Microfinance institutions and urban housing in Addis Ababa: challenges and prospects for sustainable poverty alleviation

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Abstract

This study focuses on the performance of micro finance institutions (MFIs) in sustainable housing poverty reduction for the majority urban poor in Addis Ababa, the capital city of Ethiopia. The paper assesses the impact, challenges and prospects of MFIs in transforming the urban poor residents' livelihoods through the provision of Housing Microfinance (HMF) loan product. From available data, Addis Ababa Credit and Savings Institution (AdCSI), an MFI with a customer base of 120 000, diversified its product lines to include the HMF loan product in 2006. Although findings indicate that the loan is popular with most urban poor residents, MFIs are failing to meet the demand mainly due to lack of loanable funds. As a way forward, the government through partnerships with the private sector needs to integrate MFIs into the broader financial system so as to address the financial needs of the low income people who can not be covered by commercial banks, particluarly in accessing the money to pay the 20% down payment for condominium houses. Similarly, most MFIs operating in the city need to diversify their loan products to include housing loans to tap into the lucrative market by extending the HMF loan to their clients.

Keywords: Micro Finance Institutions, Micro and Small enterprises, Housing, Urban Poverty, Outreach, Challenges, Responses, Realities, Addis Ababa.

Introduction

Most urban residents in the developing world (Asian, Latin American and African continents) live in slummy or extremely precarious environments that are invigoratingly marked by epiphenomenal deteriorating infrastructure and services. Although different schools of thought, such as the Marxist, the

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conservative and liberal approaches[2] view housing provision differently, there is common consensus that housing is a basic necessity for human survival, just like food and clothing. The 1948 Universal Declaration of Human Rights and the 1996 Istanbul resolution proffer that housing is a basic human need and as such all people, the poor inclusive, deserve a home where they and their families can live in security and comfort (UN-Habitat, 1996).

This paper argues that MFIs and their HMF loan products play a significant role in cushioning out the urban poor who are faced with critical financial paucity in Addis Ababa, as commercial and government banks fail to reach them, and therefore should be given greater attention than they are currently receiving. It begins by giving background information about the housing situation in Ethiopia and the historical development of MFIs. It goes on to present the concept of housing finance and presents the research findings, highlighting the valuable contributions of HMF loans to the country's overarching objectives of housing the city's urban poor. Finally, the paper wraps up by proffering recommendations for the future endeavours in urban poor housing and emancipation. It concedes that there are still certain gaps which need to be bunged if the government is to improve the effectiveness and efficiency of MFIs as their quest to alleviate the high prevalence of urban poverty and daunting housing shortages in all its urban centres, Addis Ababa inclusive.

Background information to the study

Ethiopia is one of the fast urbanising countries in the world and Addis Ababa, its capital city, accommodates about 26% of the nation's urban population (MoWUD, 2008). About 120,000 new residents are added to the city every year and the continuous and massive inflow have aggravated the housing problem because the absorbing capacity of the sector is too low to accommodate the influx (AACG, 2006). In the pursuit of accomplishing

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[2] The Marxist approach believes in the socialist perspectives where housing provision is the preserve of the state. The Conservative approach is where housing provision is left out to the forces of demand and supply, whilst the government plays a minimalist role. The Liberal approach is where there is multi–stakeholder participation in housing provision as well as community involvement.

Millennium Development Goals (MDGs), particularly goals (1 and 7)[3], and the government adopted a number of strategies and legislations to promote economic, social and physical development of the country.

The government approved the operations of MFIs through the issuance of the microfinance legislation in 1996 (proclamation 40/96) with the aim of availing financial services such as micro loans, micro-saving, money transfer and leasing to the poor (Peck and Johannes, 2009; Wolday, 2008). To foster holistic development of urban areas, the government formulated and endorsed the Urban Development Policy in 2005 to guide and support accelerated and equitable growth. It is this policy that informed the origination and subsequent espousal of the Integrated Housing Development Program (IHDP) in 2006, which aims at delivering adequate and decent housing, mostly to low income people who are currently living in slummy conditions as well as job creation and revitalisation of economies in the country's urban areas (MoWUD, 2008).

