industry and innovations in housing finance such the emergence of Real Estate Investment Trusts and mortgage liquidity facilities across Africa.

However, a key barrier to this growth remains the chronic lack of rigorous data on the breadth and character of financial infrastructure investment. This is particularly true for the housing sector as stimulating targeted investments requires highly differentiated data that illustrates market segmentation. In providing market intelligence that makes the case for investment in underserved markets (segmenting and quantifying the demand side; and scoping, understanding and tracking the supply side), we can support a better policy environment & increased private sector activity in affordable housing markets. In this way, we catalyse scale interventions.

Without this data, targeted interventions become challenging and result in unresponsive housing finance packages, the high occurrence of Non-performing loans (NPLs) and poor uptake of new residential developments.

The Centre for Affordable Housing Finance in Africa (CAHF) is a not-for-profit company with a vision for an enabled affordable housing finance system in countries throughout Africa, where governments, business, and advocates work together to provide a wide range of housing options accessible to all. CAHF's mission is to make Africa's housing finance markets work, with special attention on access to housing finance for the poor. We pursue this mission through the dissemination of research and market intelligence, supporting cross-sector collaborations and a market-based approach. The overall goal of our work is to see an increase of investment in affordable housing and housing finance throughout Africa: more players and better products, with a specific focus on the poor.

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PROFILES OF INVESTORS

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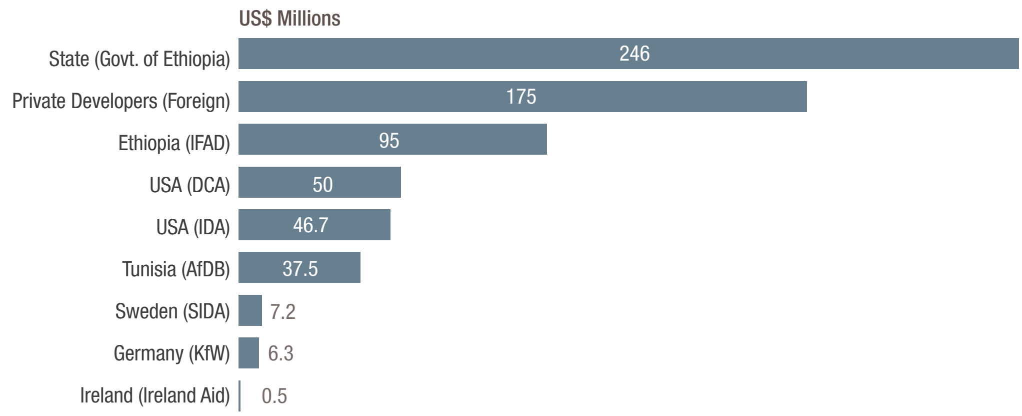
The dominant investor is the Government of Ethiopia. Since 2005, the Government has implemented the IHDP. The IHDP is entirely financed by public resources, through the CBE - the only independent financial resource for the housing programme in Ethiopia. In 2011 the CBE had provided US$ 246 million in bonds to the government, receiving a return of US$ 153 million. At the time of writing this report, the housing programme had not received any donor funding (the program has not been financed by any external donation either in the form of loan or aid from any of the bilateral and/or multilateral donors). Though acclaimed in Addis Ababa and few larger cities, implementation of the program was suspended in the other regions because lack of adequate financing from the national bank of Ethiopia. Also, low effective demand and low ability of beneficiaries to pay the down payment and the monthly mortgage (principal and interest) led to its suspension. By January 2014, over US$ 800 million was earmarked for the housing projects in cities across Ethiopia, however, these funds were never released to implement the IHDP.

Institutional Investor, Location and Total Asset Allocation to Housing Investments in Ethiopia (2000 - 2017)



Source: Institutional Investors' Annual Reports (2000 – 2020)

Foreign institutional contributed US$ 418 million (more than 50 percent of the total portfolio) in the period 2001 to 2017, intermediated through commercial banks and MFIs. The biggest source of investment was from international private developers (from China, UAE, Qatar, etc.), followed by Ethiopia (IFAD) and USA (DCA and IDA). Ireland contributed the least investment (US$ 0.5 million), intermediated through micro finance institutions, at interest rates ranging between 1.5 percent and 4.5 percent, for a period of 10 years.

