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Project Information Document (PID)

Appraisal Stage | Date Prepared/Updated: 10-Nov-2022 | Report No: PIDA34576

BASIC INFORMATION

A. Basic Project Data

Country	Project ID	Project Name	Parent Project ID (if any)
Djibouti	P176772	Djibouti Affordable Housing Finance Project	
Region	**Estimated Appraisal Date**	**Estimated Board Date**	**Practice Area (Lead)**
MIDDLE EAST AND NORTH AFRICA	09-Nov-2022	20-Dec-2022	Finance, Competitiveness and Innovation
Financing Instrument	**Borrower(s)**	**Implementing Agency**	
Investment Project Financing	Republic of Djibouti - Ministry of Economy and Finance, in Charge of Industry	Agence de Réhabilitation Urbaine et du Logement Social (ARULOS)., Fonds de Garantie Partielle des Credits de Djibouti (FGPCD)	

Proposed Development Objective(s)

The project's development objective is to expand access to affordable housing finance for underserved populations

Components

Mortgage guarantee mechanism
Innovative financing of affordable housing
Policy Reforms, Institutional Strengthening and Project Management

PROJECT FINANCING DATA (US$, Millions)

SUMMARY

Total Project Cost	85.00
Total Financing	85.00
of which IBRD/IDA	15.00
Financing Gap	0.00

DETAILS

World Bank Group Financing

International Development Association (IDA)	15.00
IDA Credit	15.00
Non-World Bank Group Financing	
Commercial Financing	70.00
Commercial Financing Guaranteed	70.00

Environmental and Social Risk Classification

Moderate

Decision

The review did authorize the team to appraise and negotiate

Other Decision (as needed)

A. Introduction and Context

Country Context

1. With a total population of less than one million and one of the smallest overall surface areas on the African continent, Djibouti is a small, low-income country, but with a strategic geographic position in the Horn of Africa. Neighboring landlocked Ethiopia and other countries that do not have the same port infrastructure, its deep-water port allows it to be a hub for trade in the region. Its economy has long relied on port services, logistics, and rents from military bases. The main sectors driving Djibouti's economic growth are transportation, logistics, telecommunications, and banking.

2. In the two decades prior to the COVID-19 pandemic, Djibouti's economy was growing at a steady and stable rate of about 7 percent per year. The COVID-19 global crisis in 2020 and other shocks such as the War in Ethiopia (impact on logistics activity) and extreme regional drought dampened growth to 0.5 percent in 2020, which rebounded to 4.3 percent in 2021. Growth is set to soften in 2022 to 3.3 percent and expand in 2023 under new infrastructure projects. Inflation and the budget deficit have remained at controlled levels (1.8 percent and 2 percent, respectively) but the country is considered at a high risk of debt distress as public debt rose to about 70 percent of GDP.

3. However, growth has not been inclusive. Poverty affects one out of six people and inequality remains high. Djibouti's Gini coefficient was estimated at 0.416 in 2017, and the country ranked 71st out of 95 countries with information available on the Gini coefficient in 2015. A high unemployment rate contributes to inequality (28.4 percent as of June 2022, and 80 percent for youth between 15 and 24 years old). Compared to Djibouti City, the rest of the country faces higher levels of inequality due to marked differences in welfare levels among the main cities and rural areas. With the COVID19 pandemic, Djibouti's extreme poverty rate is estimated to have increased to 23–30 percent in 2020 (versus 15 percent in 2019) as households felt the effects of the pandemic through job loss and price shocks. The poverty levels affect the population's ability to access food and housing. Poor quality housing contributes to overcrowding, poor health and education outcomes.

4. Djibouti is highly vulnerable to climate-induced natural disasters, including extreme heat, multi-annual drought, and flash floods, and tropical cyclones. The capital Djibouti-city is particularly exposed to flash floods due to its location, low elevation and periods of heavy rainfall. The most recent episode in 2019 damaged numerous infrastructures and resulted to an official estimate of 40,000 households affected and more than 250,000 people displaced. Temperatures are also expected to rise by 1.9°C by 2050 and 5.4°C by the end of the century. Droughts affect mostly populations living in the rural areas, and the agricultural sector; between 2007 and 2011 a prolonged drought impacted around 120,000 people in rural areas (50 percent of the rural population), leading to an estimated economic impact of 7 percent of GDP. Tropical Cyclones increase the risk of coastal flooding. The low-income populations targeted by this project lack the resources to prepare and adapt to extreme weather risks and are likely to suffer the highest economic losses from floods, drought, and storms.

