

Greater Baku

HOUSING SECTOR

DIAGNOSTIC

Advisory Services and Analytics



Social, Urban, Rural and Resilient Global Practice (GSURR)
Europe and Central Asia Region



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ACRONYMS & GLOSSARY

Acronyms

AMF	Azerbaijan Mortgage Fund
ASA	Advisory Services and Analytics
AZN	Azeri Manats
CBD	Community-Based (and Driven) Development
Co-op	Housing Cooperatives
ECA	Eastern Europe and Central Asia
ESW	Economic Sector Work
ExComs	District/Raion Executive Committees
FinDev	Finance for Development
FSU	Former Soviet Union
GBRDP	Greater Baku Regional Development Plan
GoA	Government of Azerbaijan
GRM	Gross Rent Multiplier
GRY	Gross Rental Yield
GSURR	Social, Urban, Rural and Resilient
HBS	Household Budget Survey
HCED	Housing and Communal Economic Department
HH	Greater Baku Household
HMF	Home Modernization Fund
HOA	Homeowners Association
HMiF	Housing Microfinance Fund
HQI	Housing Quality Index
IDP	Internally Displaced People
KFM	The National Housing Fund
LITS	Living in Transition Survey
LTV	Loan-to-value
MDTF	Multi-Donor Trust Fund
MFB	Multi-family Building
MFI	Microfinance Institution
MMMC	Homeowner Association in Azerbaijani
MOEI	Ministry of Economy and Industry
MoJ	Ministry of Justice
PPP	Public-Private Partnerships
OECD	Organization for Economic Co-operation and Development
O&M	Operations and Maintenance
TBS	Polish Social Housing Society (Towarzystwo Budownictwa Społecznego)
UNECE	United Nations Economic Commission for Europe
VAT	Value-added tax
ZhEKs	Housing and Communal Services Russia

Glossary of Terms Used

Below are some useful definitions used throughout the report:

Common Property, per Azerbaijan Civil Code 2000, refers to the common parts of a multi-family building, including stairwells, roofs, lifts, basements, service and electrical shafts, mechanical rooms, and common rooms, etc.

Gross Rent Multiplier (GRM) is similar to the PE (Price-to-Earnings) Ratio used by capital markets. It is a ratio of gross rental income to property prices. Rental properties are considered fairly priced in the range of 12.5 – 20.0 of GRM. Prices over 20 of GRM are overvalued and below 10 of GRM are undervalued.¹

Gross Rental Yield (GRY) is a ratio of gross annual rental income to price of property. Low GRY (below 4 percent) indicates higher prices of rental properties (overvalued) and/or low relative rental levels. High GRY (above 10 percent) indicates lower property prices (undervalued) and/or high rental levels. Both low and high rental yields trigger market responses and tendencies to move towards moderate (fair) yield levels (5-8 percent).²

Housing Effort Ratio is a relation between a household's expenditures for mortgage interest payments or, in the case of rental tenure, for rent payments - as compared to household net income (after taxes). Affordable levels in this ratio are typically assumed at 25-30 percent; Eurostat, however, uses 40 percent, but this also includes outlays for maintenance and utilities. This ratio is also called Housing Cost Overburden Rate.

Homeowners Association (HOA), also known as Condominium Association (CA), is a voluntary union of the owners of dwelling units in multi-family apartment buildings which are established in order to provide joint management of the real (immoveable) property in the building. In Azerbaijan, HOAs are considered legal entities only once they are registered by the Ministry of Justice.

Multi-family Building (MFB) is housing consisting of several dwelling units or apartments in one building block; they are also often referred to as apartment buildings.

Public (rental) Housing is owned by a government entity with rent levels that are often below cost-coverage levels or set to cover only operating costs. It is intended to be addressed to vulnerable households such as homeless, disabled, refugees, and IDPs.

Realtor is a popular market name for real estate agents both for sale/purchase and for renting/leasing.

Rental Contract, sometimes called a residential lease, is between the landlord/lessor and tenant/lessee. It can be formal or informal, and typically includes time period of occupancy and predetermined rent level.

Rental Housing is defined as property owned by a rental landlord - someone other than the resident/tenant or by a legal entity, who collects periodic rental payments paid by the resident/tenant. Rental housing covers a range of markets: corporate executive housing, middle-class apartments, rooms in a landlord's home for factory workers, and units for former slum dwellers, and many more.

(Rental) Landlords are usually of three types: (i) individuals and small-scale rental property owners; (ii) institutional rental investors; and (iii) social and public housing providers.

Social (Rental) Housing is defined as rental accommodation in which rent is set at a level below market rates – usually on a cost-coverage (non-profit) level - to make it more affordable for tenants considered financially weaker, such as low- and lower-middle income earners, the elderly, and young migrants.

¹ For more explanation see BEST (2011).

² Low GRY is pushed up as rental investments decrease and more people are attracted to renting, which drives rents up and prices down – thus pushing GRY up. And vice versa with high GRY. See BEST (2011) for further explanation.

Subsidies are public policy instruments that make housing accessible to those who cannot afford market rents. These may be in-kind, as in the case of providing public and social housing units, or financial, as in the case of income supplements to households facing unacceptably high rental effort ratios or directly to housing producers facing high development costs.

White-frame/Black-frame units – Black-frame multi-family buildings look unfinished from the exterior and the units don't have doors or window frames (including exterior windows) or interior finishes (including wiring, painting, toilet, or kitchen fixtures). In contrast, the white-frame multi-family buildings look finished from the exterior because the exterior doors and windows are finished, but the units do not have interior finishes.

ZhEKs – Building management companies owned by local authorities, which date back to the Soviet era.

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EXECUTIVE SUMMARY

The Greater Baku Housing Sector Diagnostic report provides a broad assessment of the current state of the housing sector in Greater Baku, and provides evidence-based guidance for reform initiatives. The study is a follow up to the Greater Baku Regional Development Plan (GBRDP), and was carried out in response to a request by the Ministry of Economy and Industry (MOEI). The intended primary audience is the Government of Azerbaijan, including Greater Baku city mayor, city managers, international partners, and other stakeholders engaged in the housing sector.

The Diagnostic relies on field work carried out from 2013-15 in the Greater Baku Region. The field work included a large Household Survey, focus group meetings, and interviews with relevant government and non-government agencies (details in Annex 1). It may be noted that the absence of data was a key constraint for the team, both in terms of access to some critical secondary data as well as the inability to include income-related questions in the Household Survey questionnaire.

This Executive Summary may be viewed as a “short report” which presents key findings of the housing assessment and proposes recommendations for housing sector reform. This study is centered on three major issues and related recommendations:

- 1 There is currently no national level policy or strategy in the housing sector, and the legal and institutional framework is inadequate to address the wide-ranging needs in the housing sector.** As a result, public sector interventions in the housing sector are fragmented, subsidies are not targeted to those who need them, and systems are not in place to leverage the sort of participation that makes the housing market “functional” in terms of efficiency or equity. The development of a national housing strategy is thus recommended as the first and foremost step towards achieving the gains that the housing sector has to offer.
- 2 A large proportion of the existing housing stock was built before the 1990s, and is in dire condition after decades of under-maintenance.** This is an important asset base; modernizing the old housing stock will require rechanneling of both public and private financial resources, and revising existing institutional and regulatory frameworks to create the right incentives for homeowners to undertake the necessary capital improvements.
- 3 The formal housing sector has been unable to produce new housing of the composition, type, or price needed to respond to prevailing demand.** As a result, housing choice is severely restricted for both low- and middle-income households, and a large part of the population is forced to find alternative “informal” or “illegal” housing solutions. Addressing this issue is a complex but necessary task, and will include among others the following: improving the property titling and registration process, bringing housing finance more down-market than it currently is, addressing the deficiencies in the rental market, and leveraging the private sector to build more affordable housing.

Stemming from these three points, the main findings and recommendations of the Housing Diagnostic study are further summarized below.

Key Findings

1. Poor quality of Soviet-period housing stock

The quality of the housing stock is in dire condition and continues to deteriorate due to the lack of maintenance. It is estimated that 2 million Azerbaijani's (20 percent) live in substandard and deteriorated housing.³ According to a UNECE housing study, more than 80 percent of residential buildings, were built 40-50 years ago, 30 percent of which require urgent repairs or reconstruction.⁴ In Greater Baku specifically, the median age of the city's housing stock is 40 years with the large majority constructed between 1940 and 1990.⁵ Around 77 percent of this stock constitutes multi-family buildings, which have suffered from lack of maintenance due – in part – to unclear property rights over common areas and inefficient housing management systems. Typical problems in these Multi-family Buildings (MFBs) include crumbling facades, broken windows, visible cracks in walls and floors, non-functional elevators, dilapidated common areas, and poorly-maintained facades. Some 70 percent of households surveyed in Greater Baku reported having one or more of the aforementioned housing problems.

While the government has undertaken a series of reforms⁶ focused on improving the management of MFBs, much remains to be done. On the one hand, legislation has not been fully implemented at the municipal level due to the lack of enforcement. On the other, a range of other issues have *de-facto* left management of much of the soviet-era MFB housing stock in the hands of ZheKs (Soviet-era housing management companies). These include, among others, the reluctance on part of the owners to take on responsibility for common property in MFBs, lack of awareness regarding the homeowner's role in MFB management, and bottlenecks in registering homeowners associations (HOAs) or undertaking other management alternatives allowed by law. As of May 2015, only 7 HOAs have been formed in Greater Baku, two of which are still pending registration. Furthermore, after decades of under-spending, maintenance fees paid by homeowners - ranging from 3 to 7 AZN per month per unit - are grossly inadequate, making it impossible for HOAs or ZheKs to undertake proper maintenance, let alone major capital repairs. Moreover, given the poor quality of much of this housing stock, bringing it up to acceptable levels of safety and quality would involve large investments, which cannot be borne by homeowners alone.

Most of the Internally Displaced People (IDP) households, the unemployed, and those without legal tenure live in MFBs in the poorest conditions. The difference in housing quality between IDPs and non-IDPs is striking: 84 percent of IDPs reported having one or more deficiencies in the quality of housing and common areas compared to 67 percent of non-IDPs. Furthermore, IDPs scored more than 50 percentage points across all the seven housing index indicators, which is significantly worse than the average for Greater Baku.⁷ Among IDPs, those living in collective centers present the most precarious conditions: 95 percent with one or more housing problems (see Figure 1). Important differences are also observed based on the employment status of the head of the household. While unemployed and pensioners scored 74 and 79, respectively, fully-employed households scored 66 percent. Household heads having no legal proof of ownership and renters – on average - also live in dwellings of poorer quality.

³European Union - Support to Azerbaijan Housing Sector - "Gap Analysis Report: Support to Housing Policy Reform," November 2013.

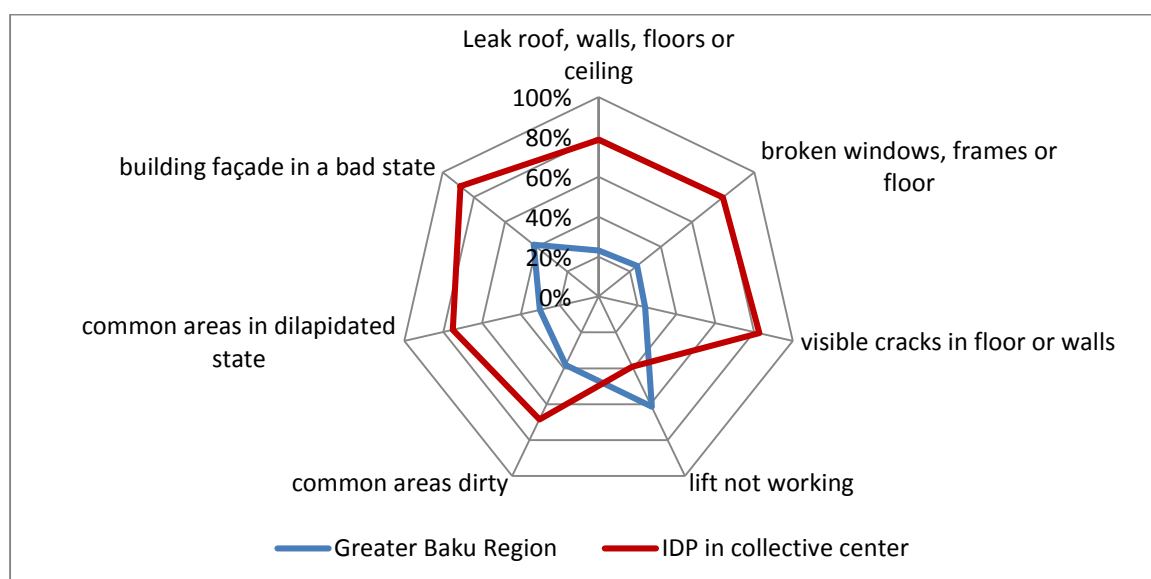
⁴ UNECE "Country Profiles on the Housing Sector: Azerbaijan" (2010).

⁵ World Bank, *Greater Baku Household Survey* (2014)

⁶ A new Civil Code adopted in 2000 defined rights and obligations of apartment owners over common property. In 2009, a new Housing Code formulated a modern legislative framework with respect to management and maintenance of MFBs and their common areas. In particular, it introduced the key option of establishing Homeowners Associations (HOAs) or MMMCs as HOAs are known in Azerbaijan. More recently, the Government created a new department within the Ministry of Economy and Industry (MOEI) in charge of dealing with housing sector issues.

⁷ A score of 100 percent reflects the worst living conditions.

Figure 1: Housing Quality Index (HQI) Greater Baku Region and IDPs Living in Collective Centers



Source: World Bank, *Greater Baku Household Survey* (2014)

2. Limited public assistance targeted to the poor

Currently, public funds are being used for cosmetic measures such as façade beautification rather than to solve the critical structural quality problems of old MFBs. Considerable public investments are being made on improving the facades of buildings – including a large number of older Soviet blocks – in the city center and other prominent areas. While these investments have clearly resulted in cosmetic improvements and visual appeal, the interiors of these buildings, including common areas and structural elements of the buildings such as elevators, roofs, external walls, etc., continue to deteriorate.

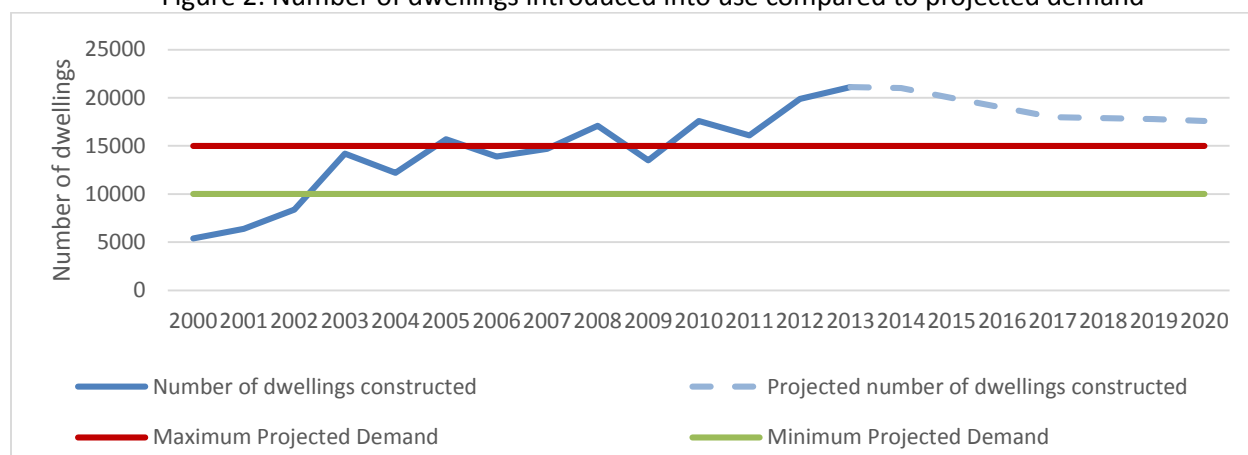
Apart from the IDP housing program, there are no public resources being targeted to the poor. Even in the IDP housing program, there is scope for improvement in terms of the program design – the current program is largely resettling IDP households to new housing developments that may or may not be well-connected to the cities. Also, it provides a subsidy in perpetuity to households regardless of income, money that could be better spent if allocations were based on income levels.

3. Lack of affordability

The formal housing sector has been unable to produce new housing of the composition, type or price needed to respond to prevailing demand. In terms of quantity, however, Azerbaijan’s housing production is in principle sufficient to meet increased housing demand. Data indicates that there is a very small housing deficit nationwide; Baku has a surplus of approximately 30,000 housing units.⁸

⁸ The total area of housing stock in Azerbaijan has increased approximately 30 percent since independence in 1991 – from 88.2 million m² in 1991 to 114.5 million m² in 2010. While housing area is not the ideal measure of housing stock, this data is used due to the lack of data on the total number of housing units submitted into use as well as housing units in existence. The average of 14,200 units submitted into use every year between 2000 and 2013 met the projected housing demand; demand is expected to continue at a rate of 10,000-15,000 units per year in the Absheron Peninsula.

Figure 2: Number of dwellings introduced into use compared to projected demand



Source: State Statistics Committee publication (historic data), WB (Projections)

The problem, thus, is less to do with a “deficit” per se, and more to do with a demand-supply “mismatch” between what the market is producing and what the end-users can afford. The price range of “white-frame”⁹ units in an average quality building in an outer city location is AZN 1,100-1,400 (USD 1,047 -1,332)/m². The cost of finishing the unit can be an additional AZN 300-350 per m². Much of this is unaffordable even for middle- to high-income households. While no official data is available, stakeholders attribute this to the high basic cost of housing to “hidden fees” paid (by the developer) for getting the necessary permits for construction, which is then passed on to the buyers. There are also reports of rampant speculation in the residential real estate market, with some local and foreign buyers purchasing multiple units as an investment and holding them vacant, thus fueling the high prices. Table 1 illustrates affordability benchmarks for housing units with a variety of tenure, location, and purchase mechanisms by income brackets.

Table 1: Affordability of different types of housing by income categories in Greater Baku

Income bracket	New housing purchase, market mortgage loan	New housing purchase, AMF Social Loan	Housing Micro Finance HMiF	Old housing purchase, market mortgage loan	Rental
Low	Unaffordable	Unaffordable	Unaffordable	Unaffordable	Unaffordable
Middle-low	Unaffordable	Affordable (Peri-urban)	Unaffordable	Unaffordable	Affordable (Peri-urban)
Middle	Unaffordable	Affordable (Peri-urban)	Unaffordable	Affordable (Small unit)	Affordable (Suburban)
Middle-high	Affordable (Peri-urban)	Affordable (Peri-urban)	Affordable (10k loan)	Affordable (Small unit)	Affordable (Suburban)
High	Affordable (Suburban)	Affordable (Peri-urban)	Affordable (10-20k loan)	Affordable (Large unit)	Affordable (Core urban)
Median**	Unaffordable	Unaffordable	Unaffordable	Unaffordable	Affordable (Peri-urban)
Income Affordability Threshold (AZN)	Peri-urban: 1848 Core urban: 5434	Peri-urban: 649*	From 1557 to 2410	Small: 1485 Medium: 2355 Large: 3043	618 (Unit more than 90 minutes from CBD)

* As the AMF has a cap of 50,000 on loans; buying units in the core urban and suburban areas (1st and 2nd zone) with this instrument would require making large downpayments (40 to 60+ percent depending on the zone), which are expected to be unaffordable for most.

** This corresponds to the official median income in Greater Baku in 2013 (800 AZN) according to the Statistics Committee

⁹ Black-frame units look unfinished from the exterior, usually don’t have doors or window frames or interior finishes (including wiring, painting, toilet, or kitchen fixtures). White-frame multi-family buildings look finished from the exterior because the exterior doors and windows are finished, but the units do not have interior finishes.

4. Increasing illegality, informality and sprawl

A significant percentage of new MFB housing stock is considered “illegal” or “incomplete” because it is either on land that is not titled and/or the property is not registered. In such cases, apartments are bought and sold on the basis of a Construction Contract/Agreement with the developer, but legally, these properties cannot be transacted. Also, these units cannot usually be leveraged as collateral for mortgage financing or other loans, so buyers must use other real estate – typically an older Soviet house – as collateral to be able to access bank financing.

Informal settlements have grown exponentially in the Greater Baku Region over the last decade. It is estimated that around 20 percent of households in the Greater Baku Region do not have the required ownership documents for their housing structures and/or their land.¹⁰ A recent study, carried out for the Committee for Real Estate Registration Issues (2014) and funded by the World Bank, estimated that 51,453 households reside in protected areas¹¹ mainly across Greater Baku.¹² Furthermore, an analysis of the establishment dates of a sub-sample (11,744) of these reveals an important growth from just 47 such households in the 1920s and 321 in the 1970s to 4,518 households in the 1990s and 6,116 after 2000.

Urbanization pressure coupled with the lack of affordable housing choices has also increased the incidence of sprawl. Informal housing in the form of agricultural land subdivisions are occurring at a fast pace in the suburbs of Baku City. The fast growth of low-density informal settlements in the periphery has important implications to the cost of service provision to these areas. Data also reveal a growth and densification of informal settlements in environmentally-hazardous areas (oil-contaminated) and areas reserved for trunk infrastructure in Baku city.

5. Lack of access to housing finance

Options to finance the purchase, construct, or improve housing are limited. Available options for housing purchase include the Azerbaijan Mortgage Fund (AMF), established in 2005, and housing mortgage products offered by financial institutions. Home improvement/ expansion/ construction may be financed through housing microfinance (HMF) products offered by banks and Microfinance Institutions (MFIs). However, most of these options have not been able to either achieve sufficient scale or reach the large majority of households in the country.

The mortgage market has had limited penetration. Mortgage lending is still considered relatively risky in Azerbaijan, and this is evident from the large down payments (40-50 percent) demanded by banks for mortgage loans. Several banks interviewed attribute this to the “unstable” and “inflated” housing market, and what is experienced as a weak legal framework surrounding foreclosure and enforcement of collateral. These high down payments together with the double-digit interest rate make mortgage loans less attractive and inaccessible for the vast majority of the population. On the other hand, households’ borrowing capacity is constrained by widely-recognized practices of unreported income. As a result, the existing mortgage loans offered by the market are beyond the reach of most households. According to data, less than 5 percent of all housing sales are financed by mortgages (see Figure 3). Azerbaijan presents one of the lowest levels of mortgage penetration across the region.

The Azerbaijan Mortgage Fund (AMF) has and continues to play a considerable role in boosting the mortgage market, but is poorly targeted. Currently, subsidized social loans appear to be serving others rather than the intended poor population of citizens¹³. Other issues include: (i) the loan cap of AZN 50,000 is too low relative to current house prices; (ii) the high down payment (30-40 percent) demanded by the banks; (iii) the limited number of social loans offered, creating a backlog and long waitlists; and (iv) the possible distortionary effect that AMF ‘standard loans’ might be having on the mortgage loans offered by commercial

¹⁰ World Bank, *Greater Baku Household Survey* (2014)

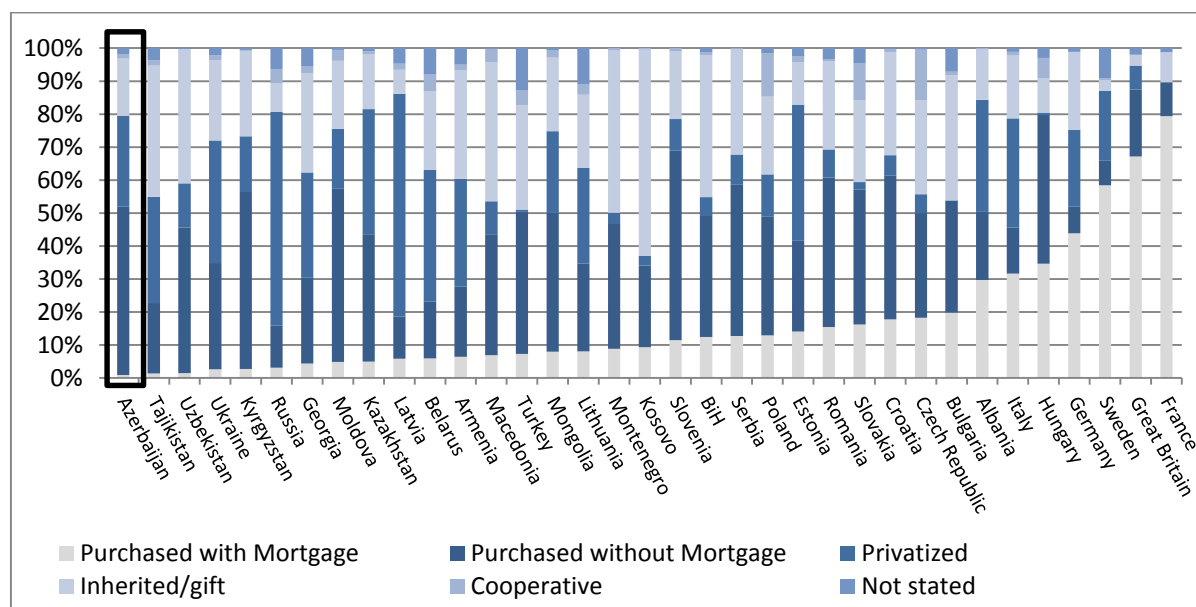
¹¹ Protected areas consist of land around hazardous oil-wells, railway lines, gas lines, sewerage lines, etc.

¹² Committee on Real Estate Registration Issues, “Policy Document on the Regulation of Informal Settlements in the Republic of Azerbaijan.”

¹³ This is in part due to the targeting of subsidized social loans towards accomplished professionals in the academic and athletic fields, for instance

banks. The Government has recently announced plans that address these issues: aiming to increase the loan cap (to 100,000 AZN), decrease interest rates, and allocate an additional 200 million AZN of the State budget to stimulate the construction market that's been affected by the slowdown of the economy.

Figure 3: Housing finance in Europe and Central Asian countries



Source: LITS (2010)

The microfinance industry is very well-established in Azerbaijan, but its direct role in financing housing is still very limited. There are 48 licensed MFIs and 4 credit unions in Azerbaijan as well as several products in the market aimed at providing home improvement or construction loans. Despite a good presence of MFIs covering different market segments across Azerbaijan (both urban and rural), these institutions report facing several constraints: (i) their cost of funds is very high, which is reflected in the high interest rates of their products (25-40 percent); (ii) they receive funds in USD, and do not have adequate tools to hedge the currency risk, so they peg the AZN loans to the USD, which essentially passes on the risk to the borrower; (iii) they have limited funds, so they are unable to give out larger and longer-term loans for home improvement – particularly to owners of flats in old MFBs who want to make improvements.

6. Weak legal and institutional framework

While the legal and institutional framework for housing in Azerbaijan covers a broad range of housing issues, some key gaps remain, particularly related to implementation. The Civil Code (2000) provides well-defined property rights, including rental tenure rights that cover both commercial and residential tenancies. The Housing Code (2009) reinforces this right (Art. 35.2), imposing obligations on apartment owners to maintain and repair common areas in multi-family buildings and providing options for property management models, the most prominent of which is the homeowner association (HOA). However, specific bylaws and procedures required for implementation are still missing. More recently, a Presidential Decree (January 2015) was issued aiming to regularize illegal constructions, but requirements for this still do not cover many of the informal settlements. With regard to housing finance, there is a need to strengthen the legal framework surrounding foreclosure and enforcement of collateral to make mortgage lending more efficient and for it to be perceived by banks as less risky. Finally, as discussed in detail in the rental housing chapter, a distinct ‘residential tenancies law’ has yet to be formulated to proactively cover potential disputes and conflicts between residential tenants and landlords.

In addition, existing Government programs for the housing sector are not effectively targeting the sector’s core problems, leading to calls for a new comprehensive housing policy and a strategy for implementation.

While important efforts have been made in the past decade, such as the establishment of the AMF, the recent housing management reform, and the façade beautification campaign, these constitute fragmented responses and remain insufficient to respond to the important housing sector challenges of Greater Baku. Thus, there is a need to develop a coherent comprehensive housing policy and implementation strategy with clear short-, medium-, and long-term targets that can lead

Recommendations

1. Develop a comprehensive National Housing Strategy and initiate reforms

First and foremost, the Government of Azerbaijan may consider developing a National Housing Strategy. This would involve undertaking a more detailed diagnostic of the current situation; adopting overarching goals and principles as well as specific targets; and developing an action plan for short-, medium-, and long-term horizons with identified funding sources and implementation responsibilities.