Statement of the problem

Ethiopia desperately needs standard houses for its urban poor. It is the only asset the poor can own, have privacy and improve the low income people's standard of living through income generating activities. Besides the availability of land, finance is the other overarching resource in urban poor housing development and it is its availability and cost that matter most. Paradoxically, the country has very few formal financial institutions and they have over the years proved to be incapable to serve the urban poor (Peck and Yohannes 2009). The few commercial banks and private housing developers are only providing financial services to the rich (middle and upper market segments) neglecting the poor and government sources only reach a few urban poor. The poor although they can win the lottery to take up government constructed condominium houses fail to pay up the 20% down payment and the houses are offered to the next person on the waiting list due to lack of finance (ECSC, 2008). Even if they access land through organised co-operatives, the poor fail to finance the development of their plots and end up selling to the rich, thus forfeiting their rights to own a basic human need. The shortage of housing finance that is affordable to the majority urban poor is most worrisome that the participation of the relatively new Ethiopian

[3] *Millennium Development Goals 1 and 7: (1) eradicate extreme poverty and hunger; (7) Ensure environmental sustainability and specifically target 11 of improving the quality of lives and reducing the number of slum residents.*

microfinance institutions, in housing finance provision to the urban poor deserves research attention.

Objectives of the study

This study focuses on the provision of HMF loans to low income households by MFIs that emerged in Addis Ababa around the 1990s, initially and primarily to supply micro enterprise finance to the disadvantaged members of the community such as women, the youths, the unemployed and the disabled. Using AdCSI as a case study, the paper looks at the role of the loans in housing poverty alleviation and the challenges that are being faced by the MFIs serving the poor. Specifically, it examines the role and performance of HMF loan products being offered by AdCSI in Addis Ababa, assesses the challenges it faces, identifies the prospects of HMF loan products to MFIs and finally, puts forward possible solutions to the challenges and offers guidelines aimed at supporting MFIs willing to add HMF loan products to their loan portfolio.

The methodology

Employing the case study approach, AdCSI, an MFI that operates in the capital city of Ethiopia, Addis Ababa, was studied. The MFI was chosen as it is currently the largest MFI operating in the city, with over 120 000 customers and a very wide loan portfolio than all the other players in Addis Ababa. A total of 70 interviewees participated in the study, and it included 30 randomly selected HMF loan product customers from three sub-cities of Bole, Yeka and Lafto, 30 randomly selected beneficiaries of condominium houses from the same sub- cities, four purposively selected AdCSI key informants, three key informants from Association of Ethiopian Micro Finance Institutions (AEMFI) and three experts from Addis Ababa Housing Development Project Office (AAHDPO). A two stage data collection procedure was undertaken. The first stage entailed stratifying customers of the MFI to focus only on HMF loan product customers separating them from customers that were not the subject of this study. Secondly, within the HMF loan product customers cluster, random sampling techniques were employed to select respondents in order to gather data about the role and performance of the loan in urban poor housing. Urban poor beneficiaries of condominium houses, particularly studio and one bed roomed houses (meant for the poor according to AAHDPO officials) and co-operative housing members were also interviewed to gather their views about HMF loan products. Semi-structured interviews were conducted with AdCSI, AAHDPO and AEMFI officials to gather information about the role and performance of HMF loan products, challenges being faced and their views about what could be done to ameliorate the situation. Reviews of documents and texts such as AEMFI publications and AdCSI reports were also done to get proper positions of MFIs in advancing financial support for urban poor housing. The urban poor financial needs and capacities of MFIs were used as the basis for exploring gaps to be filled and options to expand their businesses and operations by catering for the urban poor's housing development and ownership aspirations. The challenges highlighted throughout the field studies were also used to proffer suggestions on how relevant stakeholders can help both the urban poor and MFIs in their quest to improve lives in Ethiopia's urban centres.

Conceptual clarifications

Finance plays an integral role in housing production as it filters through the whole housing development process, from land acquisition to putting up the housing structure (Gumbo, 2005: 20). The sources of housing finance in most developing countries generally fall into three categories or tiers and can be taxonomised as conventional/formal, semi-formal and informal. Conventional sources of housing finance can further be categorized into public and private sources. Experiences have shown that public finance is rather inadequate to remedy the housing problems of the poor, whilst the private sector is infamous in avoiding the urban poor as they can not afford to borrow money from these institutions due to lack of collateral security, lack of steady income, perceived high default risks and high transaction costs (Chipungu, 2005). NGOs also deliver financial services to the poor directly as part of their poverty alleviation programs, although they have had a positive impact in developing flexible methodologies that fit the needs of the poor in their development programs, they only complement other players efforts due to shortages of resources.