B. Sectoral and Institutional Context

5. Djibouti suffers from a structural deficit in the supply of affordable housing for low and medium-income households as well as households who work in the informal sector. In a context of fast-paced population growth and rising urbanization, housing production in Djibouti remains limited at around 3,000 units per year, of which about 2/3 is attributed to self-construction by households, and 1/3 to developers (both public and private). Private developers only produce high-end housing and are not involved in the affordable housing segment which is not commercially attractive. Investment in new housing has been limited in recent years which resulted in an important housing stock deficit estimated at about 30,000 units according to the Government.

6. Against this backdrop, significant and deliberate efforts have been made by the Government since 2013 to provide affordable housing and increase private sector participation via its *Agence de Réhabilitation Urbaine et du Logement Social* (ARULoS) and *Société Immobilière et d'Aménagement Foncier* (SIAF). The 2013 Law No. 13/AN/13/7th extended a number of benefits to developers of low-income housing, such as tax breaks on consumption tax, value-added tax and imports of construction materials, as well as a reduction of taxes on profits from social housing projects. In 2018, the government launched the Zero Slum Program aimed at containing the expansion of precarious and informal housing and improving access to basic urban and social services for families. ARULoS and SIAF produce social and economic housing as well as plots with legal titles. Djibouti Ville has about 30,000 legal titles. The more ambitious projections of the two Government agencies plan for the construction of 2,964 housing units in the coming years. Their major constraint remains the absence of financial solutions for marketing these housing units to the target populations (i.e. lack of housing finance for low to middle income groups).

7. The role of the private sector in the housing supply value chain is underdeveloped in Djibouti, despite the sector's significant potential for employment and growth.[1] Public sector production by ARULoS and SIAF has only reached about 25 percent of the formal supply, and without active participation by the private sector, housing needs will continue to exceed production. Informal production remains the main option available to most low-income households, in the form of self-construction, including on undeveloped land, thus contributing to the expansion or densification of slums.

8. The cost of housing production is high (over US$500 per square meter for mid-range housing). The high costs of construction materials sold locally added to restrictive licensing and import taxes on imported materials affect

[1] Data on private sector role extracted from the diagnostic report commissioned by the Government of Djibouti: "*Etude du marché du logement et promotion d'un habitat abordable à Djibouti*", EGIS, GRET, 2022 and interview with market players.

construction costs and leave little room for technical maneuver to lower housing costs. Only cement, gravel, and sand are produced locally, as the steel is imported in bulk and re-cut locally for the construction sector in Djibouti. Intermediate-type habitats are made of wood and sheet metal that are not produced locally. A very large part of the materials is traditionally imported from China, Middle East and India. The demand for cement and steel is therefore extremely high, with the cost of cement potentially impacting 50 percent of construction costs on systems combining masonry and reinforced concrete structures. However, imports of steel and cement are extremely restricted in Djibouti.

9. In addition to the high cost of inputs, companies face a lack of professional skills that affect their productivity and the quality of the output. To remedy this, in its new policy emphasizing vocational training, the Djiboutian Government provides for the gradual disappearance of technical high schools in favor of more specialized training centers, including a new center for professional building trades. There are also two private training centers associated with promoters who train young workers directly on their sites. If the training offer for workers and higher technicians is developing, training in project management remains limited to Djibouti despite the high demand.

10. Home loans are of strategic interest to most commercial banks. The size of their home loan portfolio is between 8 and 40 percent. Despite the virtual absence of an interbank market and the challenges of external refinancing, banks are particularly liquid, and all have large and stable deposits, which in most cases allow them to offer loans with long maturities (15 to 20 years) at interest rates of around 7 percent, compared with an average of 10 percent in Eritrea and Somalia and 12.5 percent in Ethiopia. The people currently benefiting from mortgage loans are generally civil servants or private sector executives, rather young, and favoring self-construction or purchase via new real estate development programs.

11. Despite the recent increase in activity, the mortgage market remains small and serves mostly high-income households. During 2018, banks granted nearly 1,000 new housing loans but access remains limited to households with a regular monthly income above US$1,500, so not for economic or social housing. The products offered for housing finance remain little diversified, with i) conventional mortgage loans (benefiting employees with a formal work contract who receive their salary in the financial institution) and ii) Islamic products. The Ministry of Housing (MVUH) estimates that it would be necessary to triple the current production of loans to reach at least 3,000 housing loans per year so as to finance the public supply of social and economic housing.