2. Improve housing management and the quality of the housing stock

One step towards improving the quality of the housing stock is to make housing management practices more efficient. The improvement of existing management practices will require a combination of improvements in existing incentive frameworks, increase in technical and financial capacity of both homeowners and public authorities, and development of the right regulatory environment for enforcing the law. It will also require an appropriate business environment for establishing HOAs. Given the lack of incentives to form HOAs, the high transaction costs to establish them, and the lack of capacity to put in practice efficient housing management systems, there is a tendency to continue the status quo where each party expects the other to take responsibility for maintenance. Changing existing practices requires a concerted effort and is likely to involve at a minimum: (i) developing missing bylaws and defining simple and transparent procedures to mainstream the establishment of HOAs; (ii) creating incentives for the establishment of HOAs; and (iii) developing a technical assistance program aimed at strengthening existing management practices and professionalizing housing management. One option to improve the incentive structure is to make HOAs mandatory by law or conditional for the reception of capital improvement laws. These recommendations are also shared by the recent EC Housing Reform study done in Azerbaijan.¹⁴

In parallel, it is recommended that GOA consider developing a program to provide State co-financing for capital repairs, such as a National Housing Fund (NHF). Such a Fund could provide monetary support to support eligible capital improvements in the form of long-term (10-20 years) subsidized loans to the HOAs together with a co-financing element that could range from 10-50 percent of the repair costs for example. The NHF could also require that such improvements include energy efficiency retrofits.

3. Improve targeting of public funds for housing

Several instruments may be considered to provide more targeted public housing assistance to lower income groups. These could include introducing new programs as well as reviewing and reforming existing programs, as described below.

- **Introduce a cash transfer program for poor households.** The State should consider introducing a cash transfer or housing allowance program to subsidize low-income households that are paying more than a certain percentage of their income (e.g., 20-25 percent) on housing and utilities combined.
- **Introduce a social housing program.** There is currently no social housing program in Azerbaijan (the IDP housing program is called social housing, but in fact, targets a specific group of people, is rent-free, is not income-targeted, and is allocated for an indefinite time period). While other housing programs target various non-IDP population segments, they are not targeted to low-income households. A social housing program could be a combination of subsidized rentals in public housing and rental vouchers (subsidies)

¹⁴European Union - Support to Azerbaijan Housing Sector Report 2 - "Recommendations on Housing Management Options of Common Properties," February 2014.

paid by the Government for private rental housing. In terms of creating a public stock of social housing, it is important that the Government mobilize and leverage the private sector to contribute to this pool.

- **Consider reforming the IDP housing program.** Many IDP households have been accommodated in new housing built by the Government, but hundreds of thousands still remain in deplorable housing. While the resettlement into new Government-built housing may be one approach to address the IDPs' housing problem, it would be much more efficient and cost-effective to use a combination of options, such as rental vouchers in private housing, to allow IDPs to make their own decisions regarding housing. In addition, there is a need to better target low-income IDPs to make sure that those in need are given priority in housing programs. Finally, location should be considered as an important variable affecting households' livelihoods, as many of the new IDP units being constructed are distant from important employment opportunities and transport nodes.
- **Improve targeting of subsidized AMF loans.** The loan products offered by the AMF are effectively a massive subsidy from the Government to borrowers who are not necessarily in need of them and could even afford other market-rate financial products. The terms of the AMF Social Loan need to be reformed to target those segments of the population that are creditworthy, but do not have access to housing finance. The Standard Loan should be reformed to more closely resemble a market-based loan; this way, the AMF will better perform its role as a re-financing facility without competing with mortgage products offered by the market.

4. Strengthen and expand existing housing finance instruments

Establish a National Housing Microfinance Fund. A more stable source of longer-term AZN funds (7-10 years) could help MFIs address the constraints faced by MFIs in housing-related lending. It is recommended that a National Housing Microfinance Fund (NHMF) be established to serve as a liquidity facility – a source of 7-10 year AZN loans for MFIs at a reasonable interest rate (e.g., 3-4 percent, comparable to the interest rate of the current AMF Social Loan).

Improve access to mortgage finance. There is a need to address the current shortage of long-term AZN funds for housing mortgage loans. Given the recent devaluation, mortgage issuance by commercial banks using their own funds has significantly decreased. A possible approach in the short term could be to restructure the AMF in a way that it serves as a real liquidity facility pumping liquidity to the banks without distorting the market by offering loans at subsidized interest rates. More specifically, the terms of the AMF Standard Loans may be adjusted to more closely resemble market-based loans in terms of the interest rate charged and loan size, etc. Once the market for these loans picks up with adequate supply of AZN financing, the rates may be expected to become more competitive. This way, the AMF might better serve the market by filling an existing financing gap (of long-term AZN funds), rather than offering a product that effectively “competes” – while having an unfair advantage – with the commercial banks' internal loans. Also, AMF funding for such commercial loans may be considered for an increase to better reflect the scale of market demand. However, this must be done with caution as flooding the market with finance could artificially inflate demand and increase prices.

5. Facilitate the development of a robust rental market

While renting is not the panacea to solving the housing challenge, the rental market constitutes a vital housing tenure option that should be promoted alongside, and not in competition with, homeownership. This may be substantiated through programs aiming, *inter alia*, at provision of more public as well as market-based rental housing. This will require, among others, a review of the regulatory framework for market-based landlord-tenant relations and by passage of a dedicated ‘*residential tenancy law*’ including contract enforcement and dispute resolution mechanisms specifically for residential tenants and landlords.

Small-scale informal landlords may be encouraged by means of tax incentives to legalize their activities. This could be done through a specialized law on ‘occasional renting’ with a lower tax rate and streamlined eviction procedures. In addition, existing landlords may be encouraged to ‘scale up’ their activities by offering them additional incentives for qualified cases of moderate-rent moderate-standard rental offering. These

incentives may include additional tax concessions, access to land at low prices, and/or through favorable ground leaseholds. Owners of vacant dwellings could be encouraged to put them on the rental market. The introduction of a tax on vacant dwellings may also be considered as a means to bring more vacant dwellings into the rental market.

6. Create clear policies targeted to absorb and prevent the growth of informal settlements

In order to reduce the number of informal settlements, there is a need to put in place policies to prevent the formation of new informal settlements and absorb harmoniously existing ones. Preventing the growth of informal settlements needs to be preceded by a better understanding of the causes of informal housing growth. As observed throughout this diagnostic, there are important constraints in the housing market that are leaving a large portion of the population unable to afford or access formal housing. Despite having enough housing options available in terms of quantity, most available housing is targeted towards high-income households. In addition, even when households are able to secure legal tenure for land, the transaction costs for obtaining construction permits are cumbersome and high. Most of the recommendations provided herein (i.e., improve targeting of public funds for housing, expand housing finance instruments, enable the rental market, and create a better business environment) are by themselves important actions to prevent informal housing growth. In addition to these, cities in Azerbaijan need to review their current urban practices, construction standards, and more importantly, their practices for land recycling in city-centers and land-conversion in peri-urban areas.

Informal settlement absorption should take into consideration the diversity of informality and should, when possible, follow an integrated approach. Housing informality observed in Azerbaijan is diverse, including dense squatters in central areas; settlements in protected areas unsafe for humans; single-family houses in the periphery after agricultural land sub-divisions; and high-rise, multi-family buildings that were constructed without permits or are not registered. As a result, housing policies aimed at absorbing and integrating informal settlements into the urban fabric will require a diverse set of approaches. High-rise buildings, when following required building standards, can be regularized and integrated more easily and at a lower cost. On the contrary, low-density informal settlements with poor access to services and disconnected from the rest of the city require a more integrated approach that looks both at social and basic service provision, tenure, and connection to the rest of the city. Informal settlements located in protected areas (e.g., near high-voltage electricity networks), which pose hazards for their inhabitants should be resettled. For the latter, livelihood impact assessments should be done to reduce and mitigate the negative impacts of resettlement. Social housing programs can be one of the options to house resettled households. These and more detailed recommendations and actions can be found in the recent “Strategy on regularization of illegal construction in the Republic of Azerbaijan” and accompanying Policy Document produced by the World Bank for the Committee on Real Estate Registration Issues (2014).

7. Improve housing data collection

There is a need to develop systematic reporting on housing demand, supply, pricing, rental levels, and trends to inform housing policy and market actors, and to allow international comparability. This is critical to assess housing sector trends and to monitor the implementation of housing programs and policies.

The table below presents key recommendations ranked by their level of priority, including a brief description of policy options.

Table 2: Housing Sector Reform Recommendations and Priorities

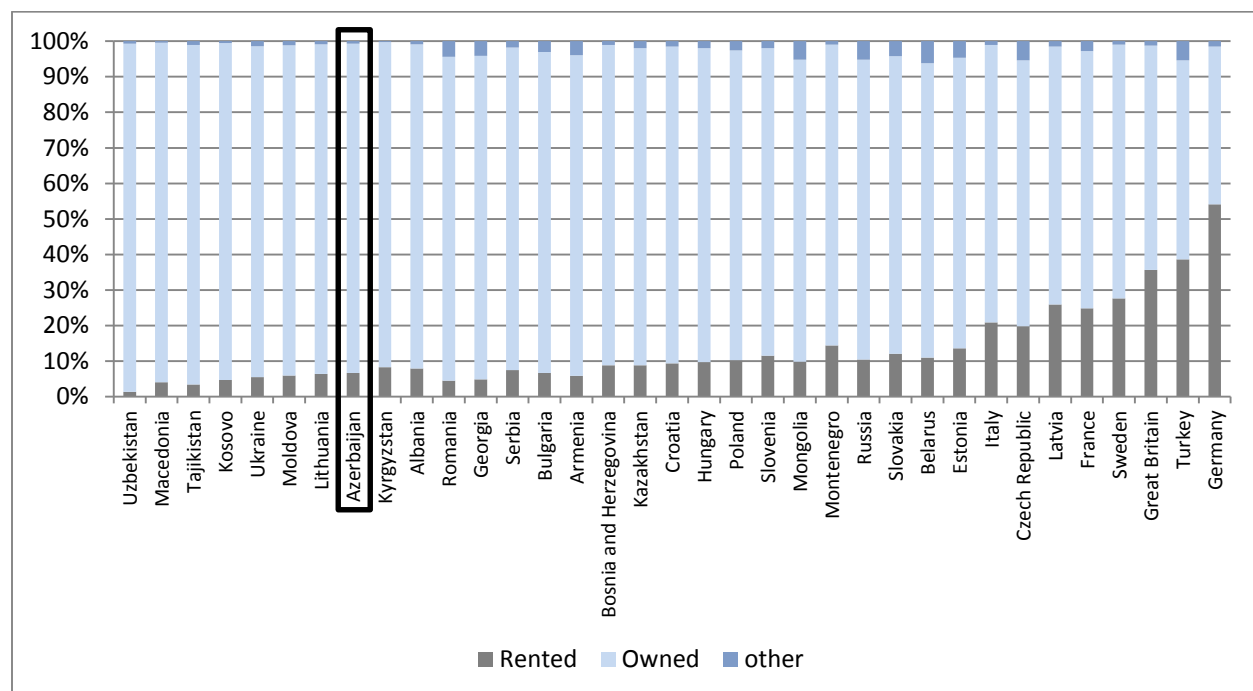
Desired Results	Recommendations	Priority
The Government has a well-defined National Housing Strategy/ Policy	Develop a clear housing policy and implementation strategy and improve housing data collection.	High
Existing dilapidated housing stock is modernized and housing maintenance practices are in place	Improve existing housing management practices, and develop a program to provide State co-financing for capital repairs. Modernization Fund (HMF) are also recommended.	High
The extent of the informal housing market is reduced	Put in place policies to prevent the formation of informal settlements and absorb harmoniously existing ones. Formalizing existing informal or semi-formal dwellings will require a diversity of approaches such as: (i) regularization of “formal” type property, (ii) resettlement of household in protected areas, and (iii) integral upgrading of informal settlements in slum-like conditions.	High
Existing public funds for housing are well targeted to those in need	Provision of housing assistance can be done through multiple instruments such as: (i) introduction of a cash transfer or housing allowance system, (ii) introducing a social housing program, (iii) review existing programs targeted at vulnerable groups, such as IDP and/or (iv) improving targeting of existing AMF subsidized loans.	Medium
Azerbaijan counts with a diversity of housing finance instruments that target different sectors of the population	Strengthen housing finance instruments by: (i) establishing a Housing MicroFinance Fund and (ii) Improving mortgage financing. The later could be achieved through the restructuring of the AMF (Standard loans).	Medium
There is a dynamic rental housing market	This can be achieved through a combination of actions such as: (i) the creation of tax incentives for small informal landlords to legalize their activities, and (ii) encouraging owners of vacant dwellings to put them on the rental market by increasing taxes on vacant property.	Low

INTRODUCTION

Background

As Europe and Central Asian (ECA) countries of the Former Soviet Union transitioned out of the Soviet model, a series of housing trends emerged: high ownership rates, underdeveloped rental housing markets, rising housing informality, shortages in good quality housing for the vast majority, and, in many cases, overcrowding. Most Eurasian cities emerged from communism with strong local demand for housing; some central Asian cities faced absolute housing shortages as their populations soared. In addition, after the wide-scale privatization of housing that followed the fall of the Soviet Union, countries in the region found themselves with some of the world's highest rates of homeownership (See Figure 4), which created rigidities in the housing and labor market. Ownership rates are as high as 98 percent in some Eurasian countries, far higher than in the US (67.2 percent) and in the EU (average of 73.5 percent). There is little public rental stock (less than 7 percent on average) and the private sector rental market is largely informal. With most public sector programs unable to cater to the housing needs of lower income groups, and the private sector almost exclusively targeting higher income groups, most new entrants (e.g., young families) and lower income households are forced to 'double-up', find alternative housing accommodation (informal sector) or live in poor quality housing.

Figure 4: Tenure status in European and Central Asian countries



Source: LITS (2010)

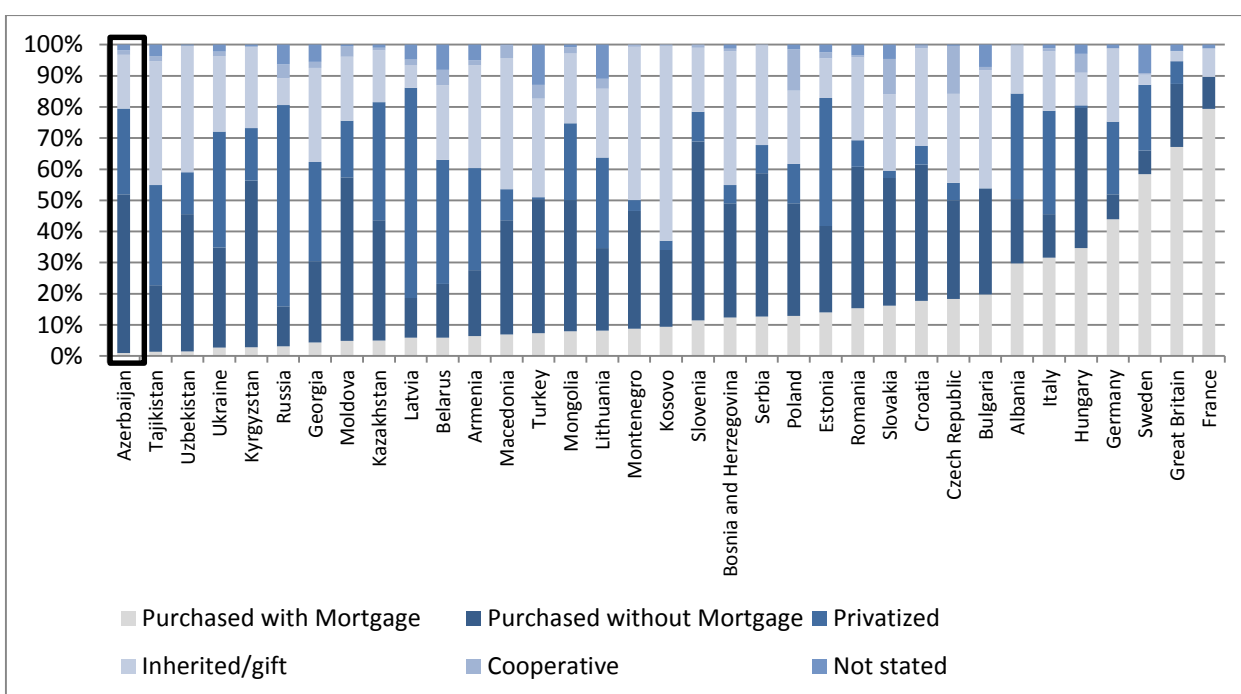
Among others, lack of maintenance of Multi-family Buildings (MFBs), has been a common problem faced by Former Soviet Union (FSU) countries. Most of the apartment blocks built after the 1970s were of poor quality to begin with, and after privatization, the lack of appropriate frameworks for maintenance of the common areas or infrastructure led to further deterioration of the stock, in many cases raising concerns of structural safety. And although security of tenure might not be an issue for their residents, many of these buildings now resemble vertical slums. These types of sub-standard dwellings are widely spread across the region.

In addition, rapid urban growth in Eurasian cities has - as in many other developing countries - been accompanied by growth of the informal housing sector. The proportion and typology of informality varies

considerably between cities and countries, but it is estimated that some 50 million people in over 20 countries in the region live in informal settlements.¹⁵

The housing sector in Azerbaijan faces problems typical to transition economies in ECA. The existing multi-family housing stock is deteriorating rapidly as a result of privatization in the absence of sufficient housing management and maintenance. According to the household survey conducted under this study, 77 percent of surveyed households living in multi-family buildings reported having one or more housing quality problems. In addition, rapid urbanization under these circumstances has led to the growth of informal housing. Azerbaijan remains one of the fastest ‘urbanizers’ in the region, maintaining annual urban growth values above 1.5 percent over the 2010-2013 period. UNECE estimated that around 30 percent of the population in Azerbaijan lives in informal settlements, many of which are concentrated in Baku and the Absheron peninsula comprising most of the Greater Baku metropolitan area.¹⁶ However, until now, no study has managed to quantify the realities of the housing stock of the Greater Baku Region. Furthermore, existing housing finance instruments and government programs have not been able to effectively target low-income households.

Figure 5: Housing finance in Europe and Central Asian countries



Source: LITS (2010)

There is a recognized need to develop reliable, comprehensive, and meaningful data to support decision-making in the housing sector in ECA. The latter has been mentioned in the recommendations of a number of Country Profiles and Working Papers. The lack of housing data also hampers the establishment of a land administration system with proper registration, standardized valuation mechanisms, and a wider taxation base. The UNECE Azerbaijan 2010 Housing Country Profile noted that although statistical information on housing exists, it does not contain important data on the condition of the housing stock, and that to better plan future activities in the sector, the country should undertake an audit of its housing stock, possibly starting with a pilot program in Baku city. A recent Russian housing affordability study - carried out by the

¹⁵ UNECE, *Self-Made Cities* (2009)

¹⁶ UNECE, *Country Profiles on the Housing Sector: Azerbaijan* (2009)

Bank - also recommends improving housing information systems as current data is not sufficient to transition to market-based methodologies for projecting housing demand or needs.¹⁷

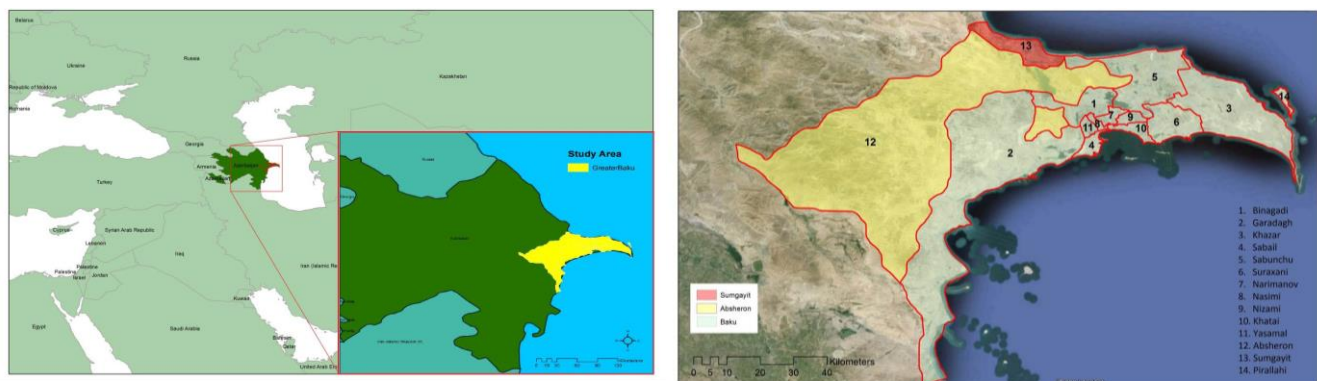
Objective and Methodology

The primary objective of the Greater Baku Housing Sector Diagnostic Advisory Services and Analytics (ASA) work is to support the Government in undertaking evidence-based decisions and policy reform in the housing sector through a broad housing sector analysis. Greater Baku was selected to conduct this Housing Diagnostic because it presented a range of housing issues: growing informality, housing located in environmentally-sensitive areas, post-Soviet multi-family housing with management and maintenance issues, supply/demand mismatch, limited access to housing finance, and so on. In addition it is home to the largest urban agglomeration in Azerbaijan and concentrates 25 percent of the country population.

The Greater Baku Housing Diagnostic was developed in two phases: Phase 1, which was quantitative in nature, and Phase 2 which was more qualitative. The *Quantitative assessment* (Phase 1) involved the development of an extensive household survey covering 1,200 households in the Greater Baku Region. The survey instrument was designed to allow creation of a diagnostic of the current state of the housing stock and the current situation in terms of access to basic services and accessibility to essential amenities and transportation nodes; an assessment of residential mobility patterns, as well as tenure types in terms of ownership and levels of informality; a review of financing options used for housing purchase; and housing improvements and an assessment of multi-family building management structures and their performance. A more detailed description of the survey design and instrument can be found in Annex 1. The *Qualitative assessment* (Phase 2) combined a number of methodologies (i.e., desk review, review of secondary data, focus group discussions, and detailed expert interviews) and focused on identifying existing bottlenecks for a more affordable and better functioning housing market. Together, phase 1 and phase 2 provide sufficient information on the current state of the housing sector in the Greater Baku Region and help identify sectoral priorities to move to a more efficient and affordable housing sector.

The following figures present the geographic location of Greater Baku, as well as the districts and satellite towns that conform this metropolis.

Figure 6: Greater Baku location, districts, and satellite towns



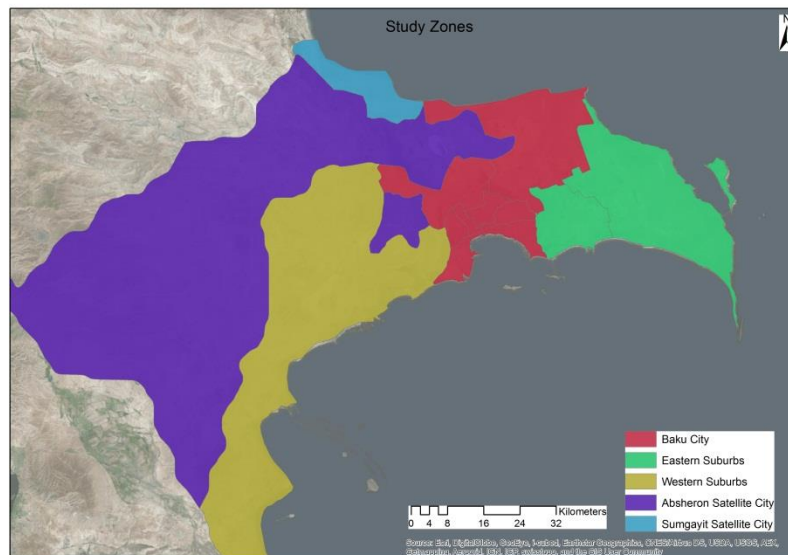
For analytical purposes, the Greater Baku Region's districts were classified into the following five zones based on their location:

- Baku city (RED): Sabail, Yasamal, Nasimi, Narimanov, Nizami, Khatai, Sabunchu, Narimanov, Binagadi
- Eastern Suburbs (GREEN): Suraxani, Khazar, Pirallahı
- Western Suburbs (YELLOW): Garadagh
- Absheron Satellite City (PURPLE): Absheron

¹⁷ World Bank, *Provision of Affordable Housing in the Russian Federation* (2012)

- Sumgayit Satellite City (BLUE): Sumgayit

Figure 7: Greater Baku Metropolitan Study Area by Zones



Report Organization

The rest of the report is organized in the following manner:

Chapter 1 – Housing Typology & Informality Trends: describes existing housing typologies in the Greater Baku Region, trends in residential growth, and emerging housing challenges, with a particular focus on growing informality.

Chapter 2 – Housing Market Analysis: presents an analysis of the current housing market (demand and supply) and existing housing finance options.

Chapter 3 – Housing Prices and Affordability: briefly takes a look at current housing prices and household preferences and reviews housing affordability based on the previous.

Chapter 4 – Rental Housing: focuses on the existing housing market, analyzing the existing legislative and institutional framework and the rental market situation, and presents recommendations to further support the development of the formal rental housing market.

Chapter 5 – Housing Maintenance and Management: focuses on the current state of multi-family buildings, analyzes the existing legislative and institutional framework, and reviews existing housing maintenance challenges.

Recommendations and Priorities: presents final conclusions and recommendations for the development of a more efficient and affordable housing market.

Annex 1 – Household Survey Methodology & Summary Results: contains a methodological note on the development of the household survey, including sampling and survey instrument design and a summary of survey results. This Annex also includes a hedonic prices model.

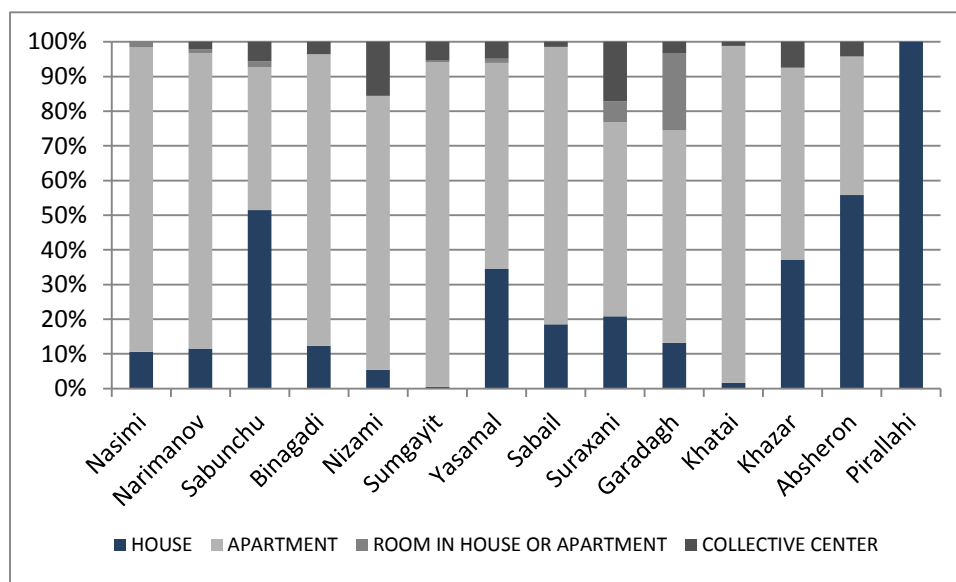
Annex 2 – Legislative and Institutional Framework: presents current legal and institutional framework in Azerbaijan relative to the housing sector and existing Government programs for housing and communal services. An analysis of legal and institutional gaps concerning the management of multi-family buildings and the rental market can also be found in Chapters 5 and 6.

CHAPTER 1: Housing Typology & Informality Trends

This chapter presents the predominant housing typologies in the Greater Baku Region and observed trends in the growth of informal housing. It is based on information collected by the Household Survey conducted in August 2014 (Refer to Annex 1 for more details) and satellite imaging analysis (Box 1). These were complemented with field assessments and expert interviews during the qualitative review.

The majority of housing stock in Greater Baku is made of multi-family buildings, most of which were built between 1970 and 1990 (see Figure 22). Spatial and primary data reveal rapidly changing residential patterns over the past decade with the growth of high-density high-rise multi-family apartments in Baku inner city and low-density single family houses (both formal and informal) in peri-urban areas. Low-density is predominantly resulting from the subdivision of agricultural land in the suburbs¹⁸. Spatial Analysis also indicates new residential infill development (Figure 9) occupying former cluster housing areas in the inner city. There appears to be a lack of land-use planning and zoning enforcement giving rise to haphazard urban residential development and, ad hoc practices of land allocation¹⁹. Despite efforts made in 2007 by the Government to establish the State Committee on Urban Development and Architecture to design, regulate, and implement uniform urban development policy, planning and architecture, urban and land use planning enforcement has been weak. In response, the World Bank financed the preparation of the Greater Baku Regional Development Plan (GBRDP) under the on-going National Water Supply and Sanitation Program. The GBRDP was finalized at the beginning of 2015 and submitted to the Cabinet of Ministers for approval by the Prime Minister.