Semi-formal financial sources have traditionally been dominant in meeting the financial and social needs of the poor in most developing countries (Johnson and Rogaly, 1997). In Addis Ababa, local financial institutions such as the *iquib*, *iddir* and *mahiber* are common. They lend money to their members at very low interest rates with no restrictive conditions. However, loan sizes per borrower from such institutions are very low, for example the average loan size was Birr 269 per client in 2005 (AEMFI, 2006).

Informal sources of finance include savings, informal loans from money lenders, remittances from friends and relatives working abroad and the sale of assets they have for example jewelry and furniture. Informal lenders have relatively flexible loan terms, but their interest rates are very high.

Evolution of housing microfinance

Since their inception in the 1980s, HMF loan products have grown considerable and have attained a prominent position among organisations addressing the shelter needs of the urban poor in many cities of the developing world. They have responded to the needs of un-banked and under-banked people in society. They include credit cooperatives, NGOs with an urban poverty focus, and MFIs. Increasingly, HMF is a loan product offered by established MFIs and they implement a broad spectrum of housing initiatives. They consist mainly of loans to low-income people for home improvements and renovations or expansion of existing homes (UN-Habitat, 2005).

There are two conflicting explanations to the origin of HMF loan products. The first approach advances that it started as initiatives for small and micro enterprises to expand the economic opportunities for socio-economically and politically mariginalised group.

From micro enterprise to housing microfinance

Early micro finance lending was solely meant for enterprise development. As enterprise lending was expanding in the mid 1980s, MFIs expanded their portfolio to offer specialised HMF loan products for home improvement and new housing construction (Dowla and Alamgir, 2003: 972). Significant growth and innovations in HMF loan products have largely been recorded in the Asian and Latin American continents since the initiative started. The expansion to include HMF loans is largely attributed to the strong connection between home and income generation within their customer base. The clients operate home-based enterprises hence investments in housing improvements essentially constitute investments in their income generating schemes. Besides, MFIs observed that their clients borrowed for income generation purposes and channel the funds into housing improvements, thus adding a room for commercial use or expanding the space needed for income generation. Productivity of food processing enterprises was also improved through diverting micro enterprise loans to infrastructure provision such as water supply and improvement of kitchens. The replacement of traditional materials with permanent building materials helped to improve the health of the clients; hence MFIs expanded their services to include loans for housing improvements for their clients with more flexible credit where they could decide optimal allocation of resources according to priority and need.

From housing rights advocacy to housing microfinance

The second approach advances that housing microfinance loan products were initiated basically by the preserve of the Non-Governmental Organizations (NGOs) that worked in housing and urban development (Schreimer, 2000: 15). The approach evolved from advocacy activities that sought to defend the rights of the poor to equitable access to land, housing infrastructure and services. The organisations later expanded into HMF loan products to help the poor access housing, since their underlying belief was that shelter is a basic human right. Currently a large number of MFIs scattered around the world are adopting best practices in HMF loan products and are successfully delivering the much-needed services to housing customers. However transaction amounts involved are normally small.

Empirical analysis and discussion results

MFIs in Addis Ababa generally offer services to informally self employed urban poor people and also formal employed low income households. According to available data there are more than nine MFIs that are operating in Addis Ababa. AdCSI is by far the largest MFI in the city, with a membership of 120 000 active clients in the ten sub cities of Addis Ababa.

Table 1. MFIs in Addis Ababa and loan products offered

Serial Number	MFI	Type of Loan Products	New Products to be Offered	Period in Operation
1	AVFS	MSE, Agriculture and construction loans	-	10,5 Years
2	ADCSI	MSE , construction and Housing loans	-	9 Years
3	Gasha	MSE and consumption loans	Consumption loans	11 Years
4	Meklit	Agriculture , MSE and consumption loans	Construction loans	9 Years
5	SFPI	Agriculture and MSE loans	-	12 Years
6	Wisdom	MSEs Loans	-	10 Years
7	Agar	MSE loans	-	
8	Digaf	MSE loans	-	4 Years
9	Metema men	Agriculture loans	-	7 Years

Source: Wolday 2008, AEMFI Pamphlets & www.aemfiethopia.org

Most of the MFIs operating in the city have been in business for almost ten years, indicating relatively adequate experience with financial services that may call for diversifications of loan portfolio to include HMF loans.

