

## Ethiopia: Options for Expanding Affordable Housing Supply for Industrial Park Workers

### Summary Note



### Context

Ethiopia has registered high levels of economic growth, averaging 10 percent per year over the last decade. To sustain GDP growth at double digits, industrial and export-led growth has become the central focus of the Government of Ethiopia (GoE), as acknowledged by its Growth and Transformation Plan. A key strategy used by the Government to transition to a manufacturing led industrialization is the establishment of Industrial Parks (IPs) to attract investors, mobilize workers, and create the necessary enabling environment for investment.

Industrialization goes hand in hand with urbanization: Ethiopia has one of the fastest growing urban populations in the world. The Ethiopia Urbanization Review (2015) estimates that Ethiopia is expected to be 30 percent urban by 2028 (nearly doubled from 17 percent in 2012). An unprecedented growth in urban population entails an unprecedented growth in demand for urban housing in Ethiopia. However, Ethiopia's housing sector is characterized by significant deficits, both quantitatively and qualitatively. Most household incomes are too low to afford formal housing solutions – public or private. And the country displays one of the highest levels of urban population living in informal settlements in sub-Saharan Africa (World Bank, 2015).

There are currently eight operational Government owned and operated IPs in the country and an additional seven under different stages of development. At capacity, these parks are expected to employ up to 1,500,000 workers. In most of the IPs, labor is predominantly migrants from rural areas, increasing the demand for local housing. For instance, as of 2019 the Hawassa IP has close to 24,000 workers and this number is expected to grow to 60,000 in the near future. More than 70% of these workers come from areas as far as 150km from the city.

To-date, housing shortage is regularly cited as one of the main constraints of workforce recruitment and retention in the IPs. There are multiple corollary problems associated with the housing situation as observed to date: (a) workers pay significant share of their monthly income on rent and are exposed to rental rate increases; (b) housing is of low quality and lacking access to basic services; and (c) safety and security issues, as women are exposed to attacks and harassment. All of these issues pose a risk for the sustainability and productivity of the IPs, including compliance concerns for the manufacturers and consumers.

The Industrial Parks Development Corporation (IPDC) and Ethiopian Investment Commission (EIC) have initiated various initiatives to tackle this affordable housing shortage for IP workers, including the Sidama scheme experimented in Hawassa.

## Objectives

This study aims to provide practical solutions for expanding access to affordable housing and infrastructure services for employees of Industrial Parks, and to recommend strategies and programs (including financing schemes) for the Ethiopian Government to support the recommended solutions.

Principles & Premises. Housing is largely a private good. As elsewhere in the world, government-led supply in Ethiopia is not meeting growing demand and cannot on its own. Government needs to enable and deepen the housing market to work by removing blockages in the entire value chain. IP housing challenges should be viewed in the context of local housing market dynamics, and solutions should be market-based, private sector driven solutions, and government subsidies are the last resort.

Methodology. The study investigates demand and supply side dynamics of rental housing markets in Addis Ababa and Hawassa – where the first IPs are operating and identifies key constraints in market-based affordable rental solutions. On the demand side, Workers Survey, household observations and Focus Group Discussions were carried out to gauge workers current living conditions, preferences for shelter, as well as ability and willingness to pay. On the supply side, interviews with key informants<sup>1</sup> on the supply side were undertaken.

A deck of slides with figures and graphs to illustrate key findings and recommendations were prepared to serve as key output of this study. This summary note serves to provide a brief narrative for policy makers to grasp the key findings and recommendations.

## Key Findings

### Demand Side

Young, predominantly female migrants seeking for bed rental with access to basic services

In both Addis Ababa and Hawassa, IP workers have largely resorted to informal rental housing supply, with limited access to basic services. This is largely attributable to the lack of affordable formal housing supply in the entire local markets. In fact, survey results have shown that IP workers

are not poor, but they are “cost-burdened” by rent. Access to drinking water, sanitation and good ventilation are top priority of IP workers surveyed, not shelter by itself. Security and safety are also raised as a concern. While workers prefer private accommodation rather than group accommodation, dormitory style housing was considered acceptable if all amenities are available.

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<sup>1</sup>Interviews with supply side players included IP Manufacturers, developers/contractors; private leaseholders, IPDC and Local governments, commercial banks, and Micro-Finance Institutions.

### Supply Side

Compound rental serves as de facto affordable housing supply for IP workers.

On the supply side, formal rental housing supply has been not affordable for IP workers. Compound rental, namely, rental properties built by existing homeowners in the compound have become the de facto affordable accommodation for them.