Figure 8: Dwelling Type by District in Greater Baku



Source: World Bank, *Greater Baku Household Survey* (2014)

¹⁸ Interview with Committee on Real Estate Registration Issues, and Spatial Analysis data.

¹⁹ UNECE, "Country Profiles on Housing Sector- Azerbaijan" (2010).

Figure 9: In-fill development within older organic cluster housing, Baku Inner City



Box 1: Spatial Analysis Methodology

A spatial analysis was carried out of the Greater Baku Metropolitan Area in 2014 to document the current housing typologies, informality trends, and residential growth patterns as part of this study. A draft background note was prepared and submitted to the Ministry of Economy and Industry (MOEI) in December 2014. The data imagery analyzed represents the current situation with regard to the type of housing available to residents of the city. Google Earth and other sources of temporal satellite imagery regularly used as a source of information on human settlements were used for this analysis. Although constraints exist in a “top down” approach to settlement evaluation, with knowledge of the study area and information from the Household Survey, the spatial analysis identified 10 distinct settlement/development patterns in the Greater Baku region.

A visual survey of the entire site was done using Google Earth Pro and imagery taken over 5-year time periods (for which high quality imagery was readily available) was evaluated to observe visible variations in spatial development patterns over the last decade. Excerpts from imagery of case study areas are included as evidence in the form of 1km X 1km square areas on the ground. The 1 Km square areas were compared at the same scale throughout the study area to best capture and compare changes in residential development intensity over the 10-year timeframe in different housing typologies across the Greater Baku Region. The spatial survey was divided into three zones – Inner City Baku, Peri-Urban/Suburban Areas and Satellite Towns (Absheron and Sumgayit).

To verify the spatial analysis, follow-up field visits to residential sites were carried out. Furthermore, the Committee on Real Estate Registration Issues was consulted on the findings, particularly with respect to growth of informal settlements in agricultural areas in the peri-urban areas of Baku.

1. Housing Typology

Based on the satellite imagery analysis, the Greater Baku Region can be classified into 10 broad housing types: (1) Old Multi-Story Housing; (2) New Apartment Buildings; (3) Planned Plotted Housing; (4) Organic Cluster Housing; (5) “Temporary” Housing; (6) New IDP Social Housing; (7) Illegal Sub-divided Agricultural Land converted to plotted housing; (8) Inner City Squatter Housing; (9) Upgraded Squatter Settlements; and

(10) Informal Plotted Housing in Protected Landstrips. Table 3 below summarizes each typology's characteristics, location, and tenure status.

These housing types span the spectrum of formality, from being informal to having formal tenure (discussed later in this chapter). For the purpose of this report, informal is defined as housing which lacks the required legal documents. Some housing types such as inner city squatter housing are mostly informal in character as households occupy land that does not belong to them legally. Other housing types, such as new multi-family housing or illegal subdivisions of agricultural land could be semi-informal as many may have a combination of some form of ownership or occupancy documents coupled with being illegal or un-authorized due to lacking building permits. To illustrate this further, many of the new buildings, for example, are not registered and households do not actually have titles, but use contracts with builders as proof of ownership. In the case of agricultural land subdivisions, most households are owners of the land, but did not acquire the permits needed to construct their dwellings.

Table 3: Housing Typologies Based on Spatial Analysis & Household Survey

	Housing Type	Predominant location	Visible Characteristics	Tenure Status**
1	Old Soviet Multi Family Housing (2-9 stories)	Inner City Baku, Eastern fringe of Inner City Baku, Inner City Sumgayit	<ul style="list-style-type: none"> *Soviet Style prefab housing *Average roof quality *Adjacency to medium-capacity asphalt roads (Collector roads) *Parking within plot - usually in the inner agora area *Rapidly deteriorating common spaces and facade *Lack proper management and maintenance 	Predominantly having formal tenure with titles
2	9+ Story Modern Apartments/ Multi- Family Housing	Inner city Baku, South-Western coastline.	<ul style="list-style-type: none"> *Good roof condition *Adjacency to high-capacity asphalt roads (Arterial roads) *On street car parking 	Ranges from semi-informal to formal. Many are built without having all required building permits and therefore can only issue a developer's contract without full title.
3	Planned Plotted Housing	Parts of the coastline, Inner city, Satellite town outskirts, peri-urban areas of Baku	<ul style="list-style-type: none"> *Mostly single family housing in older neighborhoods in Baku city *Grid-Iron Roads *Asphalt Road Surface *Uniform Size Plots *Good Landscaping *Good Roof Conditions 	Formal with titles
4	Organic Cluster Housing	Inner city Baku	<ul style="list-style-type: none"> *Good access to CBD & public transport *Mix of unplanned narrow roads and pedestrian pathways being used by small cars *Overcrowding *Once formal plot sizes now changing to more informal plot sub-divisions *Houses built very close to each other with limited ventilation and set backs *Some evidence of unauthorized construction and housing extensions *Mix of older formal housing with new unauthorized housing 	Mix of formal, semi-informal and informal ownership and/or having unauthorized/ construction

	Housing Type	Predominant location	Visible Characteristics	Tenure Status**
5	Temporary Housing	Eastern Baku, North-Central Baku	<ul style="list-style-type: none"> *Dormitories, schools, old multi-story houses *Dilapidated façade *Located near major roads with good connectivity *Significant improvements in adjacent areas EXCEPT on the plot with the Dormitory buildings *Deteriorated (old and weathered) roofs *Overcrowded (having between 3-5 members in one room) *Un-hygienic conditions 	Legally allocated by the State for temporary use/formal
6	New IDP Social Housing	Outskirts of Baku city	<ul style="list-style-type: none"> *Newly-built multi-family housing *Located near major roads, but in the outskirts of the city *Good social and community facilities in place 	Free (rental) accommodation for IDPs/no ownership titles
7	Illegal Subdivided Agricultural Land	North-eastern and Central-eastern parts of Baku, parts of Absheron	<ul style="list-style-type: none"> *Conversion of green, agricultural land into plots of unplanned residential areas *Very low population density *Prominent plot boundaries *(In recent settlements) Temporary, irregular winding dirt roads for access or (in older settlements) permanent dirt roads and are more visible as spatial features *Non-Uniform Plot Sizes *Poor quality roofs (Asbestos/metal sheets) 	Most have formal ownership titles for the land but subdivision and construction is usually illegal and do not follow planning norms
8	Inner City Squatter Housing	Parts of Inner city Baku	<ul style="list-style-type: none"> *High density housing *No visible roads or paths *Varying roof types *Slum like appearance from top view *Stark difference with surrounding areas *Encroached courtyards *Temporary materials 	Informal
9	Upgraded Squatter Settlements	Peri-urban areas	<ul style="list-style-type: none"> *Organic growth patterns *Well-built large housing estates *Generally dirt roads and pedestrian pathways *Far from public transport 	May have legal ownership of land but housing is informal by nature: lacking permits or following building and planning regulations.
10	Informal Plotted Housing in Protected Landstrips/Areas	Central Baku and Eastern-Central Baku	<ul style="list-style-type: none"> *Adjacency to exposed oil-wells, *Temporary dirt roads becoming permanent dirt roads over time *Irregular plot sizes *Haphazard plot arrangement *Protected areas consist of land around hazardous oil wells, railway lines, gas lines, sewerage lines, etc.) 	Informal

Old Soviet Multi-Family Housing (TYPOLOGY 1): Most of Baku city's housing stock is composed of 2-9 story, old Soviet-style, pre-fabricated, multi-family housing. According to the household survey, 74 percent of households in Greater Baku live in this type of housing. These buildings have remained mostly unchanged since 1991. They are located predominantly in the West-Central parts of the city in close proximity to the city's center. Some of these buildings have been demolished and redeveloped over the past decade. However, the majority have suffered from poor maintenance and many are in dilapidated condition. The neighborhoods where most of these buildings are located were formally planned, displaying distinct Soviet-style characteristics with buildings built around courtyards and with good vehicular access but limited parking availability. City administrators in Baku are facing serious challenges in managing and maintaining the old multi-family housing stock as these buildings rapidly deteriorate due to lack of maintenance of common areas (roofs, stairwells, walls, etc.). Household Survey results also indicate that respondents living in these buildings are highly dissatisfied with their living conditions and the management of their buildings by the public housing management companies called ZhEKs. The views of respondents are discussed in more detail on Chapter 5.

Figure 10: Modern (Left) and Old (Right) Multi-Family Apartments



Modern Apartments/Multi-Family Housing (TYPOLOGY 2): Within the last 5-10 years, new luxury apartments and condos, mostly in the form of high-rises, have rapidly emerged in parts of Baku's inner city. These buildings are mostly located in inner city Baku and southwestern Baku; they use modern construction materials and cater distinct to higher income groups. Time series images in Figure 11 below show one example of new luxury buildings being rapidly constructed over a span of 5 years. There is visible high-end real estate construction activity across Baku city, in some cases followed with positive improvements to the infrastructure in adjacent neighborhoods/areas. According to a UNECE Housing Profile of Azerbaijan, in the short time span between 2000 and 2005, 500 high-rise buildings (15–25 stories) and thousands of new luxury, low-rise buildings were constructed. However, many such developments were built before the 2008 financial crisis and appear now to be largely vacant. A number of these buildings have been built by private real estate developers who lack title to the land and who lack all the required building permits. As such, dwelling units are sold on the basis of a construction contract between the developer and the homeowner, making the arrangement semi-informal. Sales transactions are made on the basis of these contracts and since they are not legally recognized as ownership title, the sales are pre-dated for the new owner to the original date of sale.

Figure 11: Time Series Images of Rapidly Emerging Modern Multi-Family Apartments



Planned Plotted Housing (TYPOLOGY 3): Planned plotted housing is typically seen in the older neighborhoods of inner Baku city and also in city centers of the satellite towns of Sumgayit and Absheron districts. The residential areas are characterized by grid pattern roads, uniformly sized plots, and better landscaping/public green spaces. They are typically formally transacted and include titles. Planned plotted housing may also be comprised of government housing.

Organic Cluster Housing (TYPOLOGY 4): Inner-city, single-family cluster housing, despite being less predominant in the Greater Baku Region, has particular characteristics that are worth documenting. This type of residential housing can be observed in and around the old city. It is generally situated on narrow, congested streets; it is characterized by closely clustered, dilapidated old houses with or without inner courtyards; it is often overcrowded as multiple households rent one room among many at the same address; and many houses are inaccessible by vehicles, but connected by a network of narrow pedestrian paths. This type of housing is seen largely in the old quarters of Sovietski neighborhood, which is currently under demolition to make way for urban redevelopment efforts and a central park. These deprived residential neighborhoods started out as planned areas with a high concentration of low-income groups but over time developed slum-like conditions. There is a mix of both legal (older units) and unauthorized housing (newer); these have increasingly become a source of inexpensive single room tenements in Baku, resulting in overcrowding, with two or more families living in one house/structure. There is also evidence of illegal additions and extensions to original housing structures. Residents interviewed separately from the housing survey indicated that they were renting their units and that the only proof of residence they had was that their household was registered in the municipality.

Figure 12: Typical Organic Cluster Housing in Baku



Temporary Housing (TYPOLOGY 5): As a result of the conflict with Armenia, several dormitories, former schools, and old multi-family apartments in Baku have served as housing for Internally Displaced People (IDPs), refugees, and poor rural-urban migrants for the past two decades. Many of these IDP collective centers feature extremely poor and overcrowded living conditions, with families of five or more sharing one room, common toilets, and shared kitchen facilities on each floor. In a majority of cases, these buildings are severely dilapidated and should be considered condemned. Due to the lack of affordable housing in the market and the limited availability of social housing, however, IDPs are forced to continue living in temporary housing which are rapidly becoming Baku's "vertical slums." While the majority of IDP families and other refugees live in this type of housing allocated by the Government, other families squat in abandoned buildings around the city. Although the Government of Azerbaijan is doing a commendable job relocating IDP families to newly-built IDP social housing complexes in the periphery of Baku city, the waiting period ranges between 15-20 years or more. Most residents are reluctant or have little incentive to try and find better accommodations, even if their financial situation may be better than other IDP families in the same building.

Figure 13: Temporary Housing



New IDP Housing (TYPOLOGY 6): The Government of Azerbaijan has successfully relocated some IDP families to Social Housing Complexes in the periphery of Baku similar to the ones shown in Figure 14 below. The city government is in the process of building more of these complexes around the city; however, progress has been slow leaving many families desperate in their current living conditions. IDP families that are allocated new apartments have a life-time rental lease that allows inheritance rights, but do not have full title to the unit. Rent is free and utilities are largely subsidized. This was considered necessary by the Government to ensure apartments are not sold to families who are not entitled to IDP housing. The IDP housing complexes are of good quality and well-planned, and have community and recreational facilities. However, these apartments are located in the periphery of Baku city with limited access to public transport systems and employment opportunities in the city center.

Figure 14: New IDP Social Housing Complexes



Illegal Subdivisions of Agricultural Land (TYPOLOGY 7)²⁰: This type of housing is comprised of low-density housing developed mostly through illegal land subdivisions carried out in peri-urban areas. Across all categories, this showed the highest growth rate over the past five years, but satellite imagery analysis reveals that this form of urbanization has been happening at a large and rapid pace since 2004. Agricultural land is being converted into informal plotted housing in the mid-west, north-central, and east-central parts of the Greater Baku Region. This is happening more rapidly near existing asphalted regional and arterial roads, perhaps because of the higher regional accessibility. These settlements start off as organic pathways but over time due to sub-division activity are developed as a network of informal roads. Images show a significantly high rate of growth in unauthorized land subdivisions as well as conversion from agricultural uses to residential development. While residents in these settlements often have title to the land, as indicated by the household survey carried out under this study, the corresponding subdivision and housing construction is most likely done without planning permission and/or building permits. These new settlements are considered informal or unauthorized because they might violate land-use planning and the standard of infrastructure is low. The “Committee on Real Estate Registration Issues” confirmed that a majority of this housing is illegal. Conversion of land-use from agricultural to residential use is a complicated process that requires the municipality to submit a land-use conversion request to the Cabinet of Ministers for approval. Approvals are very rare and are limited to requests that are considered of national importance (such as in the case of a disaster, infrastructure development, etc.).

Figure 15: Low-density Illegal Subdivisions of Agricultural Land



Inner city High-density Squatter Housing (TYPOLOGY 8). Informal housing settlements have also emerged in the center of Baku city. This is mostly being done through the occupation of inner courtyards of existing multi-family housing or commercial complexes. Satellite imagery and field visits verify that encroachment is happening in such prime real estate locations given the proximity to jobs and infrastructure (See Figure 16). Construction materials used for these temporary constructions are easily distinguishable from the original, peripheral structures, which are formal in appearance.

²⁰ State Committee on Real Estate Registration Issues, “Policy Document on the Regulation of Informal Settlements in the Republic of Azerbaijan,” and Spatial Analysis data.

Figure 16: Inner-city High-density In-fill Squatter Settlements



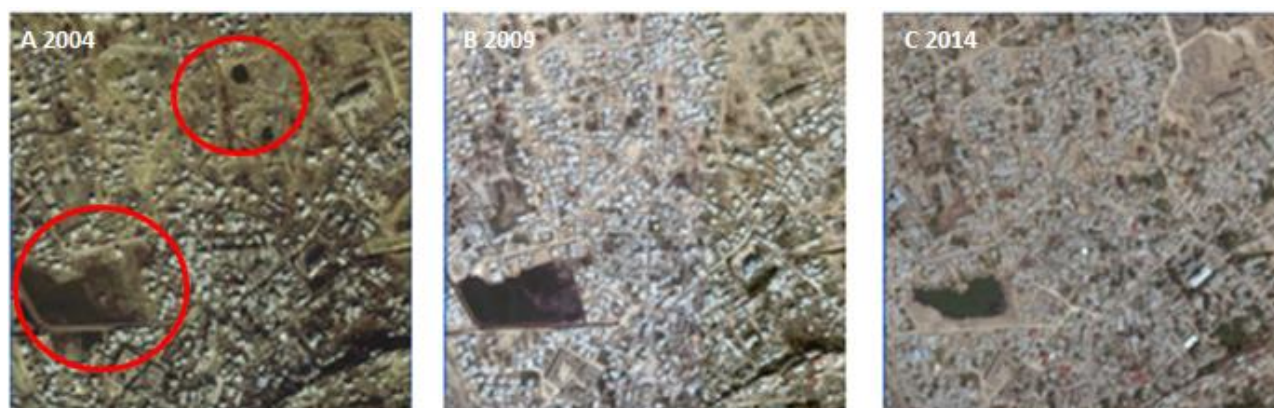
Upgraded Squatter Settlements (TYPOLOGY 9): These correspond to settlements that are mostly located in Absheron district and initially started as squatter settlements. Over the years, density increased and trunk infrastructure has been upgraded. In particular, there are visible improvements in the quality of roads as well as upgrades within plots. No subdivisions of land are observed. However, the periphery of these old squatter settlements has seen new developments emerge in the recent past from unauthorized conversion of land use.

Informal Plotted Housing in Protected Areas/Strips (TYPOLOGY 10): Finally, across the Greater Baku area there is a prevalence of informal housing on protected land, which was originally allocated as buffer zones for services lines and oil fields. According to the Land Code, no housing is permitted on land considered as protected strips/areas; these areas include land around high-voltage lines, drainage, railways, gas lines, sewerage lines, oil pipelines, and oil fields. However, there has been important growth in informal settlements on these lands. According to analysis carried out by the State Committee on Real Estate Registration Issues (with support from the World Bank Real Estate Registration Project), as of 2014 there were 51,453 households living on protected areas across Greater Baku (which also includes Absheron and Sumgayit) and in Ganja - 8,897 of which were located around water and sewerage lines, 3,194 around gas pipelines, 2,216 around oil pipelines, and 37,146 around oil wells. The growth has been partly supported by the State. In fact, in order to accommodate rapid urbanization due to rural-urban migration, close to a 1,000 (of the 51,453 total households) were developed based on authorizations given by the State²¹ - 78 by Baku City Executive Power, 436 by local executive powers, 26 by certificates given by various State agencies, 204 based on resolutions passed by municipalities, and 27 by oil companies. Encroachment of hazardous areas not appropriate for human settlement is therefore a common practice in central and eastern Baku. Airport

²¹ State Committee on Real Estate Registration Issues, "Policy Document on the Regulation of Informal Settlements in the Republic of Azerbaijan," and Spatial Analysis data.

Highway (E-W), Zabrat Highway (N-S), Amir Baghirov (E-W), Binagadi-Balakhani Highway (E-W), and Novkhany Highways (N-S) provide excellent connectivity from these areas to Inner Baku and the rest of the region. It is therefore possible that households settling in these areas appear to value high accessibility over environmental safety, as a trade-off when choosing housing location. Although the development of housing in these areas is not recent, and these informal settlements do not occupy a significant amount of land, there has been an important intensification of the built-up area and densification over the last decade (See Figure 17).

Figure 17: Informal Plotted Housing in Protected Areas/Strips



2. Increasing Incidence of Informal Housing

Housing is a fundamental pillar in the development and well-being of people and having informal tenure does not allow households to fully exploit the potential of housing. The literature suggests that households having informal ownership tend to invest less in their dwellings.²² Informal tenure also often prevents households from accessing mortgages or capital improvement loans and has been associated with both lower access to credit for business development and higher interest rates.²³ Finally, informality often limits households from benefitting from the full economic opportunities of living in cities. Studies have shown that formalizing informality can have important benefits that range from an increase in housing investment, a reduction in household size, enhanced education, and increased labor market participation.²⁴

Informality in the Greater Baku Region, as in many other cities, is also associated with lower accessibility to jobs and social infrastructure, poorer neighborhood characteristics, and limited access to - and quality of - services. As observed in Figure 18, there are large variations in both access and accessibility indicators when comparing households that have no documents to prove ownership to those having full-ownership documents (Real Estate Registry). While households having Real Estate Registry documents have almost universal access to piped water, piped gas, solid waste collection, and sewers, the situation is radically different for those that do not have any documents, particularly regarding availability of individual toilets, sewers, and solid waste collection. These limitations are reflected in people's perception of the quality of their services. Households with no documents rate as 'Poor' the quality of water supply (46%) and solid waste collection (60%), while those having Real Estate Registry documents rated those services 'Poor' only 24% and 14%, respectively. Informal households also tend to live further away from the Central Business District, where many of the job opportunities are concentrated. This, in turn, does not allow households to benefit fully from the opportunities available from living in this metropolis.

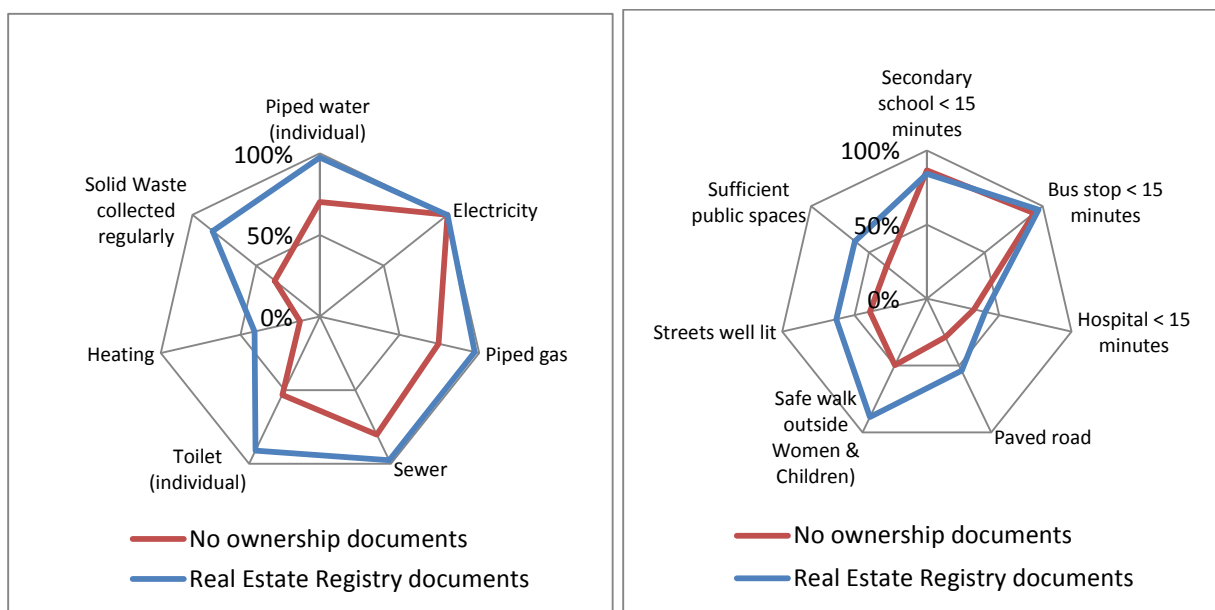
²² Field, E. (2005) Property rights and investments in urban slums. *Journal of European Economic Association*

²³ Field, E. and Torero, M. (2006) Do property titles increase credit access among the urban poor? Evidence from a nationwide titling program. *Harvard Working Paper*

Galiani S. and Schargrodsky, E. (2010) Property rights for the poor: Effects of land titling. *Journal of Public Economics*

²⁴ Field, E. (2007) Entitled to work: Urban property rights and labor supply in Peru. *Quarterly Journal of Economics*

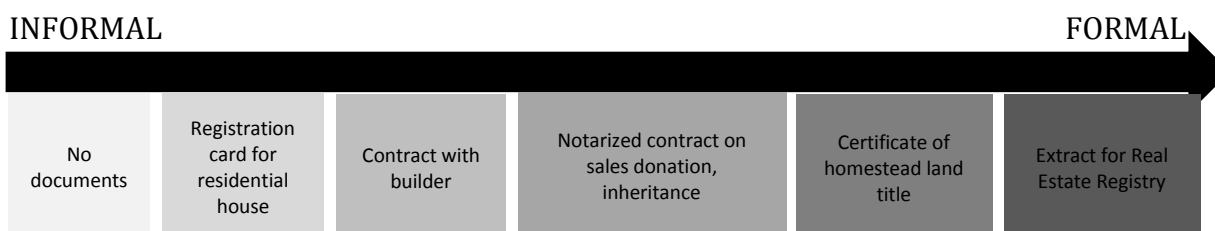
Figure 18: Access to services and neighborhood characteristics: formal and informal tenure



Source: World Bank, *Greater Baku Household Survey* (2014)

The informal settlements have grown exponentially in the last decade. According to a study²⁵ carried out for the State Committee for Real Estate Registration Issues and funded by the World Bank,²⁶ an analysis of the establishment dates of 11,744 informal settlements in Greater Baku indicates 47 were developed in the 1920s, 13 in the 1930s, 27 in 1940s, 70 in the 1950s, 182 in the 1960s, 321 in the 1970s, 450 in the 1980s, 4,518 in 1990s, and 6116 after 2000 alone.

It is estimated that around 20 percent of households in the Greater Baku Region do not have the required ownership documents for their housing structures and/or their land. Recognizing that informality is not a YES/NO answer, but that there is an informal-formal continuum, households were classified into six categories depending on the type of ownership documents they possessed (see informal - formal spectrum chart below). As households often have multiple documents, the tenure formality classification for each household was determined by the highest level of formality of the ownership documents at hand. For example, if a household had a certificate of homestead title and a registration card, it was classified as having a certificate on homestead land title. It is estimated that – among the 20 percent with informal or semi-informal tenure - around 50 percent of households have no documents to prove ownership, while an additional 35 percent only have a registration card that proves where they live; the remaining 15 percent have either a contract with builder, a notarized contract on sales or inheritance, or a certificate of homestead land tile.



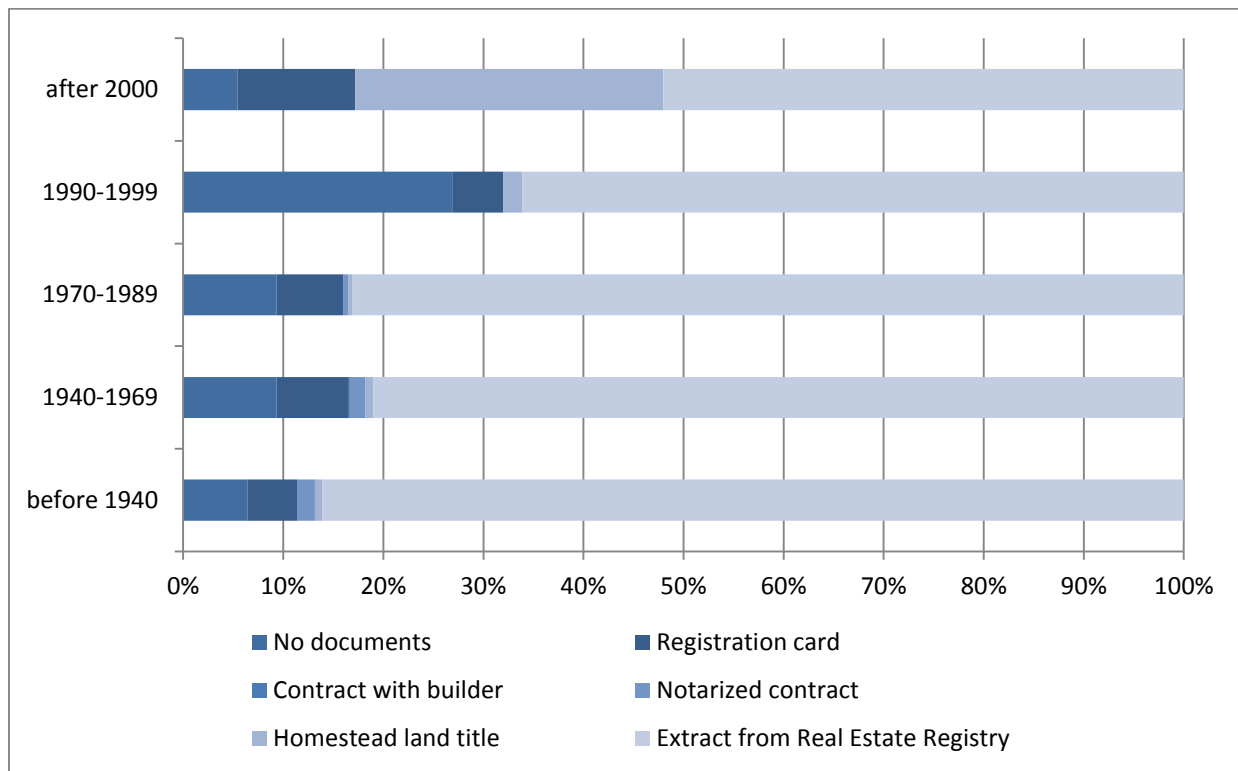
While the share of the housing stock that is considered informal in Baku is not large, data shows that informality has grown considerably in recent decades and is today one of the main forms used to access

²⁵ Committee on Real Estate Registration Issues, "Policy Document on the Regulation of Informal Settlements in the Republic of Azerbaijan"

²⁶ Funded by the World Bank Real Estate Registration Project

housing (See Figure 19). The informal housing sector grew considerably after the fall of the Soviet Union – between 1990 and 1999 – and increased further after the year 2000. In fact, over the past decade almost half of the housing units that entered the system were not fully formal. While there was a decrease in the share of households having no documents to prove ownership, there was an important increase in the share of households that had a title to land but that did not have an extract form from Real Estate Registry. This is a reflection of the growth of the city towards the periphery and the use of agricultural land subdivided to access land. In fact, many households are able to acquire land through legal means, but find it difficult to construct their dwellings legally in terms of getting construction permits and ultimately obtaining an Extract from the Real Estate Registry. The high costs of getting permits and registering housing structures was mentioned in the qualitative assessment as one of the main barriers for having full formality.