12. One of the consequences of the low penetration of the mortgage market was that ARULoS and SIAF had to set up and financially manage long-term (20 years) rent-to-own contracts in order to sell their housing units. ARULoS has about 2000 ongoing and future rent-to-own contracts and SIAF 1600, with interest rates around 3 percent. Those were originally built and designed to be sold, but ARULoS and SIAF could not sell them due to the low purchasing power of their clients. As a result, these agencies tie up their cash flow, to the detriment of their future activities as land developers and social housing promoters. Moreover, they are not equipped to manage such outstanding amounts because they are not financial credit managers. Residential leasing products with a purchase option are still non-existent and cannot finance outstanding rent-to-own agreements.

C. Proposed Development Objective(s)

Development Objective(s) (From PAD)

The project's development objective is to expand access to affordable housing finance for underserved populations

Key Results

- Number of low-to-middle income households benefitting from affordable mortgage loans partially guaranteed by the FGPCD
- Number of poor households benefitting from self-construction finance

D. Project Description

13. The Project aims to support the Government of Djibouti in its efforts to implement priority and necessary activities to create a minimum platform of conditions to develop access to affordable housing. Currently the lack of affordable and commercial housing finance solutions remains a major issue. Affordable housing supply is coming to the market through public developers, but buyers have no access to commercial financing due to the banks' risk aversion towards low-income groups. The project seeks to transition financial solutions implemented by public developers to the commercial financial system, and will:

- Expand access to affordable housing finance to underserved households through a mortgage partial guarantee mechanism
- Introduce innovative financing solutions for the self-construction of affordable housing targeting low-income households to involve microfinance institutions; and convert existing rent-to-own contracts to low-and-middle-income households into mortgage loans
- Support policy reforms to lower construction cost.

Component 1: Mortgage guarantee mechanism (US$7.5 million from IDA; US$70 million PCM)

14. Component 1 will support the capitalization of a partial credit guarantee fund for mortgage loans and related technical assistance. The fund will be hosted within the *Fonds de Garantie Partielle des Credits de Djibouti* (FGPCD), which will offer a new window dedicated to affordable housing loans. The eligibility criteria will be in the Project Implementation Manual and are expected to include: (i) loans to purchase an economic or social housing unit whose maximum price is currently established at DJF 10 million (US$56,251); (ii) minimum down payment between 5 and 20 percent as per good international practices; (iii) sound risk management and (iv) climate risk considerations. The guarantee will support households in the social and economic categories, earning between US$450 and US$1500 per month, and within the 6th to 9th deciles of the income distribution. Commercial banks will assess loan requests from potential beneficiaries, then submit applications to the FGPCD. The mortgage guarantee will allow commercial financial institutions to better share risk in order to finance mortgages for low- and middle-income earners and/or the self-employed. Banks will have to target a new category of borrowers since their average mortgage loans currently range between DJF 15-30 million (US$84,000-168,000). The FGPCD has adopted a new policy on environmental and social risks, which will guide banks on avoiding loans on properties that are exposed to climate risks such as climate-induced floods.

a. **Sub-component 1a:** The capitalization of a partial credit guarantee fund for affordable housing loans within the FGPCD (US$7 million).
b. **Sub-component 1b:** Technical support to the FGPCD, the financial institutions and the Central Bank of Djibouti (CBD) to implement the partial credit guarantee for mortgage loans (US$500,000).

Component 2: Innovative financing of affordable housing (US$5.5 million from IDA)

15. Component 2 will mobilize the financial markets in activities currently implemented by the public sector. It will help low-income households build their home through self-construction and gradually transfer this activity from the Government to microfinance institutions.

c. **Sub-component 2a:** Financial solutions to low-income households for self-construction (US$4 million), in two phases. Phase 1 (US$2 million) will provide additional financing to the successful self-construction program of ARULoS to help poor households rebuild their home damaged by climate-induced fires and regularize their property titles and will be open to any household registered in the electronic social register. Phase 2 (US$2 million) will provide a line of credit to microfinance institutions so they can extend a self-construction loan to their clients who are in the social register. The entire sub-component addresses climate vulnerabilities by ensuring that microloans finance the construction or renovation of homes that are more sustainable and incorporate climate adaptation features. All self-constructed homes will be certified for their compliance with national quality standards and their resilience to climate-induced floods and fires.

d. **Sub-component 2b:** Transformation of the rent-to-own contracts of low-to-middle income households into mortgage loans (US$1.5 million). This sub-component will seek to expand the mortgage market and support the pipeline for the guarantee fund by converting the rent-to-own contracts of ARULoS and SIAF into mortgage loans.