Addis credit and saving institutions (AdCSI) case study

AdCSI is an MFI that operates within the boundaries of Addis Ababa City Administration. It was established and registered with the National Bank of Ethiopia in January 2000 and is owned by six shareholders that include Addis Ababa City Administration, Addis Ababa Women, Youth and Teachers Associations, Karaalo Akababi Hulegeb Peasants Co-operative and a single individual. Besides pursuing the primary objectives[4] of every private business, the MFI seeks to reduce urban poverty and unemployment and to become a model urban MFI not only in Ethiopia but also in Africa.

[4] The four basic primary objectives of private business undertakings in their order of importance include: Profit maximisation, Business Growth, Customer Satisfaction, Social responsibility in order of importance and priority that should be given by a business.

According to the general manager of the MFI, AdCSI has currently three main sources of funds which include, loans from the city administration (one of the stakeholder), own equity and savings. The MFI diversified its loan portfolio in 2006 to include housing microfinance loans after realising the lucrative market in the city. The MFI offered Small loans suitable for significant housing improvements, addition of new rooms and or new house constructions. Table 2 below shows the characteristics of the housing microfinance loan products that are offered by AdCSI.

Table 2. Key features of ADSCI HMF loan products

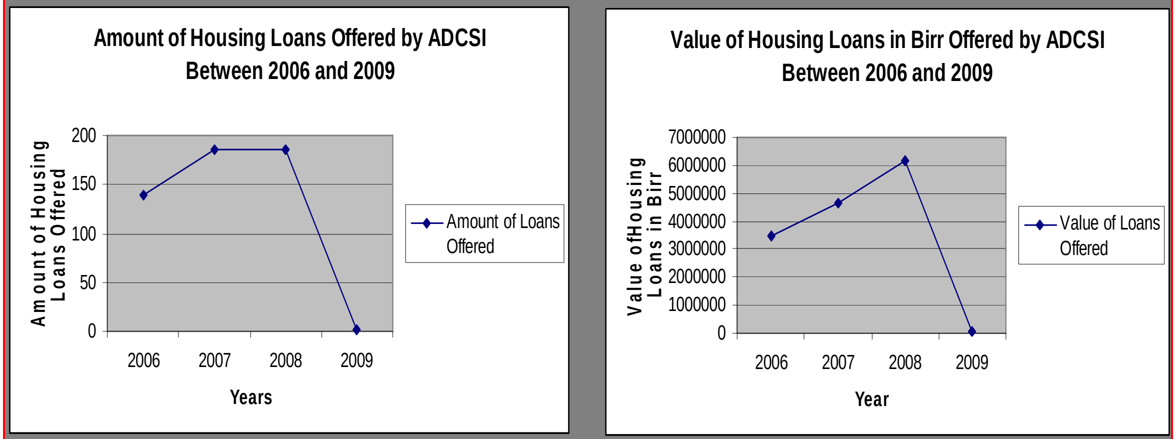
Loan sizes/ Limits	Varies but offers a Maximum of Birr 50 000
Loan Duration/Term	5 Years
Interest Rates	10 % Declining
Collateral	House under construction or maintenance
Target Clientele	Residents of Addis Ababa, with land or houses to be maintained and secure tenure
Delivery Method	Always provide to individuals rather than to groups
Other Services	Follow up by officials to check on construction progress

Source: Own Survey, 2009

Loan sizes depend on the applicants' monthly income. According to table 2 above, AdCSI can give a maximum amount of Birr 50 000 depending on the applicant's income. It should be noted that the maximum loan size for housing is considerable smaller than that of MSEs that have a maximum of Birr 250 000. The loan product has a maximum period of 5 years and security conditions include the title of the house under construction or maintenance, or the use of co-signers. The emphasis of the loans is very much on improvements of home and adding rooms, hence loan terms and conditions favour those who already have some degree of tenure security and housing structures. Currently the MFI is only extending HMF loans to individuals, this means that there is no grouping lending for this loan product.

Figure 1 below, presents the yearly amounts and values of HMF loan products that were extended to the urban poor between 2006 and 2009. From 2006 to March 2009, the institution offered a total of 512 HMF loans to the urban poor for home improvements, room additions and new construction. The loans had a total value of 14 358 200 Birr.