Figure 19: Growing tenure informality in recent years



The household survey revealed that unemployed and IDP households are much more likely to live in informal housing. 61 percent of IDP households do not have any ownership documents, despite considering themselves to be the owners of their dwellings, compared to 2 percent of non-IDP households. The situation is particularly interesting when comparing employment status. While only 7 percent of full and part-time employed households and 8 percent of pensioners live in dwellings with no ownership documents, this number climbs to 32 percent for unemployed households.

Informal housing typologies also vary according to the year of arrival to the city with unplanned land subdivision as the leading type of growth of informal housing in the past decade. While 62 percent of households with no documents have been in the city for more than 20 years, most of those who have land titles but constructed their houses illegally arrived in the city in the past 10 years. This suggests that there has been a shift in informality from squatting - most probably linked to high urbanization rates and the Armenia-Azerbaijan conflict - in the years following independence towards informal land subdivisions in the periphery of the city in the most recent decade.

These findings suggest that the housing market is not reaching its full potential and is pushing households to the informal housing market to find accommodation. Informal housing is growing in hazardous areas, which

has a negative impact on residents' health and safety. In addition, the multi-dimensional character of informality (i.e., poor access to services, lower neighborhood quality, reduced access to jobs, higher representation of vulnerable households) suggests that this is an issue that needs to be tackled with an integrated approach to be able to ensure social cohesion and inclusion.

CHAPTER 2: Housing Market

While the supply of housing in Greater Baku is keeping up with projected demand, several challenges remain. Newly-constructed housing is generally too expensive and unaffordable for the vast majority; new multi-family buildings (MFBs) lack adequate management and maintenance capacity and have a high vacancy rate due to mass speculation; and most importantly, a large percentage of these MFBs lack formal title. Old housing mostly dates from the Soviet period and is of extremely poor quality due to poor maintenance; it is, however, properly titled and more affordable than new housing. While the Government has invested significantly in façade beautification of some old MFBs in the prime areas of Baku, these projects do not address the core maintenance and upkeep issues of old buildings.

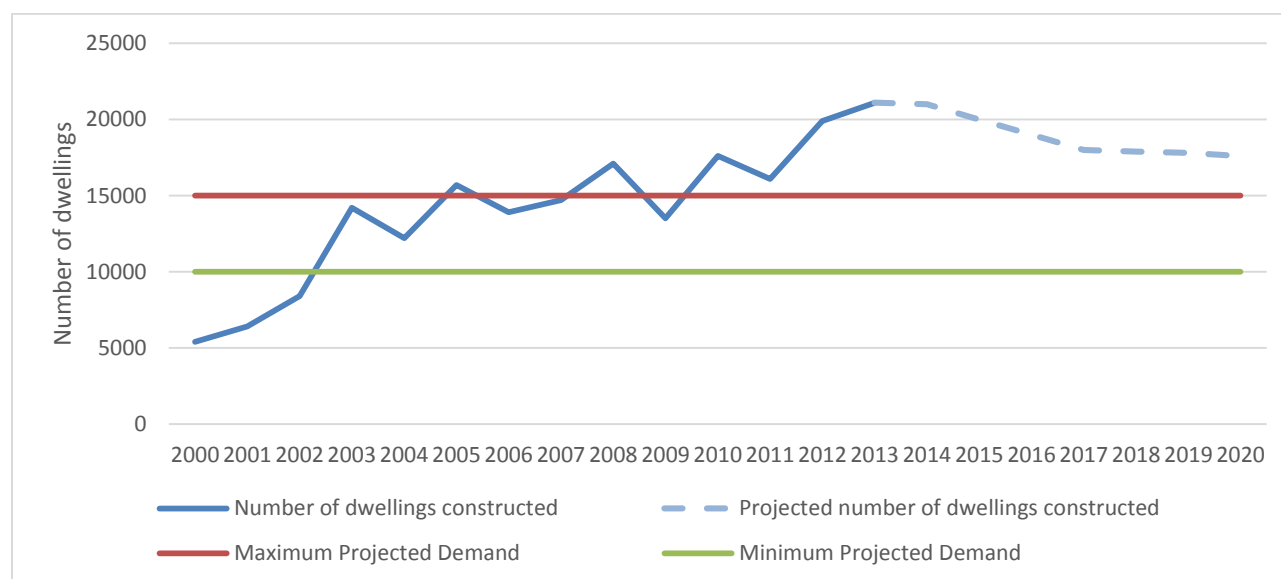
In the absence of comprehensive data on the residential real estate market, this section relies primarily on information collected from interviews, primary data collected through the household survey and data provided by stakeholders in the sector.

1. Housing Stock and Quality

1.1 Demand and Supply

The total area of housing stock in Azerbaijan has increased approximately 30 percent since independence in 1991. It passed from 88.2 million m² in 1991 to 114.5 million m² in 2010.²⁷ There are currently 1,887,673 housing units in Azerbaijan with 502,159 housing units in Baku alone.²⁸ With 1,895,941 households in Azerbaijan and 470,996 in Baku, this suggests a small housing deficit nationwide (approximately 8,000 units) and a surplus of approximately 30,000 housing units in Baku. However, the number of households on the Absheron Peninsula is expected to grow to 840,000-910,000 households by 2030 depending on population growth rates.²⁹ This correlates to an increase of approximately 210,000-270,000 dwellings, or an average of 10,000-15,000 units per year. Data from the State Statistics Committee show that that an average of 14,200 units were submitted into use every year between 2000 and 2013.

Figure 20: Number of dwellings introduced into use compared to projected demand



Source: State Statistics Committee publication (historic)

²⁷ While housing area is not the ideal measure of housing stock, this data is used due to the lack of data on the total number of housing units submitted into use and housing units in existence.

²⁸ State Statistics Committee, "Housing Stock 2013."

²⁹ State Committee on Urban Planning and Architecture/Baku State Design Institute, *Greater Baku Regional Development Plan (GBRDP)* (2015).

New housing

The share of new housing in the Greater Baku housing market was 14.7 percent in March of 2015, and the average size of new housing units transacted was 116 m².³⁰ However, the price of new housing went down 15.2 percent in March 2015 compared to the previous month, perhaps as a result of the devaluation of the New Azeri Manat by 30 percent in February 2015.³¹ While the volume and price of new housing has generally increased over the years, market participants indicate that there is currently stagnation in the market and the rate of construction is now leveling off. The volume of new housing commissioned in Azerbaijan decreased by 23.3 percent in May 2015 compared to April 2015, a trend similar to the one observed in the early months of 2015.³²

Multi-family buildings (MFBs) typically include the following types of units:³³

- Studios ranging from 30-40 m²
- 1-bedrooms (BR) ranging from 45-65m² (economy unit)
- 2-BRs ranging from 70-100m² (economy unit)
- 3-BRs ranging from 110-150m²
- 4-BRs ranging from 160-200 m²

Most of the new developments are being undertaken without a proper market demand analysis (as would be common practice for a mature market), and consequently, the types and prices of units coming into the market do not necessarily meet the demand. This is demonstrated by the fact that while developers contend that economy units ranging from 45-100 m² are the most in demand, the average size of housing units in newly built MFBs in Baku is 113 m², as reported by the State Statistics Committee. This is very large by most global standards.

While new construction within Baku proper is dominated by multi-family buildings (MFBs), the outskirts of Baku and the rest of the Absheron peninsula have witnessed the development of self-built houses, in many cases on informally converted agricultural land. Typically, a developer buys a large tract of land and subdivides and services it with basic infrastructure. These subdivided parcels are then sold to individual households, who in turn, use a microfinance loan (AZN10K-20K) or their savings to build a house incrementally. The cost of a basic core house - 1 room with toilet and kitchen, totaling about 35m², using local, inexpensive limestone blocks - is about AZN10K. This usually covers the first phase; additional rooms are then added over time. These home builders are typically in-migrants from the regions.

Figure 21: New housing on the outskirts of Baku



Note: This house is located in a new neighborhood on the Absheron Peninsula built on informally converted agricultural land

³⁰ *MBA Housing Market Indicators*, March 2015.

³¹ *Ibid.*

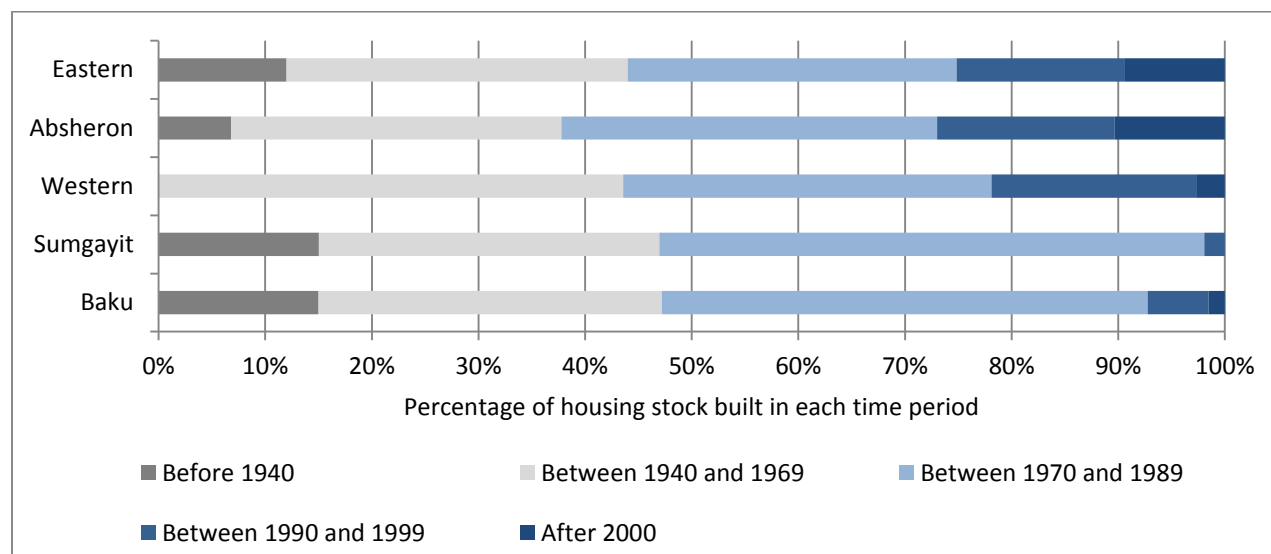
³² 'Azerbaijan's housing commissioning grew by 16.2% in Jan-May.' <http://abc.az/eng/news/89023.html>, accessed 15 June 2015.

³³ Sizes are approximations from data gathered from interviews with housing market stakeholders.

Old multi-family housing

As mentioned in the previous chapter, the bulk of housing in Greater Baku dates back to the Soviet period. Much of this housing is generally in poor condition (See Chapters 1 and 6 for more details), but it is ‘titled’ and more affordable than new housing (discussed in detail in the next section). As illustrated by Figure 22 below, over 40 percent of housing in Baku was constructed between 1970 and 1989 and 30 percent between 1940 and 1969. The average size of old housing units transacted was 84 m² and the share of old housing in the housing market was 85.3 percent in March 2015.³⁴

Figure 22: Age of the housing stock by Greater Baku zone



Source: World Bank, *Greater Baku Household Survey* (2014)

1.2 Housing Quality

It is estimated that 2 million Azerbaijani's (20 percent of the population)³⁵ live in sub-standard and deteriorated housing. More than 80 percent of residential buildings, according to a UNECE housing study,³⁶ were built 40-50 years ago, 30 percent of which require urgent repairs or reconstruction. 18 percent of this stock was pre-fabricated multi-family housing estates built in the 1950s.³⁷ Housing industry indicators deem that structures older than 30 years have begun to show deterioration and require reinvestment to maintain their quality, and housing older than 50 years requires major renovations. If regularly maintained and properly managed, this stock, although ageing, is a large resource of affordable housing..

Age of Multi-family Housing Stock

Baku city reflects of the nation's state of having relatively old and rapidly deteriorating housing stock (Figure 23). The median age of the city's housing stock is 40 years³⁸ with the majority constructed between 1940 and 1970 (32.4 percent) and between 1970 and 1990 (42.9 percent). Around 77 percent³⁹ of this stock is in the form of multi-family buildings, rising to 81 percent if IDP collective centers (generally consisting of multi-story dormitories) are also counted. The varying periods of construction present different challenges in terms of housing quality and maintenance requirements. The Greater Baku Regional Development Plan categorizes housing in Baku into six age categories: i) MFBs built prior to 1920 (mostly located in Baku old city) are

³⁴ MBA Housing Market Indicators, March 2015.

³⁵ European Commission - Support to Azerbaijan Housing Sector - "Gap Analysis Report: Support to Housing Policy Reform," November 2013.

³⁶ UNECE, "Country Profiles on Housing Sector- Azerbaijan" (2010).

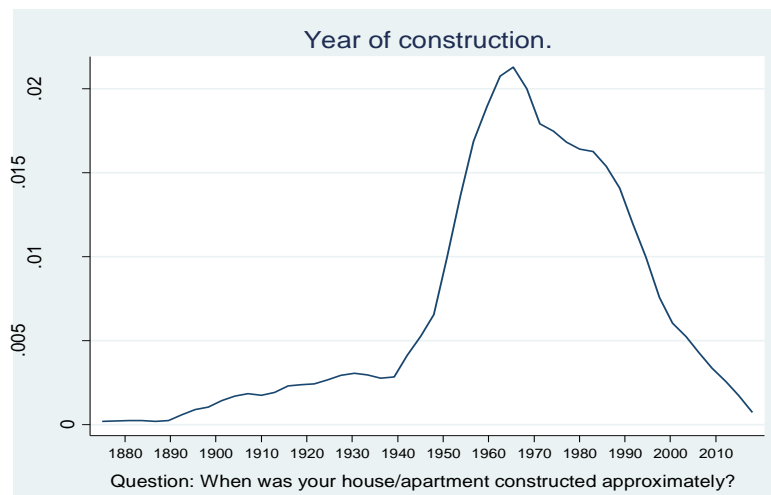
³⁷ UNECE, "Country Profiles on Housing Sector- Azerbaijan" (2010).

³⁸ World Bank, *Greater Baku Household Survey* (2014).

³⁹ World Bank, *Greater Baku Household Survey* (2014).

considered historic and have received special financing from the State towards rehabilitation; ii) units constructed before the WWII (1920-1940) that are of better quality than the old MFBs but deteriorating rapidly; iii) units from the 1950s-1960s consisting of Soviet-style, pre-fabricated MFBs based on mass construction techniques that have short life-spans and are highly energy inefficient due partly to the low quality of materials; iv) housing built in 1970s-1980s that is also predominantly pre-fabricated MFBs of low quality; v) single-family housing that emerged in the 1990s; and vi) high rise luxury apartments developed by the private sector development post-2000.

Figure 23: An ageing housing stock



Source: World Bank, *Greater Baku Household Survey* (2014)

Housing Quality Index (HQI)

Over the last two decades, the quality of the housing stock has deteriorated considerably in the Greater Baku Region. The typical problems are crumbling facades, broken windows, and visible cracks in walls and floors, as well as issues linked to maintenance in multi-family buildings such as non-working lifts, dilapidated common areas, and poorly-maintained facades. To assess the current state of the housing stock in Baku, a Housing Quality Index (HQI) was developed for this study (See Box 2). The HQI rating ranges from 0 to 100; a maximum score of 100 indicates the worst housing conditions and that a specific household reported having housing issues across all seven housing quality indicators as outlined in Box 2.

Multi-family buildings are in considerably worse condition than single-family houses. Multi-family buildings have an HQI of 77 while single-family houses fare better with an HQI of 37. This means that 77 percent of surveyed households living in multi-family buildings reported having one or more housing quality problems. Non-working lifts and the bad state of building façades were some of the most common problems present in common areas while broken windows were one of the main problems reported inside the dwellings. This reflects persistent issues with the maintenance of multi-family buildings and their common areas, particularly since residents believe that common property is the “extension of the street” and therefore the responsibility of the State.

Among the locations of the Greater Baku Region, Baku and Sumgayit city have the highest HQI. Sumgayit has an HQI of 80 while Baku scored 72. The Western suburbs and Absheron satellite city have the lowest scores, indicating that the quality of housing in these zones is better. However, the observed differences can be mainly explained by the different housing typologies present in these areas. Baku and Sumgayit both have the highest concentration of MFBs and a large share of their housing stock was built between 1960 and 1990. On the contrary, the Eastern and Western suburbs, and Absheron satellite city, have a newer - on average - housing stock and a higher predominance of single-family houses.

Box 2: Housing Quality Index

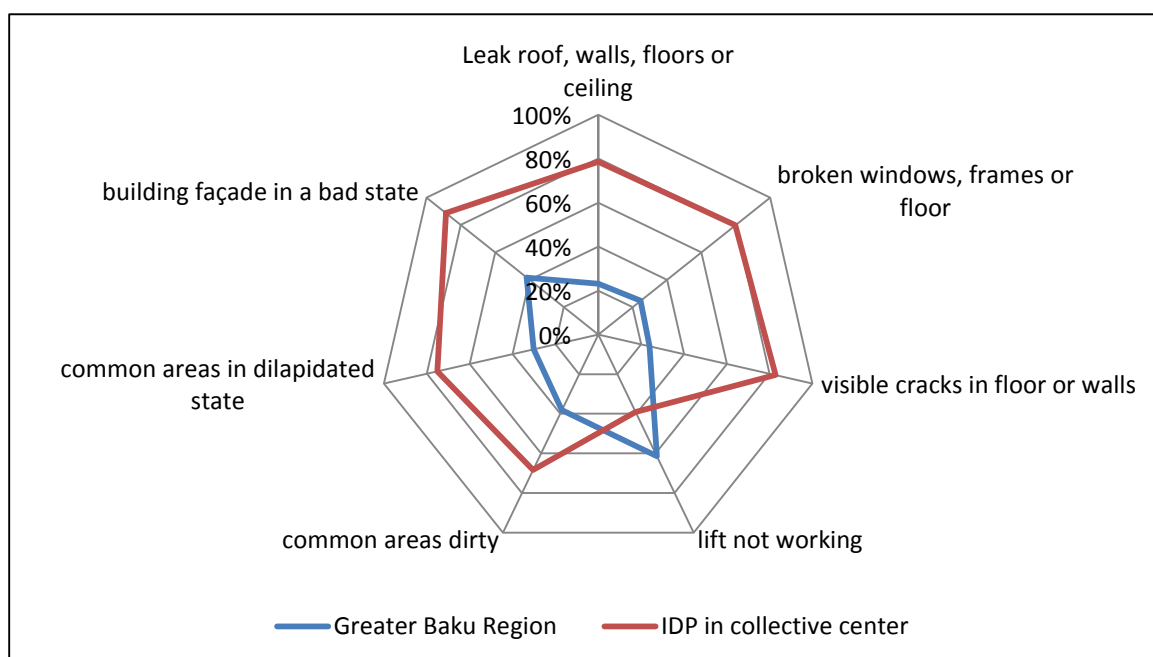
A Housing Quality Index (HQI) was developed to summarize the current structural state of housing and the condition of communal areas in multi-family buildings. The HQI was constructed based on seven housing quality indicators (three housing quality indicators and four indicators for common areas in multi-family buildings) collected in the household survey conducted in the Greater Baku Region in 2014 and is based on whether households reported having one or more of the following housing problems:

1. Leaking roof; wet walls, floors, or ceiling
2. Broken window, frames, or broken floor
3. Visible cracks in floor or walls
4. Common areas are dirty (multi-family buildings)
5. Common areas are in a dilapidated state (multi-family buildings)
6. Lift is not working (multi-family buildings having a lift)
7. Building façade is in a bad state (multi-family buildings)

HQI scores range from 0 to 100, with a 100 score representing the worst housing conditions.

Internally Displaced People (IDP) households, the unemployed, and those without legal tenure (proof of ownership or residence) live in multi-family housing with the worst conditions. They have the highest HQI scores, as compared to other residents. Important differences in the quality of the housing stock are observed when comparing the HQI scores across population groups, housing, and tenure types. The difference in housing quality for IDPs and non-IDPs is striking: 84 percent of IDPs reported having one or more issues with housing quality and common areas compared to 67 percent for non-IDPs. IDPs scored more than 50 percentage points across the seven housing index indicators presented in Box 2. Among IDPs, those living in collective centers presented the most precarious conditions with a HQI of 95 percent. Important differences are also observed based on the employment status of the head of the household. While unemployed and pensioners scored a HQI 74 and 79, respectively, fully-employed households scored 66 percent. In addition, households having no legal proof of ownership and renters live in dwellings of poorer quality. While 38 percent of those having full proof of ownership reported issues with housing structures and common areas, this number rises to a HQI of 76 percent among those having no ownership documents. Renters scored 82 in the HQI, while owners scored on average 68 percent.

Figure 24: HQI Greater Baku Region and IDPs living in collective centers



Source: World Bank, *Greater Baku Household Survey* (2014)

2. Housing Finance

This section reviews the terms, attributes, and availability of the dominant housing finance products available in Azerbaijan: (i) ‘standard’ and ‘social’ loans offered through the Azerbaijan Mortgage Fund; (ii) market-rate commercial products offered by private banks; and (iii) housing microfinance products offered by microfinance institutions. While the terms of various housing finance products differ across financial institutions, this section presents several specific, indicative examples to illustrate the range of housing finance products available to consumers.

2.1 Azerbaijan Mortgage Fund

The Azerbaijan Mortgage Fund (AMF) was established in 2005 and became operational in 2006. It received its initial funding from the State budget, and in 2009, started issuing covered bonds (with a 3 percent return). Its primary function is for re-financing of home mortgage loans made by authorized “agent” commercial banks. The AMF received USD 100 million in State funding in 2014, and USD 40 million in 2015. There are about 16,500 outstanding loans in May 2015 - all in Azeri Manats (AZN). The Central Bank provides liquidity support to the AMF by buying bonds, if needed. The risk of borrower default is retained by the agent bank. The default rate to date has been low at about 1 percent. The AMF re-finances two types of mortgage loans for ‘agent’ banks, both with a cap of AZN 50,000 (~USD 47,500) as described in the table below. The table below presents a description of the different options for housing finance under the AMF – as of May 2015 – and might not reflect recent changes in the design and funding of the AMF.

Table 4: Azerbaijan Mortgage Fund

Type/Source	Description
<i>Social loans (funded by State budget)</i>	These are subsidized loans at 4 percent interest, with a term of 30 years. The target group comprises special social categories: military personnel and young households (<35 years) who are civil servants, refugees, or sportsmen. A potential borrower must have proof of salary and adequate collateral to receive a social loan. Social loans take about four months to process. The 4 percent interest includes a 1 percent return to the AMF and a 3 percent margin for the banks.

Type/Source	Description
	The agent bank reviews and approves the loan application, and sells the loan to AMF, which then collects the loan repayments through an electronic transfer.
<i>Standard loans/ "commercial" loans (funded by bonds and State budget)</i>	These loans have an 8 percent interest, with a term of 25 years. These loans are open to all categories of beneficiaries, and follow the conventional underwriting procedures requiring proof of salary and adequate collateral; informally-employed people are not eligible. Given that the market interest rate for such loans is 2-3 percent higher, standard loans from the AMF are in high demand.

2.2. Mortgage Market

The mortgage market in Azerbaijan has picked up in recent years and at least part of the credit goes to the AMF, which has helped stimulate the market. However, with the recent devaluation of the AZN, many commercial banks incurred major losses and have stopped issuing mortgages until the economic environment becomes more predictable and stable. Examples of mortgage products offered by the leading banks are described in Table 5.

Table 5: Housing mortgage products by offering financial institution(s)

Type/Source	Description
<i>Access Bank</i>	Access Bank offers mortgage loans capped at USD 150K for 10 years at an interest of 12 percent and a down payment of 20 percent. Corporate clients may receive a 1-2 percent discount on the interest rate. All official household income is taken into account, and in special cases, unreported income may be taken into account where it can be adequately verified.
<i>TBC Credit</i>	TBC Credit offers mortgage loans capped at USD 200K for 10 years at an interest of 14 percent and a down payment of 30 percent. Their average loan size is USD 60K, which reportedly is sufficient to buy an apartment in the secondary market (typically an old Soviet flat in a neighborhood removed from the city center). TBC sometimes offers lower down payments (10 percent) on housing loans for first time borrowers due to the perceived lower risk of default. ⁴⁰
<i>Xalq Bank</i>	Xalq Bank has a mortgage loan portfolio of AZN 100 million, some 40 percent of it from the AMF, and 60 percent from the bank's own internally-funded loans. Their internal loans are offered at 10-12 percent interest for a period of 25 years, and the loan amounts range between AZN 10K-500K. The average mortgage size is AZN 120K-130K. All mortgage loans offered by Xalq Bank are in AZN. Xalq Bank limits monthly loan re-payments to a maximum of 30 percent of net monthly income.
<i>Multiple institutions</i>	Some banks, such as Xalq Bank, also offer 'special' loans to buyers of houses in affiliated housing developments in which the bank enters into an arrangement with the developer for a specific project. These are typically for budget or 'economy' apartments priced between AZN 80K-100K. The construction company guarantees the loans for these units for three years after which the Construction Contract (equivalent to a title for unregistered properties) is handed over to the bank in lieu of the guaranty. The interest is typically 10 percent for a term of 25 years.

2.3. Home Improvement Loans and Housing Microfinance

There are a total of 48 licensed microfinance institutions (MFIs) and four credit unions in Azerbaijan. Some 38 of these are currently members of the Azerbaijan Microfinance Association. Several types of home

⁴⁰ This is because, while it might not be uncommon for a person who owns multiple assets to take a loan against one asset and default on the payment, those with just one house generally do not default or fall back on payments willfully.

improvement and housing microfinance (HMF) loans products are offered by banks and MFIs, as illustrated in Table 6.

Table 6: Home Improvement Loans and Microfinance

Type	Description
<i>Home Improvement Loan (with Fixed Asset)</i>	These are offered by some banks in tranches for construction or repair work. For example, Access Bank offers home improvement loans for a 5-7 year period with a cap of USD 150K. The typical loan size is USD 20K. A down payment of 20 percent is required, with collateral in the form of a registered property (fixed asset).
<i>Construction and Renovation Loan</i>	TBC Credit offers construction and renovation loans of USD 15K-50K at 18 percent interest for up to 36 months. These are mostly for interior improvements or completion of a house under construction. All of TBC's collateralized loans are in USD. TBC also offers consumer cash loans, 20 percent of which go into housing construction or renovation. These are in amounts less than USD 15K and no collateral is required. The interest is 20 percent for USD loans, and 28 percent for AZN loans. TBC Credit is considering introducing an HMiF product that offers loans of USD 5K-6K for 4-5 years at 20-25 percent interest with no collateral requirement.
<i>Microcredit and Housing Microfinance (with soft collateral)</i>	Several MFIs offer HMiF products. For example, Azer Credit, established in 1996 with the objective of providing small business loans to IDPs and refugees, today has diversified its portfolio to include micro-enterprise loans, consumer loans (since 2006), and "family" loans (since 2011). Azer Credit today has 46 branches in 34 districts and some 20,000 housing loans. The family loans are most commonly used for housing improvement and are offered in cases where such improvements also bring about improvements to the business. The most common improvements financed by these loans are combi-heating (heating and hot water) and addition of bathrooms. Habitat for Humanity's Microbuild project provided financing of USD 4 million (at 7-8 percent interest) to Azer Credit to provide housing loans together with some technical assistance on the proper estimation of home improvement costs. The family loan is capped at USD 5K, with at least 30 percent of the improvement cost paid by the borrower. The interest rate for AZN loans is 40 percent for the first cycle and 27 percent for the second cycle. The loan term is capped at 30 months, but the average loan has been 14 months. All loans are 100 percent collateralized. Accepted collateral includes gold (<30 percent of total loan amount), a guarantor, or other personal assets co-signed by family members. There is a pre-payment penalty of 2 months' interest payment.
<i>Finance for Development (FinDev)</i>	FinDev offers business loans (maximum of AZN 15K) and housing loans (maximum of AZN 7K). The latter are provided for home improvement and expansion, construction of houses in the regions, and purchase of land. ⁴¹ The target population is low-income households. The interest rate is determined by a range of factors, among them the purpose of the loan (business versus non-business), the employment of the borrower (salaried versus unsalaried), the loan currency (AZN versus USD), and the type of guarantee (third party or family) or collateral (soft versus hard ⁴²). The broad interest rate range is 24-32 percent; the maximum loan size is AZN 10K for a maximum duration of 30 months. Some 10 percent of loans on FinDev's portfolio are housing loans, amounting to about AZN 2.5 million. According to FinDev representatives, the housing loan is a very attractive product. FinDev's liabilities (funds) are in USD as are their assets (loans), but they are now seeking to increase their AZN portfolio. Particularly in light of the recent devaluation, their clients prefer AZN loans, even though they are more expensive than USD loans.