Potential suppliers of rental housing recognize the opportunities for IP workers but face significant constraints. While some IP tenant manufacturers have built dormitory for their workers, many others do not have such expertise or resource or access to sufficient serviced land. For developers, there is no appetite to own and run rental housing properties, and investments in rental housing for IP workers is perceived as very risky, due to the lack of clear off-taker, clear policy from the government, and overall limited access to serviced land as well as construction financing. For existing “de facto” rental housing suppliers, i.e., private “landlords”, they are interested in expanding their business, but are concerned with delayed payment by tenants, limited by the lack of financing to expand business and access to adequate infrastructure services (water, sanitation, drainage, etc.). Limited knowledge and trust of the financial sector also surfaced as a constraint. For local governments, IP workers rental housing provision requires significant financial commitment which they currently don't have. Similarly, IPDC lacks financial and technical capacity for IP workers housing provision.

### Relevant International Experience

Having similar socialist past and public land ownership regime with tradable land leases/land use rights, China and Vietnam provide relevant experiences as they have accumulated substantial experiences with housing delivery associated with industrial parks. In both countries, private room rentals have provided the largest share of the rental housing in the market and become the *de facto* affordable solutions. In China, the government first focused on its limited resources on infrastructure provision to those “urban villages” that hosted migrant workers. As Governments become financially and technical more capable, integrated solutions have been implemented, while park-village; park-private; govt-private developer partnerships have long provided a variety of practical solutions.

### Proposed Options

#### No One-Size Fits All

A menu of options are needed to rapidly increase market supply of rental housing.

There are a number of options that hold the promise of expanding market supply of rental housing. Each option represents different production volume per hectare, which requires different levels of technical (design, construction, and

property management), financial, and institutional capacity, as well as different time frames. There is no one sizes fits all. Solutions need to be thought-through and customized based on the local housing market dynamics and the availability of capacity (technical, financial, and institutional) required by each option.

### **Option 1. Dormitory/Shared Apartment**

The option of multi-story dormitory or shared apartment (G+4 and below) holds the potential for mass production, as it generates the greatest number of beds per hectare compared with other options. However, the high-cost of construction of such structure renders it not affordable to majority of the IP workers, even if the land is allocated by the local government or IPDC at a deeply discounted rate. Therefore, building such dormitory is not a viable business for developers and their investors. However, both international and local experiences have shown that governments, by allocating additional land for developers to build housing for sale at market rate, can make it financially viable. This can be done through Public-Private-Partnerships (PPPs). Based on preliminary cashflow analysis, such modality can reach the IRR targeted by developers.

Nevertheless, this dormitory option also requires significant upfront investments in infrastructure (basic and social services) given the scale and population density it entails. Moreover, a successful PPP transaction needs (i) an enabling policy, legal and regulatory environment; (ii) extended time frame and sufficient capacity – on the part of *both private and public sectors* – to undertake mixed-income, mixed-tenure, mix-use development. The modeling of a PPP arrangement with rental dormitory scheme in itself is very complex and costly, and that the GoE, particularly the Local Government must mobilize externally to ensure it is done with value for money.

### **Option 2. Housing Micro-Finance for Expanding In-fill**

This option is deemed as most practical in quickly enhancing supply, in particular, if focused on improving access to basic services. This modality in fact has already existed in Ethiopia, even outside the Sidama scheme. Its construction technology is simple; lower cost contractors are available locally; and capital requirements are much lower compared to other options. Overall, production and risks are more distributed, and transaction costs minimal.

While the Sidama scheme has been less successful largely owing to its “top-down” approach which lacks real understanding of the market dynamics, the fundamentals of Micro-Finance providing home improvement or extension for rental purposes are sound. It is akin to the SME loan, as the assets are income generating.

However, is there a business case for housing micro-finance to “homeowners” to build ILO-compliant rental units in compound? The analyses have shown that, middle ground can be found, with modest subsidies. It is critical to focus on the most urgent needs, namely, access to basic water, sanitation, and good ventilation, not just the structure.

### **Option 3. Sites and Services**

This scheme requires sufficient institutional and technical capacity, albeit less demanding compared to PPPs. In a typical sites and services (S&S) scheme, local Government sub-divides publicly owned land and makes serviced plots available (in different sizes) for individuals/households to construct housing incrementally, appropriate to affordability constraints. For instance, on a 96m<sup>2</sup> plot, a dwelling may be developed starting with a single room (and washroom) and adding rooms as the family grows, or as there is need to create rooms for rent. While this scheme may not add to the rental housing supply as quickly as the infill option, scaling up delivery of small housing plots for incremental housing development coupled with proper neighborhood planning has the potential to deliver on inclusive and livable communities that are integral part of a growing city.

#### Option 4. Formalizing Informality

This option is essentially a land readjustment/pooling (LR/LP) scheme in a peri-urban area. In LP/LR schemes, the original landholders or occupants voluntarily contribute their land to the government or other project initiators. The government then plans out the whole area with roads, infrastructure, open space, and public facilities. In return, each landholder receives a serviced plot of smaller area, but often at a much higher value within the same neighborhood. This is because of the infrastructure and the fact that the plot can now be legally developed. Some parcels can be set aside for public auction and sold to recover the costs of developing infrastructure.