Fig 1. Amounts and Values of Housing Loans Offered by AdCSI between 2006 and

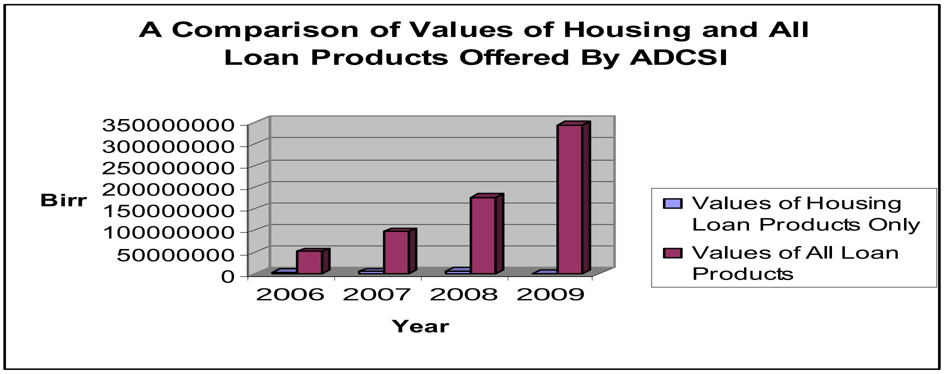


Source: Own Survey, 2009

The value of loans increased from 3 492 900 in 2006 to 6 176 500 in 2008, but fell dramatically to only 63 000 Birr in 2009. This was attributed to shortages of loanable funds. Similarly, the amount of loans rose from 140 in 2006 to 185 in 2007 but remained stagnant in 2008 before falling dismally to only 2 loans in 2009. The same reason was cited for the tragic reduction of loan amounts. It should be noted that AdCSI suspended its housing loan product in March 2009, although the loan product had received overwhelming support and demand from the customers for almost four years. The suspension was attributed to shortages of loanable funds, since the MFI had not received any financial support from the commercial bank of Ethiopia in the past two years.

Although lack of loanable funds have been cited as the sole reason to adequately finance HMF loan products, figure 2, below helps to diagrammatically show the lacking spirit to allocate more resources to HMF loan products by the MFI. The values of housing and total loans are not comparable at all.

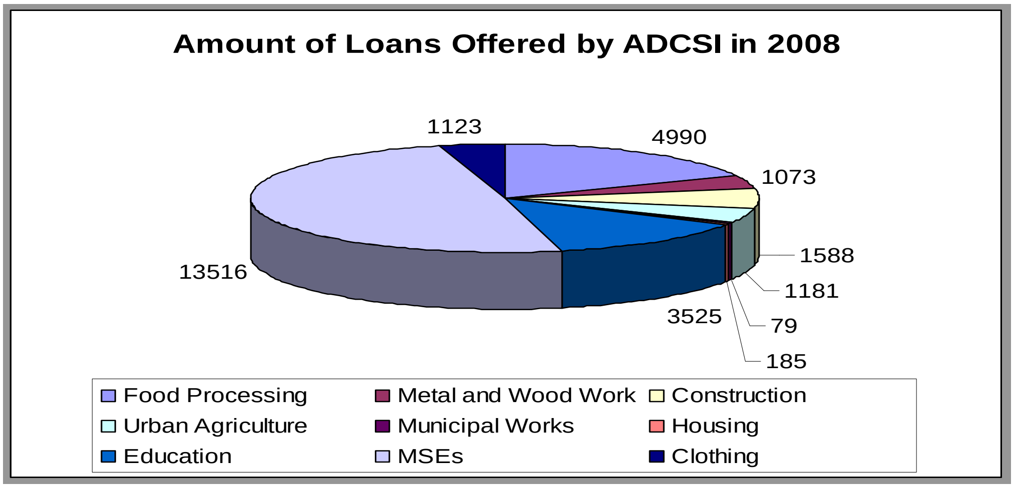
Fig 2. A Comparison of housing and total loan products



Source: Own Survey, 2009

The bars representing housing loans are barely visible due to low amounts of money allocated to housing development of the urban poor during the four years. The 2009 bar representing housing loans indicate that HMF loan products are at the verge of extinction in the city - a sad reality for the urban poor in Addis Ababa. Figure 3, helps to illustrate the amount of loans that were offered to the urban poor during the year 2008. It is sad to note that, in 2009 out of 23 667 loans, only 2 were housing loans and out of 343 178 932 Birr that was given out, only 63 000 Birr was allocated as housing loans by the MFI.