⁴¹ AZN 10K-15K is sufficient to buy a plot of land in the regions, or do a basic renovation for a 1-bedroom unit in the city.

⁴² Hard collateral is not preferred.

Type	Description
FINCA	FINCA provides microfinance to self-employed people and small businesses in the form of business loans and consumer loans. Micro-loans are for amounts less than USD 25K, with a collateral of 120 percent of loan value. For uncollateralized loans, a guarantor is required. The interest rate varies between 20 percent and 35 percent depending on the transaction cost. The maximum term of the loan is three years. Although FINCA does not currently offer HMiF products, it allows 20 percent of the loan amount to be used for “other” purposes, which it reports commonly go towards the improvement of the borrowers’ house.

3. Housing Market Challenges

3.1. Housing Market Constraints

New housing – Multi-family buildings (MFBs)

New MFB units are very expensive. The price range of “white-frame” units in an average quality building in an outer city location is AZN 1,100-1,400 per m². The cost of finishing the unit is estimated at an additional AZN 300-350 per m², which brings the actual cost of these units (for the buyer) to about AZN 1,400-1,750 per m². Fully finished turnkey units are typically luxury flats or single-family houses, priced well beyond the affordability of the average resident and targeting mostly the expatriate community (See Chapter 3 for a detailed discussion on house prices and affordability). Several factors contribute to this extremely high price of new housing, including: (i) an immature property market and relatively unstable prices; (ii) the absence of a property valuation system;⁴³ and (iii) hidden payments reportedly made by developers to public authorities for utility connections, miscellaneous permits, and ownership titles.⁴⁴

Furthermore, newly constructed MFBs present high vacancy rates. The inherent and deep-rooted culture of homeownership in Azerbaijan, together with a lack of other stable investment opportunities in the country, has made residential real estate very attractive for both first-time home-buyers as well as large-scale investors. Both small- and large-scale investors are pouring money into residential real estate, both buying new housing units in bulk⁴⁵ for speculative purposes, as well as constructing residential developments, which is also a lucrative business. Moreover, the bulk of the units in MFBs coming into the market are ‘white-frame’ construction, with no finishes or fixtures, and people purchasing these for investment purposes prefer to leave them unfinished and keep them vacant rather than putting in additional money to finish the units and rent them out. As a result, barely a quarter of new built-up residential space that has been sold and in private ownership is occupied.⁴⁶ This is evident from the large number of residential towers that are unlit at night. This vast amount of essentially ‘unused’ vacant residential space sheds new light on otherwise rather optimistic housing data reported by the State Statistics Committee: broad national-level housing indicators hide the “housing inequity” occurring at the local level, particularly in Baku, characterized by massive overcrowding in certain areas and under-crowding (vacancy) in others.

⁴³ Property valuation is currently based on the 1998 Law of Valuation of Real Estate. A new draft law was prepared and submitted to parliament three years ago, but it has not moved forward. In the meantime, there are still no licenses for valuers. When resettlement is required, compensation is often based on a valuation done by a self-proclaimed valuation company, which may have never existed before and has suddenly come into existence..

⁴⁴ The authors of this report met with several developers, but none were very forthcoming in terms of sharing their pricing formula, their profit margins, or their sources for financing for such housing developments. These figures are a very rough illustration of the cost breakdown, based on information consolidated from multiple sources.

⁴⁵ In some cases, 15-20 units at a time.

⁴⁶ Although there are no data to verify this, the vacancy rate in Azerbaijan’s housing stock is estimated to be between 10%-30%.

Figure 25: Typical newly-constructed MFB in Baku



A significant percentage of new housing is considered “illegal” or “incomplete” because it is either built on land that is not titled and/or the property is not registered. Reportedly, only about a tenth of all land parcels in Greater Baku have proper documentation. Different sources indicate different numbers for the extent of this “illegality,” but range between 50-80 percent of all new MFBs. Another source puts the number as exceeding 450,000 housing units in Baku alone. According to MBA, the first step to documenting property is registering the underlying land. Land registration is very complicated in Azerbaijan – multi-staged, and time-consuming – and can take anywhere from three months to three years. Very commonly, developers of new housing skip this process and build on untitled land, which technically renders the building “illegal.” As a result, most new multi-family housing is not – and under the current legal framework cannot be – formally registered. Also, the process of formally registering property is lengthy and bureaucratic: some 100 documents are required, involving 132 steps.

Given the large number of illegal units without titles, they are bought and sold on the basis of a Construction Contract/Agreement. This is a contract between the developer/builder and the owner, but legally, these properties cannot be transacted. If an owner wants to further sell such a property, the Construction Contract is modified to reflect the new buyer’s name, effective retroactively (from the date of occupancy of the original owner). There are reports of developers exploiting the situation and selling the same unit to multiple buyers. Also, these houses cannot usually be leveraged as collateral for mortgage financing or other loans, so buyers must use other real estate – typically an older Soviet house – as collateral for bank financing.

New buildings are also suffering from inadequate building management. Most illegal MFBs are typically set up to resemble housing cooperatives (co-ops) but without the legal framework of a co-op. Basic building maintenance is undertaken by a ‘manager’ appointed by the developer who collects monthly payments from residents and is responsible for supervising building maintenance and services. However, the appointed manager’s salary is unreported and it is common for many residents to not make monthly payments on the basis that the manager does not represent their interests. There are also reports that officials appointed to head new cooperatives sometimes sell surrounding land (designated as common area for the community’s use) for their own profit. According to the current legislation, all co-ops must convert into condominiums and establish HOAs within six months of being occupied. However, a title is a prerequisite for the establishment of a HOA. This has become a vicious cycle whereby one form of illegality leads to the next, resulting in a massive stock of housing that is technical “illegal,” and therefore, “informal.” Issues with the maintenance and management of new and old MFBs are further discussed in Chapter 6.

Old Housing: Multi-family Buildings (MFB)

The older housing stock has been undergoing a steady process of de-capitalization and is highly deteriorated as a result. Old units built during the Soviet era are often cramped, and many require massive

capital improvements. Some may also be structurally unsound, especially in cases where large apartment building extensions have been constructed.

Despite their relatively poor condition, old MFBs are considered better value for money than new housing.

This is attributed to several factors: (i) the older units have clean titles and can be used as collateral for bank financing; (ii) they have the necessary utility connections, including gas, which new “illegally” buildings do not; (iii) they are generally perceived to be more structurally sound than the “unregulated” newly-built structures; (iv) they are more affordable in terms of the basic price per square meter; and (v) they offer better value-for-money in terms of their location and the available social amenities compared to newer units at similar prices in the suburbs.

Figure 26: Old Multi-family Buildings



However, the price of old housing has also been gradually increasing over the past few years. For instance, a two-room apartment in Baku has risen from AZN 50K–60K in 2011 to AZN 80K today. Interviews with various stakeholders suggest that this might be a result of the excess demand in the market resulting from massive resettlement caused by the Sovietsky project in Baku. Despite this, older housing is still much cheaper than the new housing, and easier to finance with bank loans because the property is titled and can readily be used as collateral.

Figure 27: Demolished homes and housing-for-sale advertisements in Baku's Sovietsky neighborhood



Left: The Sovietsky neighborhood in Baku has been largely demolished to make space for the extension of a park. The majority of people have left, but some households decided to not accept the government's offer for compensation and have stayed on.

Right: Many housing-for-sale advertisements can be found on the walls of the Sovietsky neighborhood, most for old housing in Baku's 3rd zone and new housing on the urban periphery. The large number of households evicted from the Sovietsky neighborhood looking for new housing has driven up the price of old housing units in Baku.

Public funds are being used for façade beautification (see Government Programs in Legislative Annex 2), not to solve the critical housing quality problems of old MFB. Massive public investments are being made on improving the facades of buildings in the city center and other prominent areas, including for a large number of older Soviet blocks. The work involves major improvements, including putting massive stone tiles on existing facades, adding balconies, embellishing openings with cornices and sculptures, painting external walls, extensive external lighting, etc. However, it is not uncommon to find these improvements on the front façade of the building, while the side or rear wall is typically left in disrepair. These investments have realized cosmetic results, while interior areas including common areas and more critical elements of the buildings such as the elevators, roofs, and external walls – the core elements of the buildings, and in many ways much more critical than the exterior face – continue to deteriorate.

Figure 28: Beautification program in Baku



A neighborhood in Baku that benefited from the government's beautification program. The left photo is the front façade, and the right photo is the same building viewed from the back.

Rental Housing

Azerbaijani's culture of homeownership limits housing options. While renting might be more affordable and allow for increased labor mobility, especially for young professionals and starter households, an entrenched culture of homeownership compels many households to buy. The deep-rooted culture and preference to own a house rather than rent is evident from the following statements made by local residents:

"There is a young person I know, who has been engaged to be married for five years, but can't get married because he has not been able to buy a house till now."

"In Azerbaijan, to marry means to obtain a house."

"People change their jobs for a desired residential location, not the other way around. There is much more interest to buy, compared to renting." (MoED)

The rental market in Baku is mostly informal. This may at least in part be attributed to a rental income tax of 14 percent. Informal renters are often students sharing housing or in-migrants from the regions. Such rental arrangements provide no legal protection to landlords or tenants. There is also a small formal rental market, with legal contracts, but it is estimated that only about a third of the actual renters have such arrangements, and these generally involve expatriate tenants. The realtor fee for long terms rentals (>1 year) is one month's rent and for short-term rentals (<1 year) is half of one month's rent to be paid by the landlord. Rental housing is discussed in more detail in Chapter 4.

Furthermore, unlike major cities in developed economies, there is no practice of rental buildings in Baku, and more generally, in Azerbaijan. Most rental units are single-rentals, situated in MFBs, and rented out by private owners. There do not seem to be any buildings or developments dedicated to private rental, most likely due to the high degree of informality in the rental market and the deeply engrained culture of homeownership in Azerbaijan that makes such developments seem undesirable. Indeed, 80 percent of renters in Greater Baku live in apartments versus 9.25 percent living in single-family homes. Of the remaining, 9 percent are households living in collective centers (they consider themselves as renters), and less than 2 percent rent individual rooms in a larger house or apartment.⁴⁷

3.2. Housing Finance

Azerbaijan Mortgage Fund

While the AMF has and continues to play a considerable role in boosting the mortgage market, it could realize greater impact by addressing the following shortcomings:

- i. **Traditional underwriting excludes non-salaried, self-employed households.** Proof of salary is required for all AMF loans, and can be verified through the "ASAN" online document processing service. Unreported income cannot be taken into account, which excludes large sectors of the Azerbaijani population working in the informal sector or who are self-employed from AMF mortgage loans.
- ii. **Targeting of subsidies without consideration of income or need.** Neither the social loan nor the standard loan, both of which are subsidized in terms of interest rates, have any eligibility criteria related to income. Moreover, the social loan, which offers a loan at 4 percent – a third of the market rate – is targeted to categories of people who are almost certainly non-poor, and even possibly in the higher income brackets, for example, sportsmen who have ranked among the top three in national or international events or people with higher education (scientists, PhDs). It also does not take into account that people in the lower income groups – who should ideally be the target of this subsidy – are more likely to be informally employed. By qualifying only salaried people for such loans, it is in essence disqualifying the majority of lower income but creditworthy people who actually need this assistance. Also, although it is not officially specified, interviews with local residents reveal that

⁴⁷ World Bank, *Greater Baku Household Survey* (2014); see also Figure 44 in this report.

people earning below AZN 1,000 per month rarely qualify for these loans. For such households to receive a loan, according to several sources, “one either needs to show enough documented income, or have a personal contact/reference in the bank to get a loan application approved.” Further, the financial resources and formal employment needed to take out an AMF loan effectively limits such loans to Baku and the Absheron Peninsula, which excludes the population living outside of these areas.

- iii. **Unmet demand and long waitlists.** The AMF has, on average, benefitted some 2,500 households annually since its establishment. This is only about 5 percent of the estimated demand: some 80,000 new households register annually, of which at least half need new houses. Annual allocations to the agent banks are made by the AMF, depending on the funds available and the capacity of the banks. There are some 33 agent banks, so the pot of money going to each bank on average is quite small at USD 1.2 million. Many banks report that the average AMF loan size is the maximum AZN 50,000, meaning that on average an agent bank might make only 24 loans. Additional funds can be requested from the AMF mid-year, depending on the performance and disbursement of the agent banks (a second tranche of sorts). For example, Xalq Bank, one of the largest banks in Azerbaijan dealing with mortgages, received an allocation of AZN 5 million at the beginning of 2015, and is expected to receive another AZN 3 million in June 2015. To date, Xalq Bank has received AZN 40 million and issued 1,200 mortgages, compared to 1,400 of their own internally-funded mortgages. Still, the demand for these loans is extremely high and the ‘pie’ is too small: according to officials of the agent banks, the demand for such loans outpaces supply of AMF funds by 300 percent.
- iv. **High down payment charged by agent banks.** Although AMF’s requirement for down payment is a minimum of 15 percent of the loan value for social loans and 20 percent for standard loans, most banks require between 30 and 40 percent down payment. This is because the borrower’s risk lies completely with the banks. This down payment is sometimes a prohibitive upfront cost that most households – especially lower income and even many middle income households – cannot afford.
- v. **Loan amount (cap of AZN 50K) too small compared to house prices.** A loan this size with a 40 percent down payment – which is what most banks require – can fetch a house of about AZN 75K-80K. To put this in perspective, the average price of a newly-constructed 2-bedroom house in the 2nd zone is AZN 100K.⁴⁸ An old 1-2 bedroom Soviet apartment in the 2nd zone costs about AZN 80K. The small size of the loan effectively restricts housing choice: while the cap might be appropriate for the ‘social’ loan on the assumption that it should cater to lower-income households looking to purchase smaller and cheaper housing units, the same cap in the case of commercial loans implies that the buyer must cover a significant outstanding amount in the form of a down payment.
- vi. **More profitable for banks to give out AMF Standard Loans versus Social Loans.** There is a 4 percent interest markup in the Standard Loans as opposed to a 3 percent markup in the AMF Social Loans and 2-4 percent markup commonly used in commercial banks’ internal mortgage loans. There is no earmarking of funds for Social versus Standard Loans, and all loans are made on a first-come, first-serve basis. Given that the effective markup for agent banks for Standard Loans – at 4 percent – is even higher than the markup in their own internal loans (2-3 percent), there is much more incentive to approve more Standard Loans than Social Loans from the AMF funding pool.
- vii. **Distortionary effect of AMF ‘standard’ loans with agent banks’ ‘internal’ mortgage loans.** By offering subsidized commercial loans on one hand, and offering banks a 4 percent yield on AMF Standard Loans, the AMF might be causing a double distortion – first, by incentivizing banks to issue more commercial loans than social loans from AMF resources, as discussed above, and second, to some extent competing with agent banks on their market-based internal loans. As discussed earlier,

⁴⁸ Illustrative process per m² for new construction in Baku

there are currently limits on this distortion because of the limited pot of financing from the AMF. However, if this pot were to be increased with the same terms and the same products, this distortion would increase as well. This would also increase inequity in some sense because the few who receive the AMF Standard Loan essentially “win the lottery” compared to others in the same economic situation who pay 3-4 percent more interest on the banks’ internal loans. The argument here is not against increasing the AMF pot size, but rather to either target these Standard Loans more effectively so that the subsidy element is justified or to cancel this product altogether.

- viii. **Collateral requirement of titled property excludes most new properties on the market.** The collateral for both types of AMF loans must be the title of the property for which the loan is being taken. However, given that so many of the newly-constructed residential properties do not have such titles, they cannot be financed with AMF-funded mortgages. To this effect, a proposal has been made to the parliament to allow ‘Construction Contracts’ to be used as collateral in lieu of titles.

Mortgage Market

Some of the major challenges facing the mortgage market are outlined below.

- i. **Limited penetration of the commercial mortgage market.** Less than 5 percent of all housing sales are financed by mortgages. Banking sector stakeholders estimate that the ratio of AMF loans to regular commercial loans (funded by commercial banks’ internal funds) is approximately 90:10.
- ii. **Borrowing capacity constrained by limited documented income.** It is common knowledge that official or reported income can be anywhere between 20 and 80 percent of the actual household income. Because banks generally only consider official income to determine borrower eligibility, many borrowers do not qualify for a large enough loan. Certain professions, such as doctors and teachers, are particularly restricted: they earn very little officially – an average of AZN 250/month. This income level would render them ineligible to borrow an amount large enough to afford anything available in the market. However, their official income is actually supplemented with private work, and according to several people interviewed, *“they may earn as much as AZN 2,000 more. This is very common in Azerbaijan. The same goes for young people.”*⁴⁹ This is not to suggest that unreported income be factored in when qualifying a borrower for a mortgage loan, but rather that this looming issue of unreported income is a massive problem that, among many other problems, limits the ability of people to borrow to their full repayment capacity, and further constrains housing affordability.
- iii. **High down payment.** A 40 percent down payment is typical for mortgage loan products offered by commercial banks in Azerbaijan; this is based on the banks’ appraised value of the property, not the price of the house. There is a common perception among banking institutions that there is a price bubble and that most properties are over-priced. As there could be a discrepancy of anywhere between 10-40 percent between the banks’ appraised value of the property and the actual asking price of the property, this effectively pushes the down payment to as high as 60 percent. Some banks like Access Bank will not give the loan if the difference between the appraised value of the property in question and its asking price exceeds 10 percent. Other banks use a standard formula for valuing the properties; for example, TBC Credit’s independent loan appraisal discounts the market price by as much as 30 percent for an apartment and 40 percent on a house.
- iv. **“Effective” interest rate too high.** Most market-based commercial loans are offered at double-digit interest rates (12-14 percent), which is relatively high for long-term loans. There are a limited number of banks that offer AZN loans, but not only are these at a slightly higher interest rate but also, notably, they are pegged to the USD. The recent devaluation of the AZN by 34 percent in February 2015 impacted both lending institutions and borrowers: for outstanding AZN loans that were not pegged to the USD, banks took a major loss, and for outstanding USD loans, the borrowers saw their

⁴⁹ Interview with five commercial banks in May 2015.

payments increase by 34 percent overnight – raising the “effective” interest rate on commercial bank mortgages from 12-14 to 16-18 percent.

- v. **Shortage of cheap, long-term AZN funds for housing loans.** A 10-year loan period for mortgage loans is typical in Azerbaijan, which is rather short for mortgage loans and drives up monthly payment amounts. Bankers explain that the short loan period is to avoid the loan-deposit term mismatch, i.e., they cannot fund long-term loans with short-term deposits. Also, most major banks, such as TBC Credit, receive their funding from foreign investors, so their funds are in USD or EUR. Thus, they lend in USD – or in AZN but pegged to the USD (with a floating rate) – which is a challenge for the borrower earning in AZN. Also, since the devaluation, people are increasingly converting their AZN deposits into USD, which has further impacted the banks’ supply of AZN funds.⁵⁰
- vi. **Collateral issue for “illegal” properties.** In many cases, unregistered or “illegal” houses are being purchased with mortgages from commercial banks. Since these houses technically cannot be used as collateral for the loans, in a less-than-ideal situation many banks accept a second property as collateral. For example, a household may use an old Soviet-style apartment they own as collateral to buy a new house. For households that do not own a house, it is not uncommon to buy an old unit with title as their first house, and then use that as collateral to purchase the next, more desirable, house.
- vii. **Difficulty in enforcing property foreclosure.** The legal framework surrounding foreclosure and enforcement of collateral is reported by banking institutions to be inefficient, i.e., enforcement of collateral is reported as a major problem. For example, eviction of defaulters in cases of non-payment may be delayed by more than a year.⁵¹ Although the recorded default rate is low (less than 5 percent for most banks), especially in the case of first time home-buyers, this may be one of the factors increasing the risk perception – and risk aversion – on part of the lenders, which has translated into the high down payment and loan-to-value (LTV) ratios described earlier.
- viii. **Mortgage financing focused on Baku.** Apart from some housing microfinance in the regions, there is no channel for accessing finance effectively to households in areas outside of Baku and the Absheron peninsula. Part of the reason cited by banks is that the demand is relatively lower in the regions, as is their presence, and it is even more difficult to enforce collateral rights there.

Housing Microfinance

Some of the major challenges facing the market for home improvement and HMiF loans are outlined below.

- i. **Currency risk: source of funds for MFIs largely in USD.** As in the case of most commercial banks, loans offered by MFIs are in both AZN and USD, but AZN loans are pegged to USD to hedge the currency risk for MFIs. For example, Azer Credit’s ratio of USD to AZN loans is 50:50, while the investors are putting in money at a USD to AZN ratio of 80:20. Borrowers took a major hit following the devaluation of the Manat in February 2015; defaults increased, and many non-payment cases went to court. Various options for loan modification are now being considered, including basing future repayments on the exchange rate prior to devaluation, or making some adjustments in the interest rate to compensate for borrowers’ losses. Notwithstanding, both MFIs and borrowers are in a “wait-and-watch” mode until the country’s economic situation stabilizes.

⁵⁰ According to Access Bank, the shock caused by the devaluation has caused credit activity to contract by 80 percent. Loans now on offer are only in USD, and much smaller with shorter terms than was the case before the devaluation. Standard Bank reported that their cost of funds has increased, and the 12.5 percent internal mortgage loan product that they offered before has now been discontinued because it is no longer considered profitable; going forward, they will only offer the AMF mortgage loans.

⁵¹ Interviews with five anonymous commercial banks in May 2015.

- ii. **Limited funding sources for housing loans.** There are limits on the share of the lending portfolio that MFIs can dedicate to housing, and this is explained by two main factors. First, investors sometimes impose conditions on the use of their funds (the purpose of the loans offered to borrowers). Second, borrowers often take consumer loans and use part of the money for housing, and this does not always get recorded as a “housing” loan. In other words, microfinance funds dedicated specifically to housing purposes are limited (1 million to Finance for Development, 4 million to AzerCredit from HfH, at 8-11 percent interest). Also, the size and term of the HMF loans is directly related to the terms of the funds they receive to ensure adequate liquidity. According to FinDev, they could easily absorb AZN 5 million over the next two years if funding were made available.
- iii. **Legal framework for collateral enforcement is perceived as weak.** All MFIs interviewed reported that court cases to enforce collateral are lengthy, bureaucratic, and costly. It is very difficult to sell a seized asset through the court system, and the defaulters can appeal to the higher court. Smaller MFIs such as FinDev thus prefer to use “soft” collaterals and guarantees – which are relatively more straightforward to enforce – rather than hard collaterals (e.g., fixed assets) to overcome this legal bottleneck.

Construction Finance

Construction finance in Azerbaijan is expensive and unreliable. Developers report that construction finance is very expensive, so they have to rely on pre-sales and installment payments from buyers. As reported by various stakeholders, construction finance is only accessible for large and experienced companies. Standard construction financing is available at 18 percent interest for a 1-4 year period. For example, Xalq Bank offers construction loans to developers at 14-18 percent interest for 4 years, with a loan cap of AZN 20 million. Big projects are more dependent on such financing; most small projects, which includes the bulk of housing projects, are self-financed by the developer (with installment payments). Apart from being perceived as very expensive, smaller developers report that there are often problems with banks disbursing funds per the terms of the loan, and that dealing with banks is “problematic.”

Apart from the issue of lack of financial access to build projects at scale, this lack of construction finance indirectly impacts market discipline and transparency, and thus contributes to – and exacerbates – the “illegality” prevalent in the housing market. The fact that most developers do not deal with banks, and do not have to present (or “defend”) their projects with banks or other financiers, may also explain the lack of market data/ studies to inform developer projects and the market more generally.

CHAPTER 3: House Prices and Affordability⁵²

This chapter presents an overview of (i) existing housing prices in the Greater Baku Region; (ii) housing policies and government programs; and (iii) affordability levels based on an analysis of household income and available housing choices and financing instruments.

1. Housing Prices

The Union of Real Estate Market Participants divides Baku into three zones for analysis: Core urban (1st zone), Suburban (2nd zone), and Peri-urban (3rd zone). The price per m² for new construction in these zones is presented in the table below.

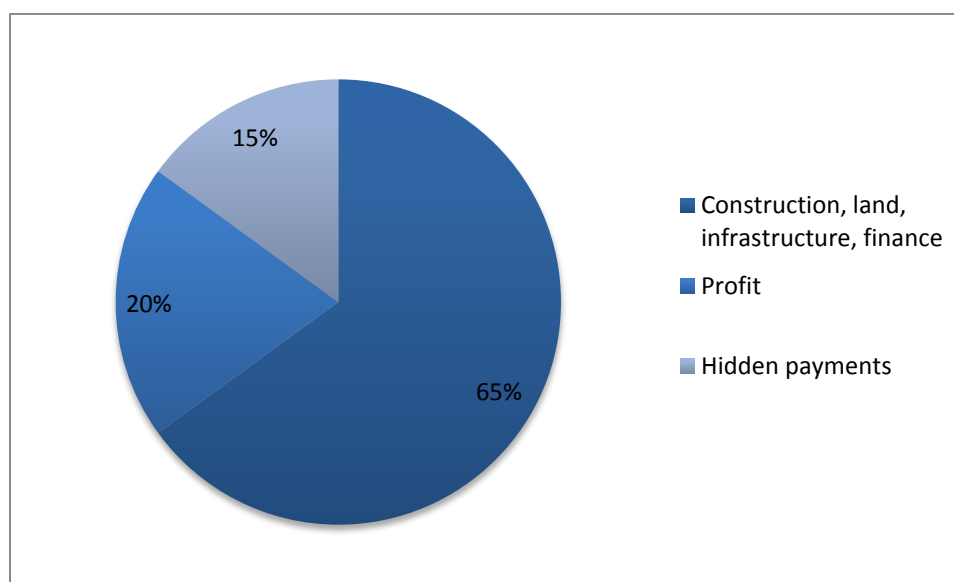
Table 7: Price zones in Baku

Zone	Distance	New construction prices (AZN/m ³)
1 st zone	3 km radius from city center	2,500-3,000
2 nd zone	3-8 km from city center	1,100-1,800
3 rd zone	8-12 km from city center	700-1,000

Note: Estimates provided by the Union of Real Estate Market Participants

The house price can be broken down into component costs and profit. While no official data is available, housing market stakeholders, particularly developers and real estate agents, provided the estimated figures illustrated in Figure 29. While construction, land, infrastructure, and finance accounts for the bulk of housing price, “hidden payments” are also believed to be a significant component. Housing sector stakeholders indicate that hidden payments can vary in nature, but are generally informal payments required of developers by public officials or bodies in order to provide service connections, property registration, construction permits, etc.

Figure 29: Estimated breakdown of final housing price in new MFBs



Note: Data are rough estimates provided by the Union of Real Estate Market Participants.

⁵² The numbers in this section are based on a database of real estate listings shared by MBA, a real estate market research company in Azerbaijan. These are not actual transactions, and the actual transaction price may vary by (-) 10% to (+) 5% of the listing price. But reportedly, transaction prices are not always recorded accurately, so it is better to use the list price. The numbers cater to a 10% “cheating factor,” which is about the difference across the various databases owned by different companies.

The price of new housing in Azerbaijan, particularly in Baku, is very high. An example is the 7 Hills development that is selling new units for AZN 1,099-1,200/m² in Baku's 2nd zone. The Xirdalan Village AAAF development on Baku's urban periphery – more than an hour's drive from the city center (the far edge of the 3rd zone) – offers a number of housing unit configurations and a desirable mortgage package from Beinelxalq Bank (10 percent down payment, 10 percent interest, 15 year mortgage period). Officials at the Xirdalan Village say that their housing products are designed for “affordability and versatility” and are targeted towards athletes. The approximate price for a “white frame” unit is AZN 650/m²; finishing such a unit would require approximately AZN 200/m². Furthermore, the price of sale or purchase transactions using a real estate agency in Baku is 2-3 percent of the housing unit price. This encompasses 1 percent from the buyer and 1-2 percent from the seller, which is negotiable. The table below lists the size and approximate prices of units in 7 hills development and Xirdalan Village, as well as the mean values of estimated selling prices for new buildings from the household survey.