Component 3: Policy Reforms, Institutional Strengthening and Project Management (US$2 million from IDA)

16. This component will provide technical assistance to support policy reforms, the institutional strengthening of ARULoS and SIAF and project management. Analyses undertaken during preparation identify several policy reforms to open up the construction sector and lower construction cost, which is key to keep housing affordable. The component will provide technical assistance to prepare those policy reforms which will support the use of low-carbon material. ARULoS will need to provide significant support to poor households to manage their self-construction projects to ensure the sustainability of self-construction and attract the microfinance sector, including by facilitating access to site managers, quantity surveyors, land surveyors. It will facilitate trainings to ensure the self-construction meets resilience standards against climate induced floods and fires, and will advise on the use of insulating and low-carbon materials. Finally, ARULoS and SIAF will require expertise to convert the rent-to-own contracts into mortgage loans and efficiently manage the reflows; as well as resources for ARULoS' efficient project management.

Legal Operational Policies

	Triggered?
Projects on International Waterways OP 7.50	No
Projects in Disputed Areas OP 7.60	No

Summary of Assessment of Environmental and Social Risks and Impacts

17. The project's combined environmental and social risk is assessed as moderate. Location for houses potentially financed by component 1 and 2 will be in discrete sites, geographically spread out within cities, and consist of individual land plots to small clusters of houses. Hence, there will be no cumulative social impacts within the area of influence.

18. Potential impacts will take place in already developed areas where houses financed by components 1 and 2 are/or will be built. The likely environmental and social impacts that would occur during self-construction, include disturbance to the communities in the area such as noise, dusts, materials stocking, construction waste and access to the sites.

19. The project also entails risks associated with poor or non-transparent beneficiary selection, occupational health and safety risks associated with the structural integrity and locations of financed existing housing units or units to be built under project financing, properties, risks associated with civil works, such as poor labor conditions child and forced labor, as well as risks associated with sexual abuse and exploitation and sexual harassment. Moreover, the project may lead to the propagation and exposure to COVID-19 or other communicable diseases as a result of project activities. Therefore, most of impacts and risks are expected to be temporary, predictable and reversible, small-scale and site-specific. The project will not support housing development or improvement that will involve large-scale involuntary land acquisition and resettlement. Activities are not expected to be carried out in the sensitive areas. The risks and impacts are expected to be medium in magnitude and in spatial extent. There is medium-to-low probability of serious adverse effects to human health and /or the environment. Mitigation measures may be designed more readily and more reliable.

20. FGPCD and ARULoS have developed respectively an Environmental and Social Management System (ESMS) and Environmental and Social Management Framework (ESMF). FGPCD will have an environmental and social (E&S) focal point that will be responsible to supervise the ESMS implementation. The ESMS of FGPCD meets the requirements of ESS9 and includes clear and transparent eligibility criteria for loans to be guaranteed, screening procedures to appraise the mortgaged properties and ensure they comply with national building codes/ regulations and include a list of excluded activities. ARULoS has prepared an ESMF on the project including eligibility criteria and selection process of the beneficiaries, as well as a negative list. Technical assistance under component 3 will be carried out in accordance with terms of reference that are consistent with the ESSs requirements. The ESMF will incorporate a grievance mechanism that will accept and address complaints and concerns regarding relevant operations in a manner accessible and understandable for affected parties. FGPCD and ARULoS will also ensure that their staff are properly trained on the ESMS/ESMF.

21. Additionally, labor management procedures will be developed to ensure that direct workers (staff from FGPCD and ARULoS), contracted workers (employees of service providers or firms that will be contracted by ARULoS) and the human resource policies and practices of the commercial banks meet the ESS requirements. ARULoS has prepared a Stakeholder Engagement Plan (SEP) that highlights how information about the project will be disseminated and grievances managed.

22. E&S instruments have been approved and are in the process of being disclosed.

E. Implementation

Institutional and Implementation Arrangements

23. The project is integrated within the institutional framework of the national housing policy, placed under the responsibility of the Ministry of Urban and Housing Development (*Ministere de la Ville de l'Urbanisme et de l'Habitat*).

24. Project oversight. A high-level Steering Committee for the project will be established no later than one month after effectiveness. It will be chaired by the Minister of Economy and Finance and composed of the Minister of Urban and Housing Development (MVUH), the Minister of Budget, the Governor of the Central Bank and the President of the Chamber of Commerce. It will oversee the project, approve work programs and annual budgets, review annual reports, and will meet at least twice a year to review project implementation progress.

25. Project coordination in ARULoS. Project execution will be conferred operationally to ARULoS. ARULoS will be responsible for coordinating overall project implementation, ensuring the timely availability of funds transfers, maintaining project accounts, and producing financial reports, monitoring and evaluation (M&E) and reporting results to various stakeholders, as well as managing relations with the World Bank. For Component 1a, the FGPCD will be the implementing entity. ARULoS will sign a MOU with the FGPCD

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APPROVAL

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