Recognizing that in Ethiopia, government has the sole power to convert rural land for urban use in form of expropriation, such LP/LR schemes will help make rural to urban land conversion more inclusive by giving the farmers the opportunity to stay (albeit likely to be on a smaller plot) and continue to derive their livelihood from rental income. It helps preserve the existing rental supply and bring in essential basic services to ensure public health and safety.

**Table 1. Comparisons across the four options**

	DORMITORY	INFILL	SITES & SERVICES	FORMALIZING INFORMALITY
Number of workers potentially served/ha	High	L-M	Medium	Medium
Affordability	Low	High	Medium	Medium
Infrastructure needed	Substantial	<ul style="list-style-type: none"> <li>Limited upfront</li> <li>Substantial in future</li> </ul>	<ul style="list-style-type: none"> <li>Medium upfront</li> <li>Substantial in future</li> </ul>	<ul style="list-style-type: none"> <li>Medium upfront</li> <li>Substantial in future</li> </ul>
Implementation complexity	Substantial	Easy-Medium	Medium	Substantial
Time required	Long	Short-Medium	Medium	M-L

#### Policy, Financial Support and TA are Needed to Kick-Start and Scale up All Schemes

There are a number of cross-cutting issues that are essential for all schemes to achieve needed scale to meet the increasing demand for workers housing.

##### Pre-condition 1. Financing for Local Governments to provide serviced land

The ability of local government to (i) provide primary or secondary “off-site” infrastructure to the boundary of the site for the PPP, S&S, and LR/LP schemes; and (ii) upgrade infrastructure and basic services in the infill and formalizing informality options is a critical pre-condition for most of the schemes to work. Even more importantly, except for the infill and the formalizing informality schemes, supplying land for PPPs and S&S likely entails resettlement of existing permit or land lease holders. Therefore, the local government must have the resources and capacity to engage all stakeholders, ensure proper compensation and provide grievance redress services.

##### Pre-condition 2. Instruments to make IP workers renter of choice

Due to the fact that formal supply falls short of demand, IP workers are effectively competing in the local housing markets for rental units. Introduction of measures to improve their payment capacity or their prospects for generating steady and certain rental income for prospect landlords is critical. Such measures may be in the form of rental guarantees, or rental vouchers, which can be financed, at least partially, from IP tenant manufacturers.

### Pre-condition 3. Appropriate institutional set up and capacity

For each of the option, there is an underlying institutional vehicle required, with different degrees of complexity and transaction costs involved. For instance, for the dormitory option to truly deliver affordable rental units, a new investment and development vehicle will need to be established to secure finance, build, manage and maintain the rental facilities over a long period of time. It is largely a PPP scheme which requires substantial financial, technical and property management know-hows on the part of both public and private sectors. For the infill option, while it can rely on existing institutions and systems, their capacity for underwriting Housing Micro-finance (HMF) loans are yet to be built up. In addition, the success of the HMF loans also warrants the introduction of an institutional function of quality assurance for home extension.

### **Next Steps**

To enable ample supply of the affordable and adequate rental housing to meet the rapidly growing demand by workers employed in the existing and pipeline IPs, the Government of Ethiopia need to deliberate and decide upon the following:

#### Immediate-term

1. Reach consensus among key stakeholders on an appropriate worker housing standard.
2. Ministry of Urban Development and Construction (MoUDC) to support IP hosting cities to design and implement a program to support urban infill for rental housing, with a focus on introducing incentives for existing land lease holders to add rooms with access to basic services, and technical assistance to ensure that minimum housing standards are met.
3. MoUDC to support IP hosting cities to design and pilot PPP schemes (mixed-income, mixed-use, mixed-tenure) for affordable rental housing provision for IP workers.
4. MoUDC to support select IP hosting cities to pilot Sites and Services schemes
5. GOE to adopt integrated approach to housing solutions (transportation, social services, cultural and sports amenities), starting from integrating IPs into city's structural plan and infrastructure investment plan.

#### Short to Medium-term

6. Scale up urban infill rental program
7. Scale up sites and services schemes
8. Implement affordable housing PPP schemes
9. MoUDC to support select IP hosting cities to pilot inclusive urbanization through land readjustment /land pooling (regularizing informality)
10. GOE to better align federal and local interests and incentivize City-Park, Region-Park Partnership, with particular focus on how local government can be better resourced for the supply side to function, including resettlement compensation, infrastructure provision, etc.
11. Review and introduce policy reforms to address systematic constraints in the market
  - a. Unlocking land supply through more market-based allocation
  - b. Sustainable infrastructure financing