Table 8: Unit area and price for different projects and new buildings

	Unit type	Area (m ²)	House price (AZN)
7 Hills development	Studio	50	57,475
	2 rooms (1 bedroom)	86	98,857
	3 rooms (2 bedroom)	132.5	152,308
	4 rooms (3 bedroom)	180.5	207,484
Xirdalan Village AAAF	Studio	28	18,200
	1 bedroom	32	20,800
	1 bedroom	36	23,400
	2 bedroom	64	41,600
	3 bedroom	140	91,000
Mean for new buildings (built after 2000)	Studio	40	66,736
	1 bedroom	52	75,479
	2 bedroom	70	80,658
	3 bedroom	107	76,908

Sources: Interview with 7 Hills representative (unit area and price per m2 are averaged from range of sizes and prices); data obtained in interview with officials from Xirdalan Village AAAF; household survey data

Older Soviet-period housing units are more affordable than newly-constructed housing. The price ratio for an old unit versus a comparably sized new unit is about 70:100. That said, the price of old units has increased marginally since 2011, partly as a result of public projects such as that in the Sovietsky neighborhood of Baku which caused many residents to vacate their houses in exchange for compensation from the government. The average price of a two-bedroom old unit in Baku was estimated to have been AZN 50K-60K in 2011 and is now AZN 80K. Table 9 outlines the area, price, and average occupancy of housing in old multifamily buildings.

Table 9: Unit area, price, and occupancy for an old flat in the 2nd zone

Type	Area (m ²)	Price (AZN)	Occupancy
1 bedroom	24	41K	2-3 inhabitants
2 bedroom	42	65K	3-4 inhabitants
3 bedroom	65	84K	4-5 inhabitants

Source: World Bank, *Greater Baku Household Survey* (2014)

Price for a 3-room (70-90 m2) old flat in Baku

Zone	Average Price (AZN)
1st zone	150K-350K
2nd zone	80K-130K

Rental housing prices and data are reviewed under the rental housing chapter (Chapter 4, Section 2.2.).

2. Existing Housing Policies and Government Programs

Currently there is no housing strategy or policy framework establishing overarching policy to guide programs or projects, or to provide a setting for formulation of local housing strategies at Raion and/or district levels. The Government has a draft State Program on Development of the Housing Sector for the Period of 2013-2017; but that was not shared with the World Bank team. However, the MOEI is said to be working on a “plan of action for development of the housing sector in Azerbaijan during 2015-17,” which is currently being developed with collaboration across different government agencies. The draft State Program was examined by an EU expert team in 2013, which indicated a number of desirable improvements in policy development including, inter alia: (i) ‘reforms support fund’ to ensure financial support for housing reforms; (ii) social benefits (housing allowances) for payment of maintenance and repair bills by low-income families; (iii) improved energy efficiency; (iv) State participation in cooperative housing society; and improvement of statistical accounting in the field of municipal housing economy.⁵³ For now, there is a lack of a long-term housing policy program with a clear allocation of funds in the multi-year budget, and policy decisions are often discretionary and not based on assessment of housing needs, and thus, there is a lack of monitoring of performance indicators.⁵⁴

The legal and institutional framework for public intervention into the housing sector remains fragmented. This is especially the case with the Housing Code (2009), which still lacks many pieces of secondary legislation despite Presidential Decree No. 153 (2009) pertaining to approval and enforcement of the Code.⁵⁵ These dispersed activities are to be coordinated by the Ministry of Economy and Industry as empowered to do so by Presidential Decree No. 379 (2011).⁵⁶ Implementation of housing policy programs is vested mostly with Executive Committees; municipalities surprisingly have little role.⁵⁷ The committees also continue to use ZhEKs for management of the multi-family buildings despite the stated intent of the Housing Code (2009).

The following are the main existing Government programs:

- **Mandated multi-family building maintenance tariffs.** Old post-Soviet multi-family buildings managed by ZhEKs carry very low maintenance tariffs mandated by the Government Decree No. 40 (2000) On the Approval of Tariffs According to the Housing and Communal Services and Fee for the Use of Residential Area (housing fee) in the Houses with State and Private Housing Fund (stock). The consequences of very low maintenance fees are discussed in Chapter 6.
- **Multi-family building’s façade beautification.** Substantial funds are being expended on improving facades of selected buildings – mainly in core-urban and other prominent areas. However, these cosmetic measures do not address the problems of deteriorating internal common space and more critical building elements such as elevators, external walls, and roofs.⁵⁸ More about this can be found in Chapter 3.

⁵³ For a full list of proposals see Section 25 in the European Union report by J. Fiszer, A. Chalabova: “Support to Azerbaijan in Reforming the Housing Sector – Gap Analysis Report,” November 2013.

⁵⁴ Conclusion from the European Union report by J. Fiszer, A. Chalabova: “Support to Azerbaijan in Reforming the Housing Sector – Gap Analysis Report,” November 2013.

⁵⁵ This was to ensure approximation of pertinent normative legal acts of the relevant executive authorities so that the Housing Code implementation would be effective.

⁵⁶ Charging the Ministry with “conduction of unified State policy in the areas of housing and communal services, provision of development concepts, state programs, and statutory-regulatory elaboration.”

⁵⁷ This stems from Presidential Decree on Local Executive Powers (2012), charging them with implementation of state policy in the area of the housing economy in relevant areas, including organizing management of communal economy and housing operational areas and maintenance of residential and non-residential areas of state housing fund.

⁵⁸ There are references to selected roof-improvement spending as well.

- **Provision of social housing.** Social housing remaining after the mass micro-privatizations in the 1990s is allocated to tenants on merit-based and not means-tested criteria. These ‘preferential’ categories now include: (i) invalids and families of martyrs of the Karabakh War;⁵⁹ (ii) public servants and politicians; (iii) orphans leaving orphanages; (iv) journalists; (v) sportsmen; (vi) popular singers; (vii) writers; and (viii) students. Efforts are being undertaken to produce new social housing as, for example, student dormitories at Baku State University, or a new building dedicated to homes for 150 journalists. The Government realizes there is a shortage of such dwellings, but no specific data has been produced on the size of this shortage.
- **Provision of public housing.** Public housing is provided to vulnerable groups, such as the blind and disabled, which require direct shelter intervention. The main focus in this area falls on refugees and IDPs. The State Committee for Refugees and IDPs runs a program of resettlements into newly-constructed, State-funded public housing, and also provide them with social protection measures such as employment, education and health protection. Under the housing resettlement program for IDPs, the units are allocated to households based on a lottery basis, and the beneficiary household can live there rent-free indefinitely. Of the 700,000 IDPs in the country, some 230,000 (46,000 households) have moved into newly-built housing that is intended to be ‘temporary housing’ and thus of rental type. At about 94,000 households, that is dwellings, the rest forms a potential demand for public housing including rental tenure.⁶⁰ More about this can be found in Chapter 3. There is also a group of invalids of the Karabakh War and families of martyrs of this War; by Presidential Decree, there is a program to provide these families with housing during the period 2014-18. In addition to new construction of dedicated buildings, the Government is also interested in purchasing newly-constructed dwellings from developers for the purpose of enhanced integration of the disabled in the society.
- **Reported apartment ‘give-away’ by developers.** Housing sector stakeholders have reported that Executive Committees and Municipalities sometimes persuade developers to ‘donate’ some 5-10 percent of their newly-built dwellings in order to add to their public housing inventories, which can then be allocated to qualified households.⁶¹ This practice might influence the economic calculus of residential developers and could make buyers of new apartments pay higher prices to cross-subsidize the pool of social dwellings. However, such a cost burden may be mitigated in cases where developers obtain government land at a commensurately lower price to compensate them for apartment give-away.

Home improvement loans and housing microfinance. Banks and microfinance institutions offer several types of home improvement and housing microfinance loans. One such ‘product’ is a home improvement loan with fixed asset collateral, which is offered for construction and repair work. Another product is microcredit and housing microfinance with soft collateral.

⁵⁹ The Ministry of Labor and Social Protection maintains a waiting list for eligible beneficiaries.

⁶⁰ There are separate housing management organizations dedicated to the task (ZhEKs).

⁶¹ This type of ‘exaction’ is practiced in some other post-Soviet countries. For example, in Ukraine developer contributions are at 15-20% of new construction, according to BEST (2011).

Box 3: IDP Housing Program

According to the State Committee for Refugees and IDPs, the state program has reportedly helped reduce the poverty rate of IDPs from 75% in 2003 to 12% in 2014. The program pays for resettlement of IDPs in newly constructed state-funded ‘social’ housing, and also provides social protection measures – including employment, education and health facilities – for the beneficiaries. Some AZN 5.4 billion has been spent since 1993 to date under this program, which amounts to an average of AZN 1,200 per IDP per year.

Under the housing resettlement program for IDPs, the units are allocated to households based on a lottery basis, and the beneficiary household can live there rent-free indefinitely. All utilities are paid for by the state. Beneficiaries do not own the units, and therefore, cannot sell the units or pledge them towards a bank loan. The Housing Department under the State Committee for Refugees allocates a maintenance budget for these public housing units every year. The World Bank provided support for the IDPs through the IDP Living Standards and Livelihood Project, which also had a housing component involving upgrading some of the existing IDP housing structures. This component has, however, faced many challenges, and is not likely to be extended after the project closes in March 2016. Given that the state program involves construction of new housing to resettle IDPs, it is very expensive and time-intensive; however, there is no other state program to house refugees or IDPs. For example, a rental voucher system is not under consideration by the state because, according to the State Committee for Refugees, they “*want to invest in houses for their people until they return to their homelands*” and not “shortchange” them with rental options.



Left: Very poor quality old collective housing used by IDPs; Right: New IDP housing built by government

3. Housing Affordability

Housing affordability is defined as a relative standard that compares the cost of housing in relation to income or other economic benchmarks. The standard for affordable housing in any given context is then examined at different strata of the population and compared to a minimum adequate housing standard to paint a full picture of affordability. This analysis employs the most widely-accepted measure of housing affordability as a threshold of the percentage of net income that a household spends on housing costs. Housing costs are defined in this report according to Eurostat’s definition, which includes mortgage payments, housing loans, interest payments, rent payments, utility costs, maintenance costs, and structural insurance costs.⁶² Due to the unavailability of data for some of these component costs in Azerbaijan, this analysis focuses on mortgage payments, housing loan repayments, interest payments, rent payments, and utility costs. Unaffordable housing is defined by Eurostat as that which is beyond the cost overburden rate of *40 percent of net household income spent on housing costs*. As a 30 percent cost overburden rate is also commonly accepted, this threshold will be used as a more conservative baseline. In addition to the 30 percent threshold, it may

⁶² Alice Pittini, *Housing Affordability in the EU: Current Situation and Recent Trends*, CECODHAS, January 2012.

be assumed that households can spend an additional 10 percent on payment for utilities and housing maintenance.

This section examines housing affordability constraints for 5 different scenarios: (1) purchasing newly-constructed housing; (2) purchasing old, mainly Soviet-era housing using a mortgage loan; (3) purchasing land and building a house on the urban periphery with a housing microfinance (HMF) loan; (4) renting a house; and (5) the cost of maintaining current homeownership, i.e., already owning a house but paying utility and maintenance/management costs.⁶³

Household income

Understanding affordability begins with segmenting households by income brackets. It is common knowledge among stakeholders in the housing sector and Azerbaijani society as a whole that informal, unreported income comprises a large proportion of total household income, sometimes as high as 80 percent. The formally reported monthly household income deciles from the State Statistics Committee are presented in the table below.

Table 10: Baku Household Survey monthly income deciles

Decile	Income (AZN)
1	627
2	629
3	681
4	709
5	735
6	735
7	776
8	840
9	955
10	1044

Source: Data from State Statistics Committee

However, these data are gathered formally by the State Statistics Committee and therefore might not capture the full extent of informal, unreported salaries. Estimates of household monthly income from housing sector stakeholders, particularly those dealing with mortgage finance and microfinance, far exceeded the data reported by the Statistics Committee illustrated in Table 10.

Table 11: Baku HH monthly income quintile estimates by stakeholders in the housing sector

Income bracket	Income (AZN)
Low	400
Middle-low	800
Middle	1500
Middle-high	2250
High	4000

Source: Data estimates obtained from representative of FINCA and confirmed by other housing market stakeholders including Xalq Bank⁶⁴

While the income data for the lowest four deciles from the Statistics Committee are similar to the lower income brackets in Table 11, the middle and higher income segments diverge – for instance, income reported in the statistical data for the 4th, 5th and 6th deciles is about half of the income estimated by stakeholders for the ‘middle’ income bracket. Interviews with homeowners and knowledge gathered on formal and informal salaries from qualitative interviews support the data presented in Table 11, particularly for the middle-

⁶³ The survey conducted by the World Bank as part of the Greater Baku Housing Diagnostic indicated a 92% homeownership rate in Baku.

⁶⁴ All income data used in this section is from this table unless noted otherwise.

income brackets. Due to the known prevalence and significance of informal income and the substantiation of estimated income data from qualitative field research, the estimated income in Table 11 will be used as the basis of this affordability analysis. The median officially-recorded household monthly income of AZN 807 will also be used throughout the analysis as a reference point for the officially-reported income data.

Housing choice

Housing choice is severely constrained not only for the lower income brackets, but also for medium and higher income households. Constraints are in the form of a lack of variety of location, quality, and tenure form; urban areas are dominated by small dwellings in multi-family buildings, while peri-urban areas contain mainly single-family homes with larger floor areas. The average housing size in Baku is 54 square meters compared to 68 and 65 square meters in Eastern and Absheron City respectively. In the same way, Baku housing stock is overrepresented by multi-family buildings (83 percent), while in the surrounding suburbs there is a much larger proportion of single-family houses. In addition, the old housing stock is highly-deteriorated, and new housing is not generally of high quality. Formal rental housing is basically unavailable, except for high-end dwellings offered to foreigners and expats.

The constraint in housing choice affects households differently depending on their age and their life-cycle phase. Older ‘asset rich’ households typically own debt-free dwellings. While these theoretically become under-occupied as children leave the family nest, the small size of these units can continue to suit the remaining inhabitants. That said, the youngest starter households entering the housing market find themselves overcrowded due to the lack of centrally-located, affordable units large enough for a growing family. Consequently, there exists a mismatch between dwelling size and household size in urban locations, which is especially difficult for larger (household size of 3 or more) households living in small multi-family units. The ‘income-poor’ households, that cannot afford urban locations, live in peri-urban areas occupying larger dwellings in single-family houses.

Table 12: Percentage of households by household size and by number of rooms in unit

Rooms in unit	1 -2 people	3-4 people	More than 5 people
1	30.26	15.07	6.36
2	48.51	37.17	22.72
3	17.4	38.41	45.33
4	2.32	7.11	18.51
5 or more	1.51	2.24	7.08
Total	100	100	100

Source: World Bank, *Greater Baku Household Survey* (2014)

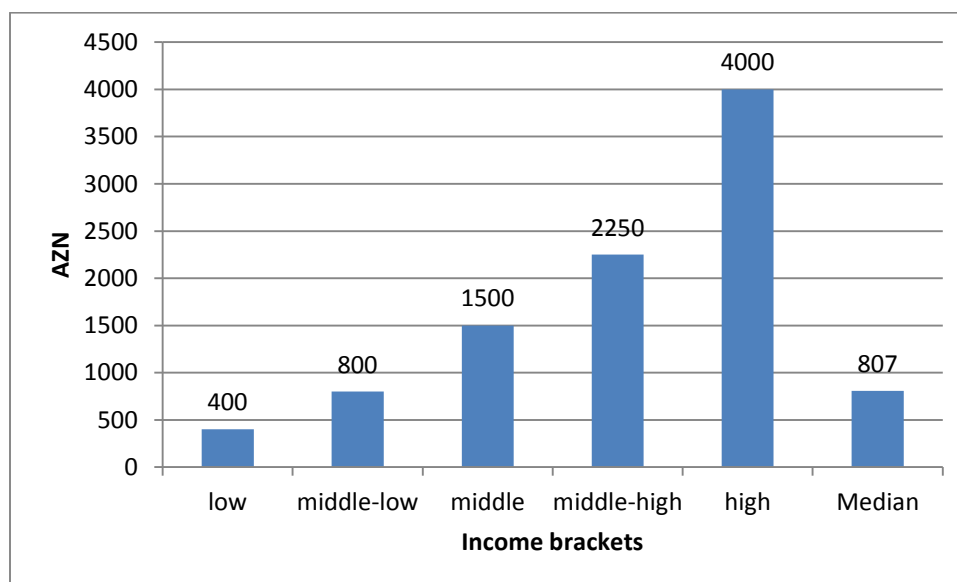
As can be seen in Table 12 above for the whole Greater Baku area, approximately 15 percent of the large households (3-4 people) are crowded into one-room dwellings. Additionally, almost 30 percent of the largest households (5+ people) are crowded into one-room or two-room dwellings. The lack of adequate housing choice is due to high ownership rates (lack of diversity of tenure) and constrained housing finance options. This locks older households into under-utilized privatized housing, while younger households generally cannot afford anything suitable in the market to buy or rent. This leaves the informal rental market and informal self-building on the urban periphery as two primary options. The restrained formal housing choice is a force behind the increasingly informal and/or illegal solutions prevalent in the housing market.

Figure 30 presents the income levels in the Greater Baku area by five income brackets. Households in the low income bracket have virtually no choice beyond their current housing or they have to arrange intra-family transfers through swaps, gift or inheritance. Households in the middle-low and middle income brackets can afford informal private rental, but cannot afford to buy an apartment or a home; a majority of these households remain “locked-in” to their current housing, since availability of rental tenure is severely restricted due to the prevailing informality.

The middle-high and high income brackets can consider home purchase, though are restricted by the lack of diversity and unavailability of various housing products. The middle-high income bracket can afford new construction in the peripheral 3rd zone and a small (24 m²) old unit, while the high income bracket quintile can afford a new housing unit in the 2nd zone or a 1, 2, or 3 bedroom old unit.

The vast majority of households, however, are homeowners due to the massive privatization of sitting tenants that took place in the 1990s. The privatization was implicitly aimed, *inter alia*, at increasing housing choice to a broader group of households, who presumably could optimize their 'housing consumption' through market mechanisms. Households of diverse income status thereby became owners of considerable debt-free home equity, thus creating numerous cases of 'income-poor' and 'asset-rich' homeowners. These are now typically older households, many of which have seen their home equity eroded substantially due to the under-maintenance of multi-family buildings (see Chapter 5). Such sitting homeowners generally have very low housing costs, affordable for almost all income quintiles, which is part and parcel of the systematic de-capitalization of the housing stock. Nevertheless, some of these older households living in high-value locations still have a possibility of "monetizing" their home equity by selling their dwellings and this way raising their financial affordability threshold. They can thus join the higher-income households in the unrestricted housing choice category, but likewise face the constraints of limited availability of housing products.

Figure 30: Monthly HH Income Brackets in Greater Baku Area (Manat)



Source: Data estimates obtained from representative of FINCA and confirmed by other housing market stakeholders including Xalq Bank;⁶⁵ Official Median for Baku obtained from the State Statistics Committee

Table 13 below illustrates existing housing options for each household monthly income bracket for varying types of housing tenure, typologies, and financial products. Households in the low income bracket cannot afford any market housing options, and are not currently the target of any significant public assistance program. As such, they are not served in the housing sector. Social loans from the AMF are affordable – in terms of monthly repayment of loan – for the middle-low income bracket, although these loans are often miss-targeted to non-poor households and can entail unaffordable down payments. Rental housing can be obtained from the middle-low income bracket upward, but often in locations at great distances from the CBD, limiting household members' mobility. New housing for purchase with a market mortgage loan is affordable only for the middle-high income bracket and higher, and only for small units located in the 3rd zone. Likewise old housing units for purchase with a market mortgage loan are affordable for the middle-

⁶⁵ All income data used in this section is from this table unless noted otherwise.

income bracket and higher, though only small 1-bedroom units (24 m²). All options are unaffordable to the median income except for renting a housing unit located more than 90 minutes from the CBD.

Table 13: Access to different types of housing by income category

Income Bracket	New housing purchase, market mortgage loan	New housing purchase, AMF Social Loan	Housing Micro Finance HMF	Old housing purchase, market mortgage loan	Rental
Low	Unaffordable	Unaffordable	Unaffordable	Unaffordable	Unaffordable
Middle-low	Unaffordable	Affordable (3 rd Zone)	Unaffordable	Unaffordable	Affordable (3 rd Zone)
Middle	Unaffordable	Affordable (3 rd Zone)	Unaffordable	Affordable (1 Bedroom - 24 m ²)	Affordable (2 nd Zone)
Middle-high	Affordable (3 rd Zone)	Affordable (3 rd Zone)	Affordable (10k loan)	Affordable (1 Bedroom - 24 m ²)	Affordable (2 nd Zone)
High	Affordable (2 nd Zone)	Affordable (3 rd Zone)	Affordable (10-20k loan)	Affordable (3 Bedroom - 65 m ²)	Affordable (1 st urban)
Median**	Unaffordable	Unaffordable	Unaffordable	Unaffordable	Affordable (3 rd Zone)
Income Affordability threshold (AZN)	3 rd zone: 1848 1 st zone: 5434	3 rd zone: 649*	From 1557 to 2410	Small: 1485 Medium: 2355 Large: 3043	618 (Unit more than 90 minutes from CBD)

* As the AMF has a 50K cap on loans, buying units in the 1st and 2nd zone with this instrument would require making large down payments of 40 to 60+ percent depending on the zone, which are expected to be unaffordable for most.

** This corresponds to the official median income in Greater Baku in 2013 (800 AZN) according to the State Statistics Committee

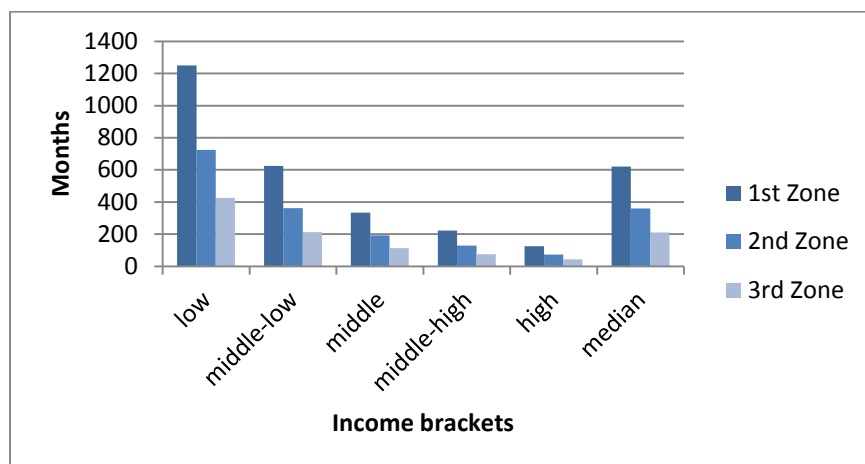
Affordability constraints

1. New Housing: Multi-family Buildings

Based on prices discussed in the earlier section, a standard 60 m², newly-constructed, “white frame” apartment would cost AZN 150K in the 1st zone, AZN 87K in a 2nd zone neighborhood, and AZN 51K in the 3rd zone. While speculation is rampant and many buyers use cash to purchase multiple units as an investment, Azerbaijanis purchasing such units as a primary residence can either do so using cash (savings) or a mortgage loan. Because new construction is often without title and therefore ineligible for mortgage loans, the affordability/ability to purchase a house using savings is illustrated based on the number of months’ salary needed to match the price of such units.

As expected buying with cash (savings) is not possible for most households. Figure 31 shows how many months it would take for a household to save enough income to buy a newly-constructed unit, assuming that a household can save 30 percent of its earnings towards housing purchase. For example, it would take a household in the middle income bracket 333 months or almost 28 years to save and pay in cash for a 60 m² house in the center city, 193 months for a house in the 2nd zone, and 113 months for a house in the suburbs. This is clearly not a viable option.

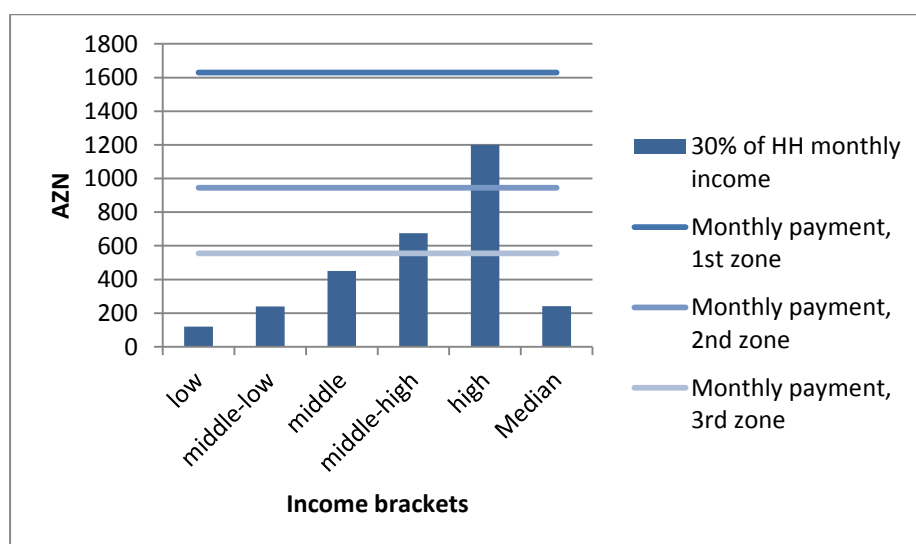
Figure 31: Months' savings required to purchase a new 60 m2 housing unit



Note: Housing prices obtained from Table 5

Buying new housing with a mortgage loan – using another unit as collateral – is unaffordable for poor, middle-low, and middle income households. Purchasing a newly-constructed unit with a mortgage loan entails collateralizing another property (typically an old Soviet housing unit) when the new unit lacks formal title. It can be assumed that those able to maintain ownership of a second property and also take out a significant mortgage loan to purchase a new housing unit would be in the middle-high and high income brackets. Figure 32 illustrates this case with a TBC Credit loan of 10 years at 14 percent interest with a down payment of 30 percent.

Figure 32: Monthly mortgage payments compared to 30 percent of HH monthly income⁶⁶

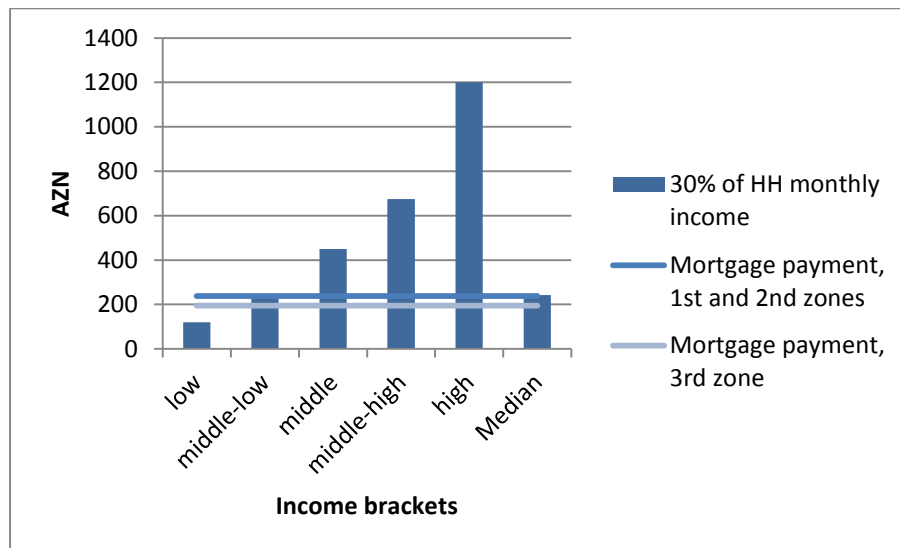


Overall, social loans from the AMF are the most affordable mortgage option on the housing market for buying new housing. Figure 33 shows that the monthly mortgage payments for AMF social loans are “in theory” affordable to almost all income segments (60 m² house in the 1st, 2nd, and 3rd zones of Baku). However, due to the AZN 50K cap on the loan amount the down payments are very high, especially for houses in 1st and 2nd zones, at AZN 37K and AZN 100K respectively. Figure 34 shows that a household in the middle income bracket

⁶⁶ Note: The monthly mortgage payment values are determined for a mortgage loan from TBC Credit (10 year period at 14% interest with a down payment of 30%).