Fig 3. Amount of loans offered by AdCSI in 2008



Source: Own Survey, 2009

The graph clearly shows that housing the poor is not being prioritised even in the face of shortages of loanable funds; it is not regarded as a basic human need by the institution as it is not receiving the same treatment with other loan products.

Interviews that were conducted with HMF loan products beneficiaries from three sub-cities of Addis Ababa helped to reveal the impact of MFIs in housing financial support. About 30% of the 30 interviewed AdCSI clients used their loans to build new houses in various sub cities of Addis Ababa, whilst 45% of the studied clients said that home improvements had enhanced their family wealth and health and the remaining 25% used the loans to meet the 20% down payment for their studio and one bed roomed condominium houses in the city. Overall livelihoods have improved as the improved houses have in turn been used for income generation from their small businesses, with clients willing to repeat borrowings to further extend or improve their houses. The case study revealed a clear correlation between poverty and housing. However, some respondents were concerned about the small loan amounts they were given by the MFI. A sizeable number of clients did not manage to finish their housing structures due to the small maximum loan amounts of 50 000 Birr. The challenges of failing to complete housing improvements or developments were also attributed to inflation that rose sharply between 2006 and 2007, forcing the prices of building materials to rise significantly.

Challenges faced by MFIs and clients

Although HMF loan products have proved to be effective in improving the housing conditions of urban poor people, there are many challenges that are being faced by both MFIs and their clients.

Challenges Faced by MFIs

According to interviews conducted with AdCSI officials and their source documents the critical problem faced by MFIs is limited and unreliable sources of funding. The main sources of finance are equities (contributions from the six mentioned stakeholders) that are mostly inadequate, followed by savings that are rarely enough to cover the demand of housing loans. According to AEMFI officials that help in networking MFIs with suppliers of finance, there is limited debt financing as loans from commercial banks are not guaranteed due to lack of collateral. Currently, MFIs finance 40% of their assets with equity due to challenges of attracting funding from commercial sources (Peck and Yohannes, 2009). The other challenge that was highlighted by officials from AdCSI concerns the collateral demands by the Commercial Bank of Ethiopia in the form of physical assets such as buildings and vehicles, which most MFIs do not own. Besides adequacy, the other challenge concerns the period of loans to MFIs by commercial banks. Whilst HMF loan products need to be funded with capital that matches their longer term structure, if finance is available, MFIs are only given short term loans of less than 5 years by commercial banks whilst HMF loan products are of long term in nature, sometimes ranging between 5 to 10 years thus resulting in term mismatches (AEMFI, 2008).

Discussions with AdCSI managers also revealed that lack of formal proof of land ownership by the poor, is a challenge for MFIs who are willing to diversify into housing microfinance loan products. Although formal land titles may not be necessary in housing microfinance, land security is very essential to the MFIs. MFIs can only extend financial services to the urban poor when they are confident that the clients will be allowed to enjoy the benefits of their investments and consequently repay their loans. The other challenge is inflation that has been eroding the value of monetary assets of the MFIs. Inflation has been rising in the past five years, causing a lot of suffering to MFIs. Inflationary pressures increased financial expenses considerably and accounted for approximately 30% of MFIs’ total expenses after adjustments (Peck and Yohannes, 2009).

Challenges faced by clients

The major challenge to the urban poor is lack of affordability due to their low incomes. Interviews with the low income people revealed that some who could have benefited from the loans were not willing to be indebted for long periods thus resulting in their reluctance to participate in the HMF loan products. However, the results revealed some urban poor who were willing but could not benefit due to lack of secure tenure as MFIs demanded formal proof of ownership of houses in the city and the poor did not have the title deeds to cede as collateral for the loans. Inflation emerged to be the other challenge that is faced by the poor HMF loan product customers as their loan values were being eroded before they could finish their housing structures. The scourge has been on the rise for the past four years (Peck and Yohannes, 2009). The poor are then forced to make unnecessary repeat borrowings or use part of their savings to complete the projects, thus adding unnecessary costs and burdens.