Investment Activity in the Ethiopian Housing Industry

This sections analyses the different investment tools targeting the housing and housing finance sector in Ethiopia, their investment horizon and the period of investment.

How the IHDP Works

The CBE is a government owned bank, whose mandate is to provide finance for commercial purposes allowing municipalities to purchase bonds in order to finance the implementation of the IHDP.

The city of Addis Ababa, sells bonds to the CBE to finance construction costs. The Bank provides funding for the total cost of the program's implementation in Addis Ababa and in the regions. The Bank also provides a loan-service to all condominium beneficiaries, whereby the Bank pays 60, 80 or 90 percent of the unit price on behalf of the beneficiary at the handover of the property (the beneficiaries, depending on economic level, pay the remaining per cent down payment themselves) and the families enter into a loan-agreement with the CBE to pay back this amount subject to interest.

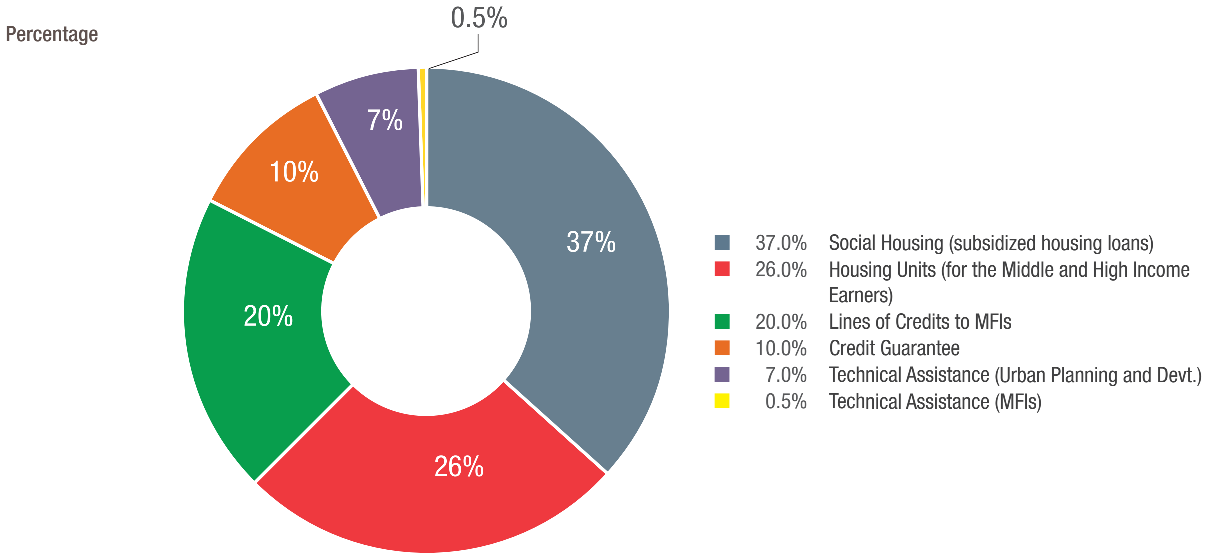
Source: National Habitat Report 2014

Top Performing Investment Tools

Social housing (through the IHDP - low cost housing program) constituted about 40 percent of the instruments/tools used to invest in Ethiopia's housing and housing finance sectors. The initial goal of the IHDP was to construct 400,000 condominium units, create 200,000 jobs, promote the development of 10,000 SMEs, enhance the capacity of the construction sector, regenerate inner city slum areas, and promote homeownership for low income households. Although the program has not met its original targets it has built 171,000 housing units to date. Housing units by international property developers constituted about 30 percent of the investment tools/instruments.

Credit guarantees constituted 13 percent of the instruments/tools invested in Ethiopia housing and housing finance sector. DCA (US $50m) and SIDA (US$7.2m) provided credit to Enat Bank, to partially guarantee loans to SMEs. SMEs in Ethiopia play an important role in the housing sector as importers of housing construction materials. The package also included technical assistance to Enat Bank and borrowers' cover under the guarantee, through training in business management and development. KfW (US $6.3m), IFAD (US$95m), AfDB (US$37.5m), Ireland Aid (US$506,128), have provided partial credit guarantee and technical assistance to MFIs with a funding horizon of 3 years. Lines of credit constituted 27 percent of the tools invested in housing. USAID and SIDA further signed another loan portfolio agreement (US$10m) with Enat Bank under the Portfolio Risk Sharing Loan instrument. This agreement allowed Enat Bank to cover up to 50pc of losses on a US$10-million-dollar loan.