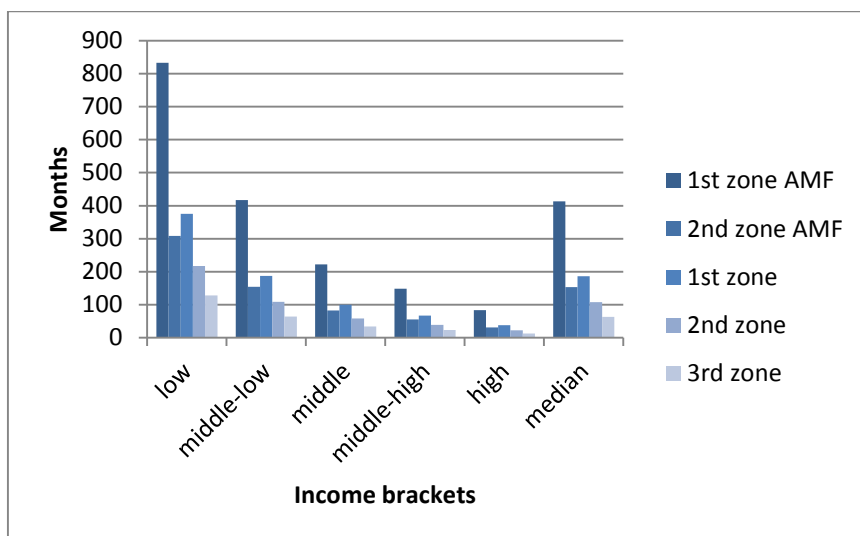
would need to save for 18.5 years to cover the down payment for an AMF social loan for new construction in the 1st zone.

Figure 33: Monthly mortgage payments on an AMF Social Loan at 30% of HH monthly income



Note: The monthly mortgage payments were calculated based on an AMF Social Loan (maximum loan amount of AZN 50,000, interest of 4%, period of 30 years). Because the high price of units in the 1st and 2nd zone would in theory require the maximum loan amount of 50,000, the monthly mortgage payments are the same for units in these areas.

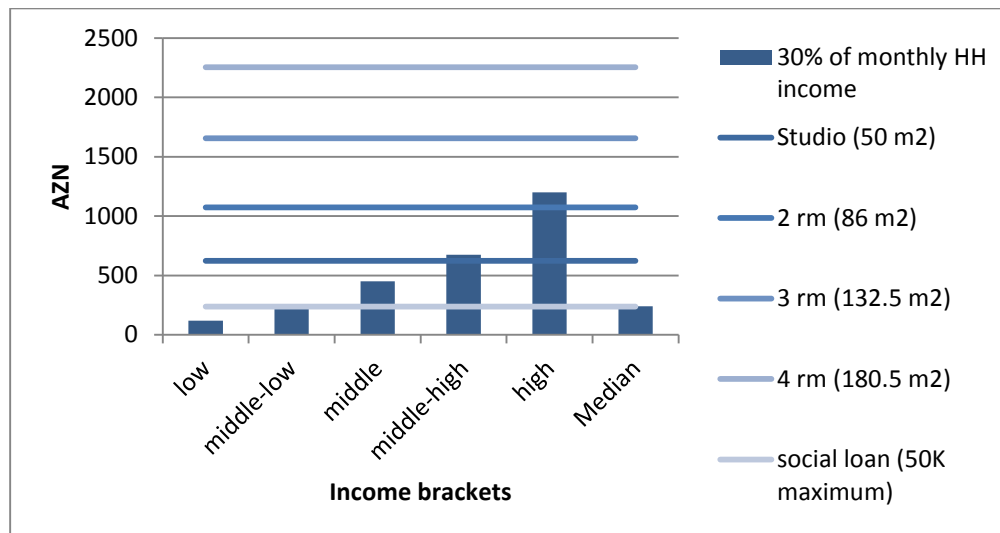
Figure 34: Months' savings required to cover a 30% down payment on a market loan (or down payment for AMF Social Loan) for new housing



As mentioned in the earlier sections, white frame units in MFBs in Baku require internal finishes, which can cost AZN 200-500 per m² depending on the desired quality. This could mean an additional cost of up to 30 percent of the unit price in the urban periphery. The high-end 7 Hills development in the 2nd zone features white frame units ranging from 50 m² studios priced at AZN 57,475 to 180.5 m² 4 BRs priced at AZN 207,484. The smallest studio apartment would only be affordable to the middle-high income bracket, while even a two-room unit of 86 m² would only be affordable to the high income bracket. A Social Loan from the AMF at the maximum of AZN 50K would make a studio affordable for the middle-income bracket, although the down payment for an AMF Social Loan for a 2BR unit would require a household in the middle-income bracket to save for nine years. The AAAF Xirdalan Village features more affordable new construction, though it is far from central Baku in the 3rd zone. While mortgage payments would be more reasonable, such new

developments are rare and the financial market is not supplying products suitable for lower income households.

Figure 35: Monthly mortgage payments for units in 7 Hills at 30 percent of HH monthly income

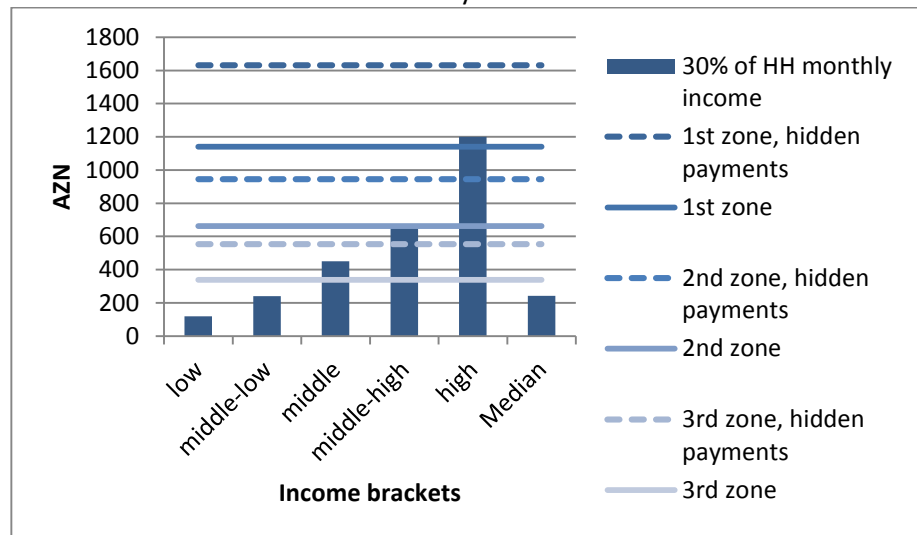


Note: Housing prices obtained from Table 9

To summarize, households in the high-middle and high income brackets can generally afford new, modest studio or two room units with commercial bank mortgage loans, but larger new units or new units in Baku center remain out of reach. Households in lower income brackets can only afford very modest units with an AMF Social Loan, and would likely face unaffordable down payments given the AZN 50K limit on the loan amount. Moreover, the small number of new units eligible for mortgage financing (given that the bulk of new construction is 'illegal') poses a further constraint on households that do not have an alternative asset to use as collateral, the savings to make heavy down payments, or buy the unit cash-down.

The affordability of new construction would be improved if existing hidden housing payments were eliminated. As discussed earlier, hidden payments might make up an estimated 30 percent of the final selling price of new construction in Baku (See Figure 29). Figure 36 illustrates how affordability increases with the elimination of hidden payments through administrative reform. For example, a new 60 m² house in the 1st zone will become affordable to high income bracket households, a similar unit in the 2nd zone to households in the middle-high income bracket, and a similar house in the 3rd zone becomes affordable for households in the middle income bracket.

Figure 36: Mortgage payments on new construction with or without hidden payments at 30% of HH monthly income

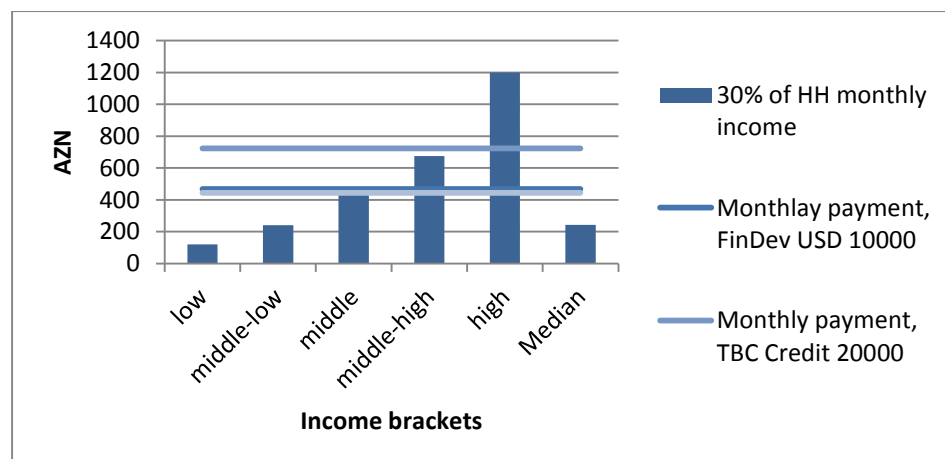


Note: The monthly mortgage payment values are determined for a mortgage loan from TBC Credit (10 year period at 14% interest with a down payment of 30%).

2. New housing: Incremental single-family housing

Purchasing land in the periphery of the city and getting a microloan for housing construction is affordable for the middle-income bracket and higher depending on the loan product. As mentioned earlier, land can be purchased and a home constructed in outlying areas surrounding Baku for amounts between AZN 10,000 and AZN 20,000.⁶⁷ This offers a comparable option in terms of affordability to the purchase of an old house or flat in Baku. While some households construct such houses with savings, MFIs have targeted such households with housing microfinance (HMF) products. A USD 20K microloan from TBC Credit and a USD 10K microloan from Finance for Development (FinDev) have been used to illustrate affordability benchmarks. Figure 37 shows that such loans are affordable to the middle, middle-high, and high-income brackets. In addition a standard home improvement loan (USD 20K, 14 percent interest, 7 year tenure) has been included, which is affordable for the middle income bracket and higher.

Figure 37: Monthly microloan payments at 30% of HH monthly income

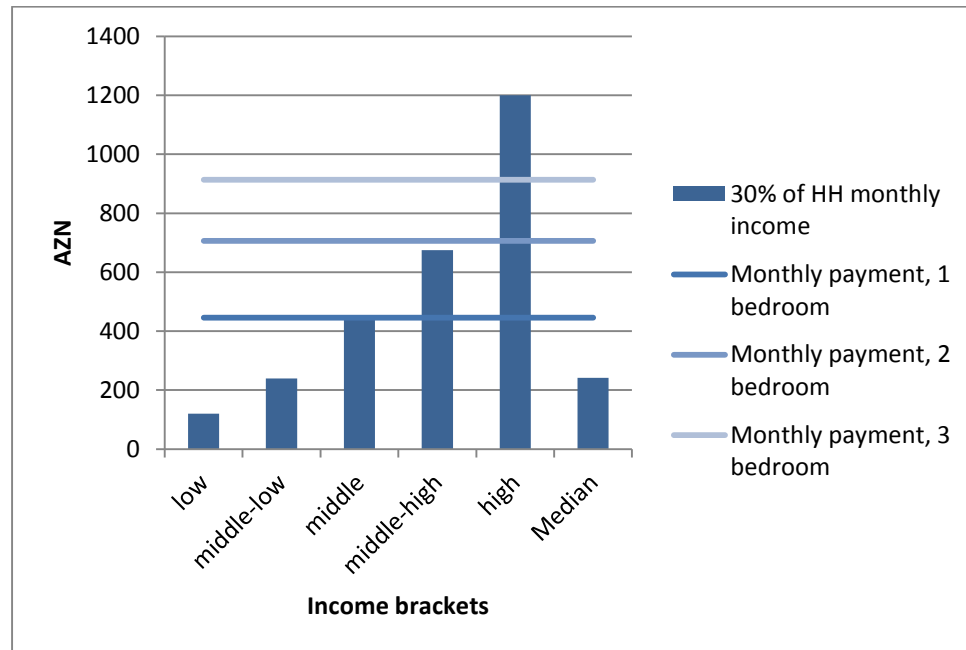


⁶⁷ Multiple HMFIs interviewed indicated that AZN 10,000-20,000 was sufficient to purchase land and self-build (albeit incrementally in some cases) on the urban periphery of Baku.

3. Old multi-family housing

While cheaper than new housing, old housing still remains largely unaffordable for low-income groups or only affordable in overcrowded conditions (buyers purchase less space than they need). Even though the older MFB housing units often lack sufficient space and their price has gone up marginally since the relocation of households due to large-scale public works (e.g., Sovietsky Park), they are still marginally more affordable than new housing and sometimes more desirable due to better utility connections and a formal title. Figure 38 shows monthly mortgage payments on standard TBC Credit loans for different sizes and prices of old units. For example, households in the middle-income bracket can afford a small 24 m² one-bedroom unit priced at AZN 41K for 2-3 inhabitants.⁶⁸

Figure 38: Monthly mortgage payments at 30% of monthly HH income for different housing products



Note: The monthly mortgage payment values are determined for a mortgage loan from TBC Credit (10 year period at 14% interest with a down payment of 30%); See footnote 70 for a list of housing sizes and prices.

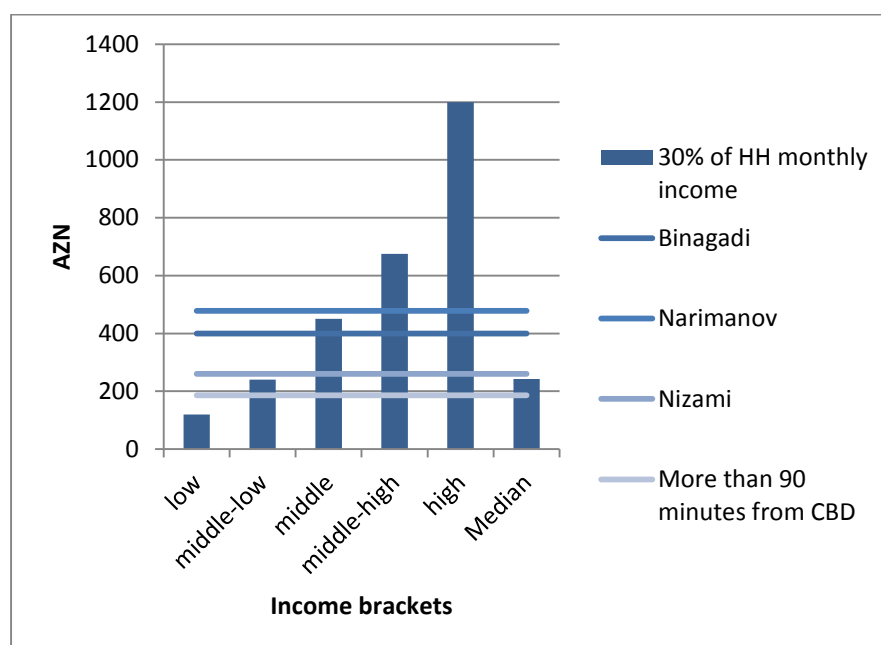
4. Rental housing

Mean rental prices in Baku are relatively affordable even for centrally-located units. Across the board rental prices are comparable or lower than monthly mortgage payments for housing units in the same districts of Baku, indicating the financial favorability of rental arrangements. That said, the culture of homeownership in Baku and the lack of rental housing on the market limits this option. One respondent's rental unit in an old Khrushchevka style building next to the 28 May Metro Station (1st zone) was AZN 400/month in addition to AZN 5 for gas and AZN 18 for electricity. This price aligns with the mean rental prices gathered as part of the World Bank's Household Survey for different districts of Baku presented in Figure 39 at 30 percent of HH monthly income. More centrally-located rental units are affordable for the middle income groups and up, a rental unit on the urban periphery more than 90 minutes from Baku's Central Business District is affordable even for the middle-low income bracket as well as median income households.

⁶⁸ The sizes, prices, and occupancies for old units used here are obtained from the World Bank's *Greater Baku Household Survey*:

Type	Area (m2)	Price (AZN)	Occupancy (individuals)
1 BR	24	41,000	2-3
2 BR	42	65,000	3-4
3 BR	65	84,000	4-5

Figure 39: Mean rental prices in different districts of Baku at 30% of HH monthly income



Note: Mean rental price data from World Bank, *Greater Baku Household Survey* (2014)

5. Homeowners of Privatized houses

For a large proportion of households that neither rent nor buy housing but simply own privatized, Soviet-era housing means that housing-related costs constitute only utility payments, maintenance, and housing management. Fees paid to ZhEKs average about AZN 3-5/month, which does not come close to the amount needed for the basic upkeep of these buildings.

The total expenditure on utilities and other housing maintenance costs is less than 10 percent of HH monthly income, even for households in the low-income bracket.⁶⁹ This suggests that there is significant margin for increased payments for building management once the transition from ZhEKs to HOAs or cooperatives is completed. This would enable proper maintenance and “re-capitalization” of old housing stock, although the initial improvements might require significant government support given the extensive capital resources needed to make basic improvements to long-neglected housing stock.

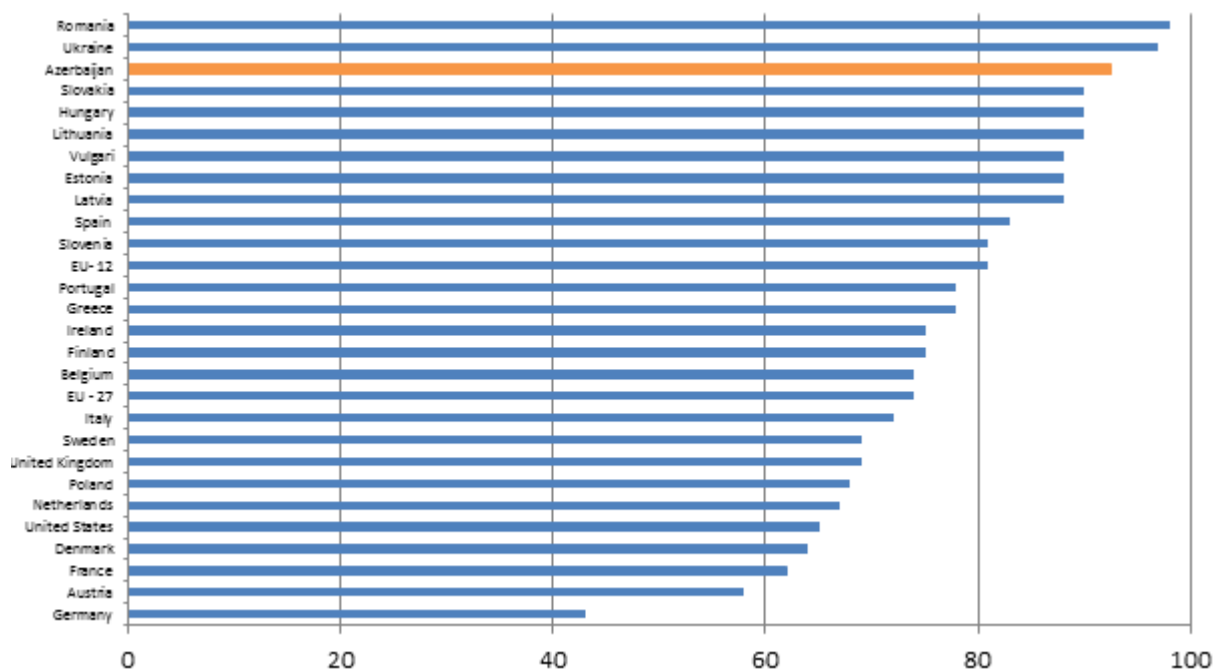
⁶⁹ The AZN 58.5 in monthly housing expenditure per household comes close to the per capita household expenditure of AZN 76 for housing, water, electricity, gas, and other fuels multiplied by the average household size. Even this higher estimate of household expenditures on housing comprises a small percentage of monthly household income for the lowest income quintile.

CHAPTER 4: Rental Housing

Tenure flexibility is important for the Azeri economy due to the interaction between labor-market mobility and availability of affordable and tenure-neutral housing choices (See Box 4 below). This relationship is pivotal to macro-economic performance since low labor mobility is generally considered to hamper economic efficiency and growth. Labor mobility in the ECA transition economies tends to be lower than in the Western European economies; this can be partly ascribed to the scarce availability of affordable housing in the former Soviet countries, and partly to the very low desire of their populations to relocate unless offered higher salaries and ‘free’ housing.⁷⁰

Conditions for ‘flexible homeownership’ have not been attained yet in Azerbaijan and the lack of alternative rental housing choice exacerbates the problem of low residential mobility and thus labor market flexibility. Higher homeownership requires commensurate market efficiency and affordability of financing through expedient mortgage underwriting, low down payment requirements, and favorable (affordable) mortgage interest rates. Homeownership markets need to be stable and predictable making it easy to sell and buy.⁷¹ Growing homeownership tends to increase unemployment because of (i) lower residential mobility – selling a home and finding a new one is expensive (transaction costs are high); (ii) lower labor mobility – workers may take jobs poorly matching their skills (labor productivity); (iii) home owners tend to commute longer distances – higher congestion and costs; (iv) housing markets dominated by home owners can impede settling of younger and productive newcomers; and (v) home owners are more reluctant to let business startups in residential areas through land development restrictions and local planning regulations. The wide variation of homeownership rates is illustrated in Figure 40 below. Azerbaijan’s homeownership rate of over 90 percent places it among the top countries such as Romania and Ukraine - well above the EU27 average of around 70 percent.

Figure 40: Ownership occupancy rates in selected countries



Source: Eurostat (SILC, 2009) and State Statistics Service of Ukraine (Household Survey 2010)

⁷⁰ Synovate (2010) found that more than 50% of respondents in Russia and Ukraine would move if offered free housing and much higher salaries.

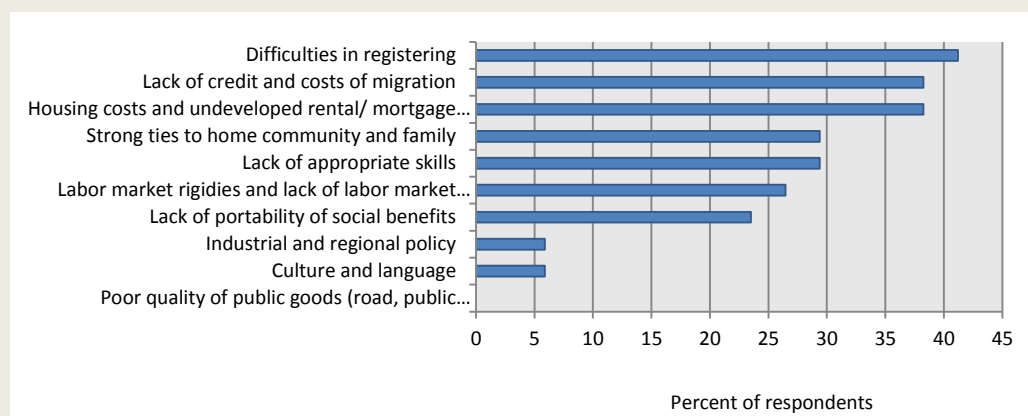
⁷¹ Housing market recessions can create negative equity making owners reluctant to sell and move for new jobs. They become ‘house locked’ as negative home equity and rising mortgage rates hamper homeowners’ mobility.

Box 4: Evidence that Housing Markets Affect Labor Mobility

Recent studies by the OECD, UNECE, the World Bank, and others show that housing markets can greatly hinder or promote residents' mobility important implications for labor mobility and the efficient allocation of human resources across economy. The United States has one of the most mobile labor forces worldwide because of its labor market conditions, low cost of internal migration, housing markets' fluidity, availability of rental housing, low market transaction costs, and well-developed mortgage market. The low residential mobility in Eastern European and CIS countries (e.g., 3.5 percent in Kyrgyzstan) implying a move every 50 years or so, has contributed to labor market rigidities. Empirical evidence from the 2012 World Bank study of labor mobility in Ukraine shows that housing costs and undeveloped rental markets form one of the top three barriers to labor mobility in that country, in addition to the system of residency permits, credit scarcity, and migration costs.

Three most important barriers to labor mobility in Ukraine:

Registry, Credit, and Housing



Source: World Bank, *Ukrainian Labor Mobility Study* (2012)

Rental tenure, as opposed to homeownership, is an important predictor of labor mobility. Studies in OECD countries including from Eastern Europe have shown that homeowners are less mobile than market renters. As an example, very high rates (93%) of homeownership, combined with a lack of commercial rental housing, appear to be critical barriers to internal labor mobility in Ukraine. For example, more than 80% of Ukrainians surveyed would not move despite a 1.5 times increase in salary, while more than 50% would consider moving if provided with free housing - a vivid illustration of how the housing market influences mobility decisions among families and individuals.

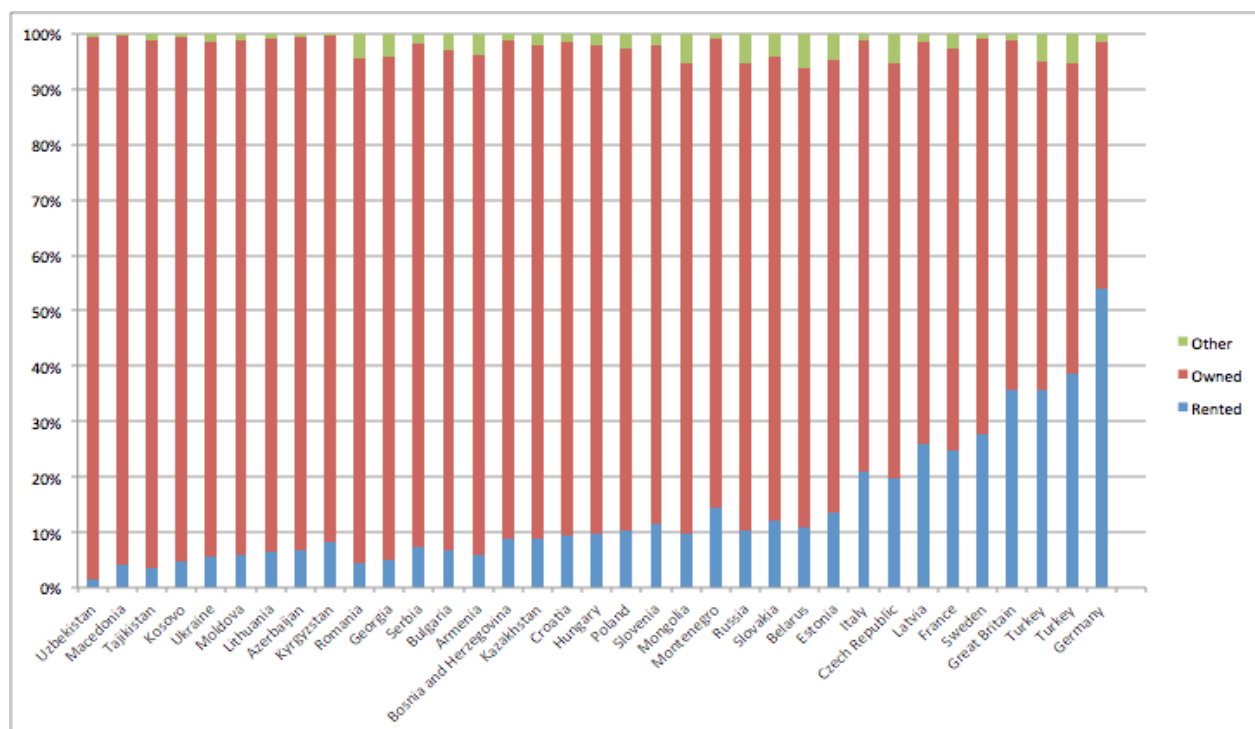
Rental housing has remained outside the focus of Azerbaijan's housing policy since 1991 despite its role in balancing housing choice and facilitating housing market fluidity. The Ministry of Economy and Industry, which is responsible for housing policy, does not have an assessment of the rental segment of the housing sector and has not developed a comprehensive program for fostering the development of the rental segment with requisite objectives and performance indicators. The share of rental housing has fallen well below international benchmarks. Presently, some 5-7 percent of the housing stock in Azerbaijan is formally rental,⁷² although in Baku's central districts it is much higher, exceeding 25 percent in the case of Nasimi.⁷³ In every

⁷² European Union report by J. Fiszer, A. Chalabova: "Support to Azerbaijan in Reforming the Housing Sector – Gap Analysis Report," November 2013. Figure 7 indicates the level is closer to 7%.