Prospects for MFIs in housing financing

There are brighter prospects for MFIs to be integrated and mainstreamed into the broader financial system and participate in different housing provision approaches for low income housing. Since low cost housing for the poor can either be directly provided by the government, or indirectly by co-operatives and poor individuals who participate in assisted self-help approaches, the MFI can capitalize on such developments by partnering with the government and the urban poor in finding solutions to the housing problem (Amha, 2000: 3).

The other potential role of shelter micro finance is within more comprehensive slum upgrading programmes of which more than 70% of housing in Addis Ababa is slum (MoWUD, 2008). There is also potential in funding the poor who are benefiting from the Addis Ababa low cost condominium housing program. The MFIs have greater prospects of extending loans to the poor to pay for the 20% down payment, for example according to officials of the AAHDPO, a three bed roomed house requires only 29 730 Birr as down payment and have a total price of 148 680 Birr . If compared to MSEs loans that have a maximum loan amount of 250 000 Birr, the prices of these houses are relatively low such that MFIs can dominate the financing of the program and realise considerable profits from the scheme.

Conclusions and recommendations

AdCSI has proved over the past four years that housing investments are more directly linked to income generation. It has demonstrated that HMF loan products do not only alleviate poverty, but also lead to economic growth due to intrinsic linkages between housing provision and overall development in the wider economy of city, as housing improvements have positively impacted on the businesses of informal traders in Addis Ababa. The improved houses and added rooms are now being used for storing wares for small businesses. However research findings reveal that a lot still needs to be done to introduce and sustain HMF loans, since MFIs specialising in micro business lending have been very slow or unwilling to diversify their loan portfolios and offer HMF loan products to fill a niche for the low income households that commercial banks have failed to fill. MFIs operating in the city need to change their current view of HMF loans as consumption to that of investment, a secure and well constructed houses aid not only the well being and health of poor families but also to break the vicious circle of poverty.

The urban poor revealed that they still depend on informal lenders who charge exorbitant interest and the Construction and Business Bank (CBB) is only extending mortgage loans to middle and upper income groups. Part of the problem has been shortages of loanable funds as for the case of AdCSI that was forced to suspend its HMF loan product after four years of successfully offering without any problems from the urban poor. There is therefore need for the government, donors and commercial banks to partner and offer diverse funding options (grants, loans, guarantees, or a mix of all three) to MFIs, thus enabling them to expand into HMF loan products in a significant way because without reliable and streamlined access to commercially priced funds, they will never be able to diversify or sustain their loan portfolio.

Besides, a mixed bag of housing approaches should be adopted by the Addis Ababa City government which among others may include assisted self-help schemes to allow more flexibility in building and community help to keep the cost affordable, since the urban poor can afford to develop their houses incrementally according to their capacity, borrowing money in small batches from MFIs. There is also need to combine MSEs loans and housing loans so as to holistically develop the poor from all angles and develop not only their physical environments but their social and economic conditions. Failure to improve the poor's housing conditions renders all the successes of MSEs loans futile as the poor continue to live in squalid conditions. The worst is when the poor are forced to use their savings and income from their MSEs to service exorbitant housing loans from the informal money lenders due to an absence of well packaged and priced housing loans from their regular and reliable financial institutions - the MFIs.

In a city where more than 80 percent of the 150,000 government houses were constructed with mud and straw and are older than their estimated life of 30 years (MoWUD, 2008), the overarching goal of government policy besides direct construction of condominium houses, should be the development and support of housing finance mainly by facilitating the operations of MFIs, the only formal financial institutions that are accessible and affordable to the urban poor.

This indicates that the process is and requires an intricate and complex network and web of relationships between various organisations such as private developers, financial institutions for example MFIs and the state. The paper concludes by advocating for a more comprehensive and pluralistic approach to enabling housing strategies that include all related agents such as MFIs in expanding housing provision to urban poor groups.

The potential market in Addis Ababa for small housing loans is great. With adequate support and capacity building, MFIs can reach a large housing customer base in the city and consequently help to consolidate asset use for income generation and family well-being. Besides, they are best placed to generate excellent repayments, if innovative and appropriate credit modalities are applied hence HMF loan products can be a viable business for MFIs if properly applied in the untapped market. The urban poor require flexible and small loan arrangements which they can pay back and repeat the borrowings as their financial status improve.

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