Top Investment Tools for Housing



Source: Annual Reports of Institutional Investors

Investment Horizon and Period (Timeframe)

In the period 2005 – 2015, the average horizon, for top performing investment tools targeting the housing and housing finance sector, in Ethiopia, was less than 10 years. The horizon, matches the average tenor for social housing finance products by the Governments and credit guarantees (7 years). The only challenge, is that the institutions providing long-term funds are few.

Investor, Investment Asset, Investment Tool, Activity, Horizon and Period

Investor	Funds and Intermediary	Investment Tool	Horizon	Period
GoE	US$ 246m via CBB and CBE	Housing loans to CBB,CBE and MFIs	Since 2005	Since 2005
DCA	US$ 50m via Enat Bank	Credit guarantee and Technical Support	3 years	2005 -2008
IDA	US$46.7m via CBE	Addis Ababa Urban Devt project	7 years	2002 – 2009
IFAD	US$ 95m via MFIs	Equity and credit funds for MFIs	7 years	2011 – 2015
AfDB	US$ 37.5m via CBE	Equity and credit funds for MFIs	7 years	2005 – 2012
SIDA	US$ 7.2m via MFIs	Partial(50%)Credit guarantee and technical Support to MFIs	3 years	2005 – 2012
KfW	US$ 6.3m via MFIs	Loan guarantee to MFIs	3 years	2006 – 2009
Ireland Aid	US$0.51m via MFIs	Technical Support to MFIs	3 years	2006 – 2009

Source: compiled by Consultant from various online sources

Impact of Investments on the Ethiopian Housing Industry

The Breadth and Depth of Housing and Housing Finance Products on the Market

Properties (Housing Units)

The annual housing shortage is estimated at about 250,000. By 2025 the population of Addis Ababa is expected to reach above 4.1 million with average household size of about 4 members. While Addis Ababa had 798,000 households in 2015, it is expected to rise to 1,000,000 households in 2025.

Presently, a significant number of Ethiopians (particularly low and lower middle income groups who constitute more than 50 percent of the population and earn between US$200 and 400) build their houses through formally registered housing co-operatives that obtain loans from the CBB. Ironically, over 50 percent of the middle and higher income households (who constitute 20 percent of the population and earn between US$ 1,000 and 2,400) choose not to borrow, but prefer to finance housing out of personal savings, to avoid debt and the complexities of the mortgage system. Building incrementally, and financing construction from savings and current income, is the normal method used in the construction of informal housing. About 30 percent of the population build houses informally. Financing for housing is leveraged through "edirs" and community savings schemes with close to 400 million ETB (US$50 million) currently saved in credit unions which can be mobilized towards housing and infrastructure improvements.

In spite of the above, from the table below, property developers, were only able to reduce the annual housing requirement by about 5,000 units, in the period 2014 to 2017.

Output vs. Annual Housing Requirement in Ethiopia

Property Developers	Units delivered in Year/s			
	2014	2015	2016	2016
Ayat Real Estate	240 units	160 units	200 units	400 units
Enyi Real Estate	-	70 units	78 units	500 units
Sunshine Real Estate	30 units	60 units	50 units	90 units
Tsehay Real Estate	-	-	323 units	400 units
Habitat New Flower Homes	-	70 units	100 units	150 units
Ropack International	-	-	50 units	80 units
Ambassador Real Estate	-	100 units	120 units	160 units
Gift Real Estate	80 units	100 units	160 units	300 units
Flintstones Homes		100 units	220 units	350 units
Total	**350 units**	**560 units**	**1,301 units**	**2,430**

Source: Consultant's mini-survey of Selected Property Developers in Ethiopia

Housing Finance Products

Commercial banks in Ethiopia favour short-term loans (about 5 years). The low degree of penetration of formal housing finance institutions means that the housing financing sector has had 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.

A significant portion of Ethiopia's population (over 65 percent) don't have access to basic, affordable and sustainable financial services. This is largely due to the perception by commercial banks of the unattractive risk-return outlook of serving the low income urban and rural population. This, together with the high demand for bank loans in the mainstream economic sectors of the country, has created a comfort zone for the existing commercial banks, leading Ethiopia to be one of the least banked countries in the world. Data from the National Bank of Ethiopia suggests that the country has a ratio of total population per bank branch of 112,000. As a result of these factors, more than two third of the population of Ethiopia has resorted to traditional, informal and expensive financial services such as money lenders, keeping cash at home, funeral funds etc.

Opportunities/ Challenges to Deepening and Broadening of the Investment Landscape in Ethiopia

Challenges

From an investment perspective, key challenges constraining deepening and broadening of the investment landscape in Ethiopia include:

- Ethiopia does not have a securities market, and sales/purchases of debt are heavily regulated. GOE is drafting legislation to regulate the over-the-counter market for private share companies. Moody's rated Ethiopia's credit worthiness a 'B+', while S&P and Fitch gave it a 'B'. GOE offers a limited number of 28-day, 3-month, and 6-month Treasury bills, but prohibits the interest rate from exceeding the bank deposit rate. GOE began to offer a one-year Treasury bill in November 2011. Yields are below 2 percent. This market remains unattractive to the private sector and over 95 percent of the T-bills are held by the state-owned Commercial Bank of Ethiopia and public enterprises.

- Access to finance impedes domestic private investment. While credit is available to investors on market terms, a 100 percent collateral requirement limits the ability to take advantage of business opportunities. The April 2011 measure forcing non-government banks to invest the equivalent of 27 percent of each loan in National Bank of Ethiopia (NBE) bonds contributed to liquidity shortages that further reduced the ability of banks to lend to the private sector. This requirement was however receded in Ethiopia financial sector reforms.

- According to Eden Sahle, "Much of the private real estate operators are competing based on location and the type of housing they plan to erect. In terms of price, almost all of them offer a one storey house on a 250sqm plot (small size) for up to ETB 2 million, on a 500sqm plot for up to ETB 4 million, and on a 1,000sqm plot for over ETB 6 million. Almost all commit to complete and hand over homes within 24 months, although hardly any of them have managed to do so…" There are over 630 large scale real estate investments in the country with over 80 foreign direct investors in real estate sector, with investment capital of over ETB 3.5 billion(US$175m)-(Samson Berhane). Beside the limited capacity to timely deliver on their projects, private delivers are affected by inflation that keeps construction material costs increasing during the project cycle hence facing budget shortages. Even at the low end of the residential housing market (homes of 250 square meters), prices are generally above the ETB 1 million (US$50,000) mark. With respect to houses in the 500 square meter range, prices are generally in the range of ETB 2- 4 million (US$100,000 – 200,000). At the high end, covering homes with 1000 square meters and four or more bedrooms, average prices rise to as much as ETB 6 millionUS$300,000) and in upscale neighbourhoods average prices are as high as ETB 10million(US$500,000).

- Since 2006, the government has channelled housing finance through CBB for on-lending to individual borrowers and Microfinance Finance Institutions (MFIs) across the nation. However, following government's removal of subsided interest rates, the lending rates increased from (i) 4.5 percent to 7.5 percent for MFIs/Cooperatives and (ii) 4.5 percent to 16 percent for individual borrowers; each following the market – led adjustments. This has further contributed to the growth in the housing deficit currently estimated at 250,000 units per year and subsequent low physical quality characterizing the current state of the housing sector in Addis Ababa.

Opportunities

The Commercial Bank of Ethiopia and the Development Bank of Ethiopia (both government owned) are increasingly being recognized in the commercial construction industry, for their modest interest rates (9-10 percent) and the 10 year tenor for developer finance. Private Banks have also ventured into the housing finance business, providing loans as short as five years, at interest rates as low as 5%. Awash International Bank S.C, Dashen Bank, Bank of Abyssinia, and Oromia International Bank are few of the 18 private commercial banks offering construction finance to large and modestly sized residential property developers.

The partial liberalization of the housing sector has been possible, thanks to a shift in policy, premised on a market-oriented system to housing development. For the past two decades, housing development has undergone a significant paradigm shift, from the provision/supply of heavily subsidized residential housing, to interventions that are dictated by the market. Historically, the CBB was the sole provider of mortgage loans to home builders. By 1995, the CBB had given out subsidized mortgage loans at below market interest rates to a tune of US$42 million for the construction of 26,912 residential houses. 14,881houses (55.3 per cent) of the total units built, were built by borrowers with a monthly income below US$52 demonstrating the key role CBB played in financing the middle income group of society for housing construction.