⁷³ World Bank, *Greater Baku Household Survey* (2014)

country, a certain segment of the population cannot afford to buy a home, cannot get mortgage credit, or simply does not want homeownership for some period in their housing life cycle. And this despite rental housing being the object of considerable attention and support in the developed economies, which have much higher share of rental tenure than the record-setting homeownership in transition economies of ECA, including Azerbaijan with its 90+ percent homeownership rate. The figure below presents the owning-renting mix in selected countries.

Figure 41: Owning-renting mix in selected countries



Source: LITS (2010)

Generally, renting incidence increases with city size and with a preponderance of high-density, multi-family buildings. It is especially prevalent in 'expensive' core-urban and mid-urban locations of metropolitan cities.⁷⁴ In Germany, in 2003, the country's rate of rental tenure was 60 percent, while in Berlin it was 89 percent; in the USA, the rate of rental tenure was 34 percent, while in New York it was 55 percent; in the UK, the rate of rental tenure was 31 percent, while in London it was 41 percent.⁷⁵ The proportion of renters in any city depends also on the nature of the local land market, the proportion of recent migrants, the amount of public employment, and on topography that determines availability of affordable, well-located land suitable for residential use. Incidence of renting may depend even on possibilities to encroach land with illegal construction. In cities where it is not possible, more people tend to become tenants.⁷⁶

Around the world, rental policies are attracting growing policy attention. Until the global mortgage, financial, and fiscal crises of 2008, housing policies in transition (and other) countries were strongly focused on increasing homeownership, even though some development institutions (UNHabitat 2003, World Bank 2006) were calling for greater recognition of rental tenure in housing policies. There had been very little discussion about market-based rate rental housing, less about social housing, and virtually none about public housing. However, after the 2008 crises, the international housing debate 're-discovered' the rental housing segment and its integral role in housing policy.⁷⁷ Governments in the transition economies of ECA have increasingly

⁷⁴ Hence, it is inaccurate to focus only on country averages.

⁷⁵ UN-HABITAT (2003).

⁷⁶ See UNHABITAT (2011) for more discussion.

⁷⁷ See discussion in World Bank (2013).

been recognizing that sustainable homeownership for all citizens is neither financially or fiscally possible, nor is it desirable for all household groups and life-cycle stages. Consequently, they have acknowledged the need for post-privatization housing policies addressing, *inter alia*, the need for more public, social, and market-based rental shelter options for their populations. These countries have also been realizing that excessive homeownership can create disincentives to relocate closer to jobs and thus become a ‘mobility trap’ in labor markets.⁷⁸

1. Legislative and institutional framework⁷⁹

1.1. Rental Legislative Framework in Azerbaijan

Regulatory framework for renting is basically in place albeit with some remaining gaps. Formal renting of residential dwellings is popularly referred to as *commercial apartment lease (agreement)*, and is regulated by the Civil Code (2000) (Chap. XXXIII). Rental accommodations are required to be filed in written form and registered in title registry if it lasts longer than 11 months (Art. 139). It is important to note that formal Civil Code renting is not subject to rent controls, and neither is informal renting. The Code requires the landlord to serve 3-month termination notice, but does not require it of the tenant.⁸⁰ Additional regulations are embodied in the specific *Law on Leases (1992)*. In practice, most residential renting agreements are unwritten (verbal) so they avoid governance by the Code, and those that are in written form avoid registration by setting duration for up to 11 months. In Greater Baku, over 72 percent of residential renting agreement are in unwritten form.⁸¹

Chapter 33 of the Civil Code regulates relations between landlords and tenants based on the principle of equality of the parties (Arts. 675 – 699), which includes definitions of rights and responsibilities and their legal enforcement. Any additional regulation of landlord-tenant relations is embodied in written rental agreements, which are typically drafted by real estate agencies,⁸² and contain stipulations regarding: (i) subject property; (ii) terms and conditions; (iii) responsibilities and rights of the landlord; (iv) responsibilities and rights of the tenant; (v) duration and termination of contract; and (vi) other considerations. Although there is no separate definition and regulation of residential renting in the Civil Code (2000), the Housing Code (2009) regulates social renting arrangements including eviction sanctions.⁸³ This constitutes a gap in regulating market-based, non-social residential tenancies.

Since renting is recognized as commercial activity, it is subject to the Tax Code (2000) (Art. 679), which requires landlords to pay income tax. In practice, most landlords enter into verbal (unwritten) agreements and thus avoid income tax liability. This also means that rights and obligations in rental tenancy agreements embodied in the Civil Code (2000) are not effective.

There is a framework for formal renting by small-scale, individual homeowners. Those small-scale rental owners who choose to operate in the formal sector are subject to the Civil Code’s rental contract regulations and are subjected to the income taxation regime. Through this they may operate as individual entrepreneurs (small business), as a limited liability company, or as a partnership. There may be various reasons for their formal rental operations: (i) concentration of rental dwellings in one ‘rental’ building, which is highly visible; (ii) tax incentives encouraging formal rental operations; and (iii) access to (project) finance to fund retrofitting and upgrading. This framework, however, still lacks more expedient dispute resolution mechanisms, such as rent tribunals, mediation, and arbitration services, as well as effective eviction procedures. On the other hand, the Civil Code (2000) gives parties a freedom of contract (Art. 6), which allows parties to structure rental contracts in the way that suits them (Art. 390), as long as they do not violate provisions of the Code.

⁷⁸ See discussion in BEST (2011).

⁷⁹ This does not include the non-market, ‘social’ rental framework.

⁸⁰ Tenants can also terminate with 3-months notice, but only if accepted by the landlord; see Dentons (2014).

⁸¹ World Bank, *Greater Baku Household Survey* (2014).

⁸² Agencies need written contracts to substantiate claims for receiving commission.

⁸³ The Code differentiates between non-payment of rents and willful damage and misconduct.

Taxation of rental income is regulated, but needs some incentives for individual landlords to formalize. The Tax Code (2000) recognizes rental income and taxes individual landlords at an income tax rate of 14 percent (Art. 124). Taxable rental income can be reduced with deductions for expenses incurred to generate that income (Art. 115.3 0 115.8). There is also a possibility for ‘amortization charges’ (capital cost allowance/depreciation) applied to building capital costs at the rate of up to 7 percent per annum (Art. 114.3.1), which is quite a favorable rate.⁸⁴ The Code also allows to carry forward rental losses up to five years and set them against future profits (Art. 121).

Informal renting, which dominates in Greater Baku, has produced some practical mechanisms. The effectiveness of the Civil Code (2000) in regulating informal rental contracts is questionable for unwritten contracts, so the parties are left to resolving their disputes internally, although they sometimes ask real estate brokers to help with mediation and arbitration.⁸⁵ The informal market has developed some practical mechanisms allowing it to function, albeit less efficiently than the formal market.⁸⁶ Simple oral agreements do not list responsibilities and rights of the parties.⁸⁷ When disputes arise, the parties use various informal methods to reach a solution.⁸⁸

1.2. Institutional Framework Supporting Formal Rental Market

There is no specific institutional framework to support development of the rental market in Azerbaijan. Housing policy and its programs have been focused solely on fostering the homeownership market. There is no separate regulation on residential renting/leasing in the Civil Code (2000) and there is no dedicated law on residential tenancies, since the Housing Code covers only social renting (public housing). In addition, there is no specialized institution for resolving landlord-tenant disputes in the residential market. Developed countries with a high incidence of residential, market-based renting have in-depth experience in regulating residential tenancies in such a way as to prevent or minimize landlord-tenant conflicts, and if they do arise, they have experience using expedient conflict resolution mechanisms. See Box 5 for a discussion of landlord-tenant regulations in Germany.

⁸⁴ In Poland, for example, it is 2.5% and in Canada 4%.

⁸⁵ Those brokers who are viewed with confidence by both parties.

⁸⁶ For example, tenure security of renters cannot be as good as in formal renting governed by the Civil Code.

⁸⁷ Based on interviews with informal tenants.

⁸⁸ Much depends on the sentiment of the rental market; e.g., landlords facing the prospect of losing a tenant in a ‘renters’ market’ are ready to make concessions and vice versa.

Box 5: Some regulations on landlord-tenant relations in Germany

Rent setting and rent increases:

Setting of rents and rent increases are freely negotiated, but landlords cannot demand over 20% above a comparable rent level. To avoid disputes, contracts may contain gradual rent-increase or indexation clauses. Rents cannot change more than once a year and tenants have to be informed in writing about dates of the onset of rent increases. If there are no clauses, landlords have to inform tenants 15 months in advance, and rent increases are limited to 20% over three years. Landlords must state their reasons, including expert opinion showing three 'sample' rents for comparable units, or they can present a 'qualified rent table' issued by the municipality and approved by landlord and tenant associations.

Duration and termination:

Duration of rentals may be time limited or unlimited, with the latter a dominant form. Limited duration requires a justification. 'Ordinary termination' notice on unlimited contracts can be served if the tenant breaches the contract, if the landlord needs the unit for his purposes, or if the contract prevents economically justifiable use of the unit. Notice period for landlords for tenant's leaving the rental can stretch three to nine months depending on how long the tenant has lived in the unit. The notice period for tenants by landlords is usually three months and needs no justification.

2. Rental Housing Situation

Data and information on rental housing is not officially compiled. Capturing information on rental housing from official sources and existing real estate organizations is difficult since: (i) renting remains limited in general and is concentrated only in some areas; (ii) most rental arrangements are informal and are not reported for taxation purposes; and (iii) rental housing has not been a focus of attention of Government housing policies and programs.

Some information has been produced in two recent surveys: at the national level, the LITS in 2010,⁸⁹ and the Greater Baku Household (HH) Survey carried out by the World Bank in 2014 to support this diagnostic study. The Greater Baku Household Survey had a very high response rate with 94 percent of households selected accepting to participate; it is at present the main source for the analysis of typologies of renters and available rental housing options and prices.⁹⁰ The survey found that 8.38 percent of households living in the Greater Baku area are renters. However, the survey lacks socio-economic data due to restrictions set by the government on collecting such data. Some additional information on rental market activities is gathered by real estate analysts, such as Immovable Property Market Indicators by the MBA Company. In addition, anecdotal evidence from real estate brokers, who facilitate the operations of the informal rental market, often constitute the only supplementary information and data.

2.1. Rental Housing Typology

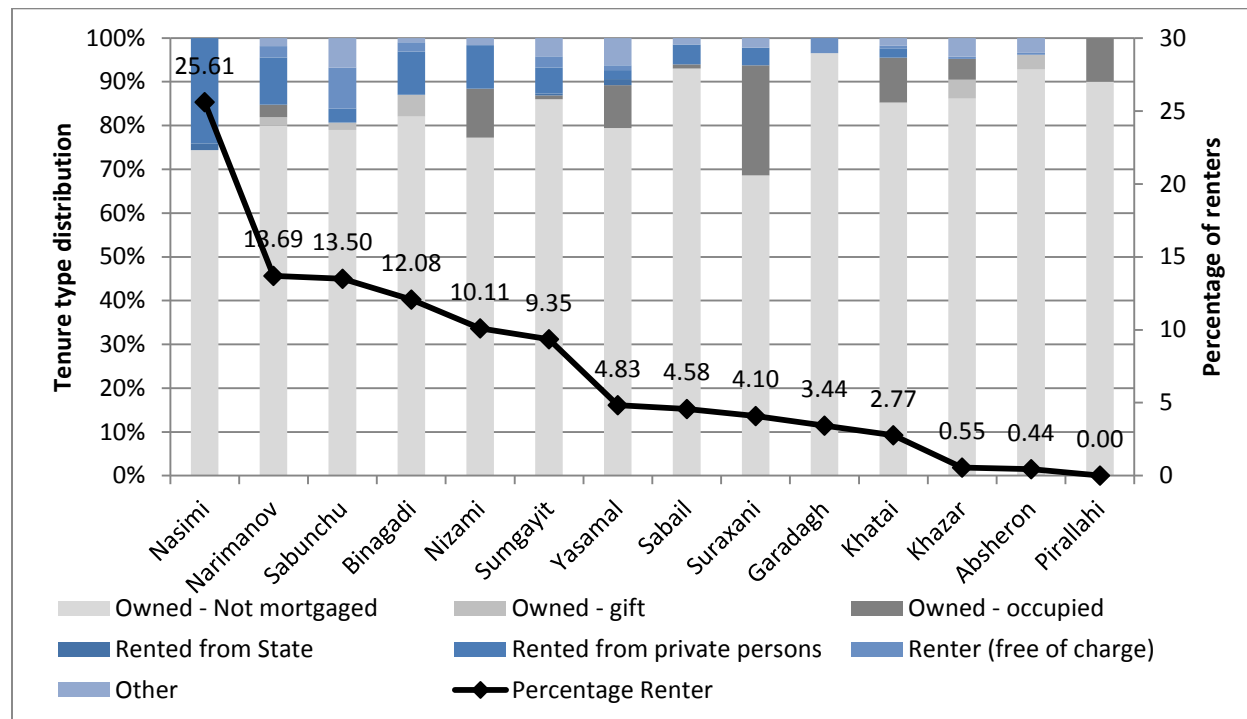
Rental tenure in Greater Baku is highly concentrated in core-urban zones dominated by multi-family buildings. Most renters live in Baku (73 percent), the Eastern Suburbs (13 percent), and Sumagayit Satellite City (13 percent). The highest share of renters is found in core-urban areas of Nasimi, Narimanov, Sabunchu, Binagadi, and Nizami, with the percentage of renters among residents ranging from 10.11 percent in Nizami to as high as 25.61 percent in Nasimi, as shown on Figure 42. It is evident that high density urban zones dominated by multi-family buildings exhibit higher incidence of rental tenure, except for Sabunchu, which

⁸⁹ European Bank for Reconstruction and Development and the World Bank, "Living in Transition Survey II" Survey of households (2010).

⁹⁰ World Bank, Greater Baku Household Survey (2014).

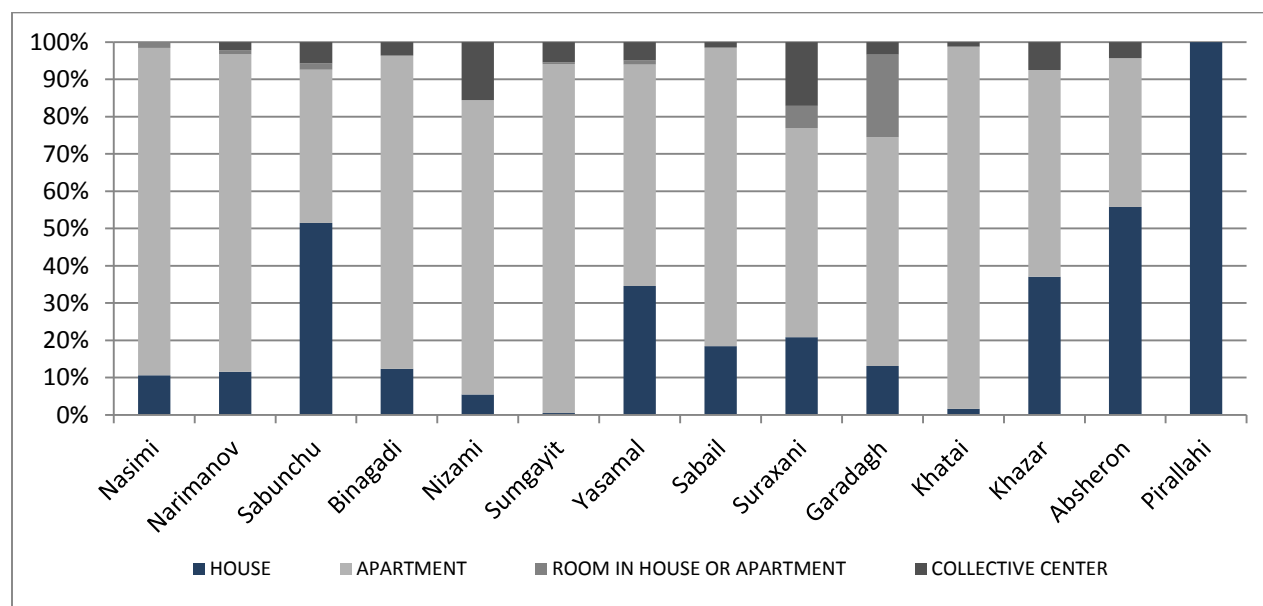
has slightly more houses than apartments. And districts with the lowest rental incidence are those of peri-urban character with low density and little, if any, multi-family buildings (e.g., Pirallahi, Absheron, Khazar).⁹¹

Figure 42: Tenure form and percentage of renters by district



Source: World Bank, Greater Baku Household Survey (2014)

Figure 43: Dwelling type by district



Source: World Bank, Greater Baku Household Survey (2014)

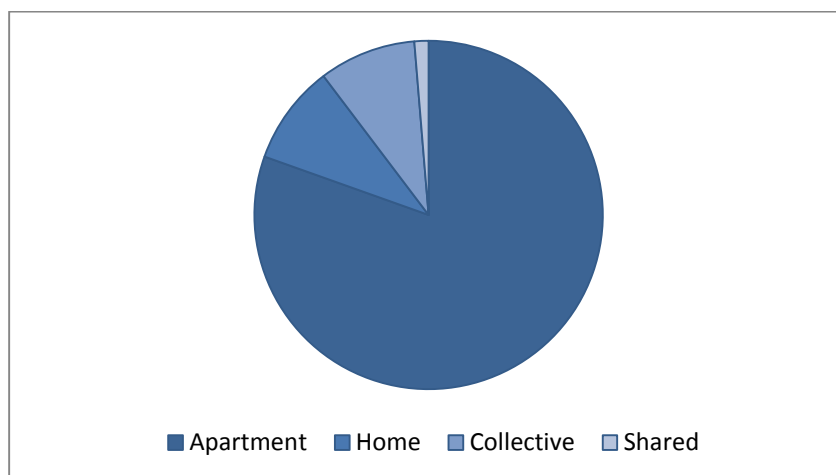
Renting in Greater Baku correlates strongly with apartments and hence with multi-family buildings (Figure 43). Over 80 percent of renters (80.44 percent) in Greater Baku live in apartments, against 9.25 percent living

⁹¹ Except for Sumgayit district, which is a separate urban center from Baku.

in single-family homes. The remaining 9 percent are households living in collective centers (they consider themselves as renters) and individuals renting rooms in a larger house or apartment (less than 2 percent).

Renting in Greater Baku is also strongly correlated with residential mobility and urban migration. Over 80 percent of renters (81 percent) in Greater Baku have lived in their dwellings for less than 10 years, compared to only 21 percent of owners. And residential mobility correlates also with urban migration, although less strongly, as 61 percent of renters were living outside Greater Baku prior to moving to their current dwelling, compared to only 37 percent of owners.

Figure 44: Type of dwelling - Renters



Source: World Bank, *Greater Baku Household Survey* (2014)

2.2. Rental Market

Finding and Contracting Rental Dwellings

Renters find their dwellings mostly through realtors and agencies (nearly 47 percent), and through personal contacts. Renters with oral contracts prefer to use realtors (49 percent) over agencies (3 percent), while those with written contracts equally use realtors and agencies (18 percent each). Almost one quarter of renters (24 percent) rely on friends and relatives to find their rental dwelling. Even though renters rely heavily on realtors and agencies for finding their dwellings, very few pay a fee for these services (4 percent) with those having written contracts paying more often (7 percent). This indicates that a commission is typically paid by landlords.⁹²

Most of the rental contracts are in the form of oral agreements. Oral contracts predominate (72 percent) over written contracts (28 percent). Renters feel a considerable sense of security with their rent tenures. Despite the dominant use of oral contracts, most renters (66 percent) believe that their landlords are unlikely to ask them to vacate the premises without giving due prior notice. Tenants without written contracts are more optimistic in this respect (72 percent) than those with written contract (49 percent).⁹³ Landlords typically do not take security deposits – only 3 percent of renters paid them, slightly more in the case of written contracts (4 percent).

Rents and Trends

Due to the lack of official reports on the rental market, information and data on rents and trends is derived from the recent World Bank household survey,⁹⁴ and from professional market analysts.⁹⁵

⁹² Interview with the MBA market analytics company. Commission amount is usually 30-50% of monthly rent, depending on length of the contract.

⁹³ The reason for this might be that written contracts are typically prepared by realtors to secure their commission and not for tax registration.

⁹⁴ World Bank, *Greater Baku Household Survey* (2014).

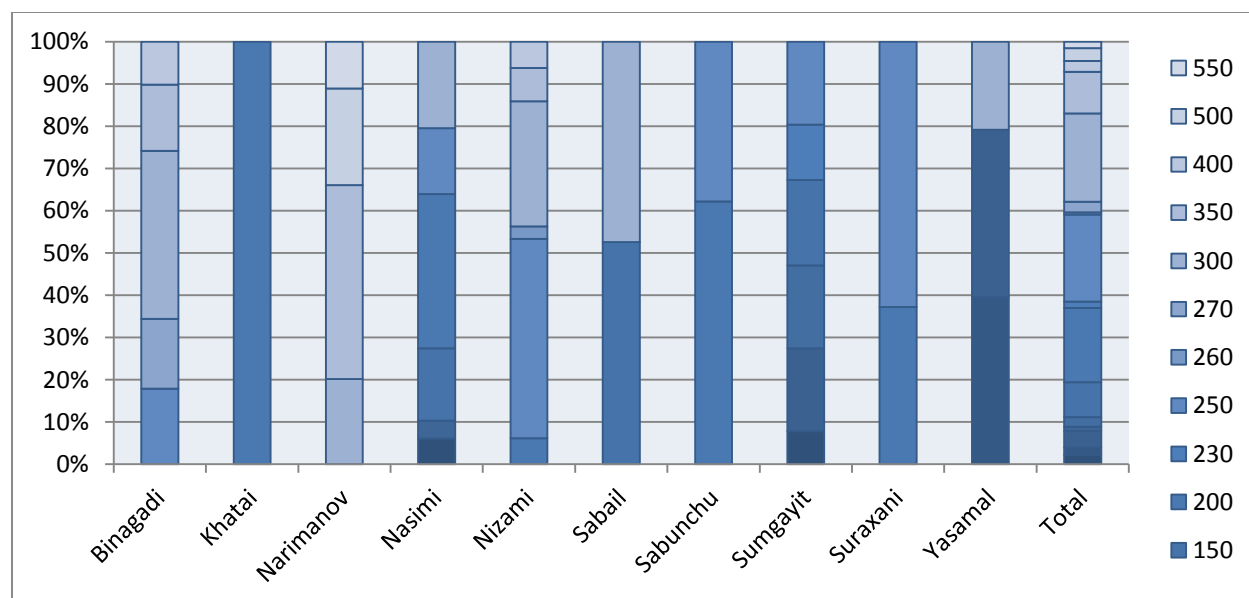
⁹⁵ Interview with the MBA market analytics company, which produces monthly market indicators for the Central Bank of Azerbaijan.

Rents are relatively stable in Greater Baku. The rental market has been experiencing a continuously increasing supply of apartments for rent over the past 5-6 years. Negotiations of rental contracts involve rent discounts, which typically are in the range of 5-10 percent of the asking rent amount. Only rents in the upper-end (luxury) market niche have dropped drastically as foreigners and rich business clients have virtually ‘disappeared’ in the wake of recent economic downturn.⁹⁶ Due to the February 2015 devaluation, rents in USD have declined considerably, but have been stable in AZN.⁹⁷

Rents show considerable differentiation in the same locations. There are three rental market segments customarily considered by market participants and analysts:⁹⁸ (i) low-end (*cheap*) below 500 USD/month; (ii) mid-level (*average*) between 500-1,000 USD/month; and high-end (*expensive*) above 1,000 USD/month. Within each segment rents vary further by size, standard, and location of dwellings with obvious correlations. In core-urban locations there is quite a mix of rents paid reflecting considerable heterogeneity of rental offerings in terms of size and quality standards (see Figure 45). Most renting clients are currently lower-income households looking for accommodation costing less than 500 USD per month.

A more standardized measure of rental levels is possible when looking at rent amount per room, which allows adjusting for size. Generally, rent per room in Baku averages at 131 AZN/month, while in Sumgayit 85 AZN, thus reflecting locational superiority of Baku. Within Baku one can distinguish high-rent areas of Binagadi, Narimanov, Nasimi, and Nizami, with rents per room ranging 123-159 AZN/month and low-rent areas of Sabail, Yasamal, Khatai and Sabunchu with rents per room ranging 72-89 AZN/month.

Figure 45: Share of monthly rental levels by location (Manat)



* As very few households are renters, representation at the district level of rental data is not assured

Source: World Bank, *Greater Baku Household Survey* (2014)

⁹⁶ Luxury villas that used to rent for 10,000 AZN are now available at 2,000 AZN.

⁹⁷ Immovable Property Market Indicators, March 2015 shows a year-on-year decline in average asking rent in USD at -21.53%, and a slight increase of 5.04% in rent in AZN; see MBA (2015).

⁹⁸ This is what is used in Immovable Property Market Indicators produced by MBA market analytics company for the Central Bank of Azerbaijan; see MBA (2015).

Turnover in the rentals is about half of sales. In May 2015 some 1,100 sales were reported in the Greater Baku area and 600 rental contracts. These figures are rough approximations and are closer to deals made by realtors and agencies, so that actual numbers may be higher.⁹⁹

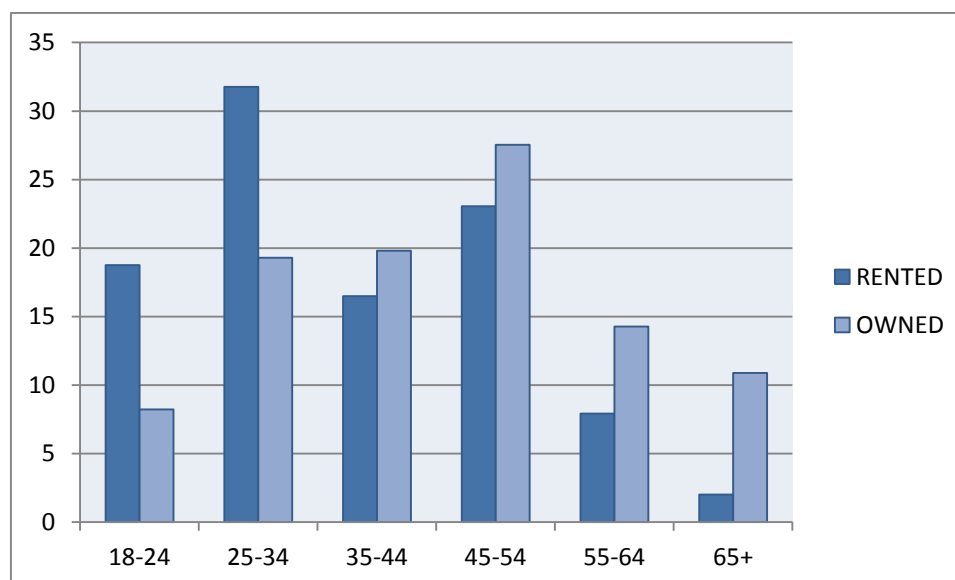
Present Rental Trends

In March 2015, rental transactions had average rent listed (asking rent) at 609 USD/month. Average dwelling listed for rent had 2.23 rooms and 73 m² of floor area. Average asking rent in the low-end segment was 358 USD/month, in the mid-level segment was 709 USD/month, and in the high-end segment was 1,435 USD/month. Across all the segments one-room dwellings averaged 345 USD, two-room dwellings 542 USD (271 per room), three-room dwellings 767 USD (256 per room), four-room dwellings 1,103 USD (275 per room), and five-room dwellings 1,525 USD (305 per room). In the historic center (1st zone), average asking rent/month was at 1,043 USD; in the CBD (2nd zone), it is 827 USD; in mid-urban residential (3rd zone) it is 564 USD, and in the peri-urban zone (4th zone) is 420 USD.

Demand and Affordability

Renters in Baku are generally young, mobile, and low-salaried households with few children. The Living in Transition Survey (LITS) in Azerbaijan¹⁰⁰ and the Greater Baku Housing Survey¹⁰¹ characterize renting households as younger than homeowners (Figure 46), forming smaller households (Figure 47), and as more mobile in the sense of living shorter periods of time in their current dwellings. Share of young adults (18-24) among renters is much higher (18.76 percent) than for owners (8.22 percent). Similarly among young families (ages 25-34) renters's share (31.76 percent) is much higher than for owners (19.29 percent). Then in mid-life age intervals (ages 35-54) owners form a slightly higher share, with their share increasing considerably during pre-retirement age (ages 55-64) as compared to renters (14.27 vs. 7.91 percent). Finally, during the retirement age of 65+, the share of owners is much higher (10.88 percent) than renters (2.02 percent).

Figure 46: Age distribution of renters vs. owners



Source: Living in Transition Survey, LITS (2010)

Being younger than owners means that renters form smaller households and have more of their income coming from salaries and less from pensions. Furthermore, they have fewer children than home owners, and

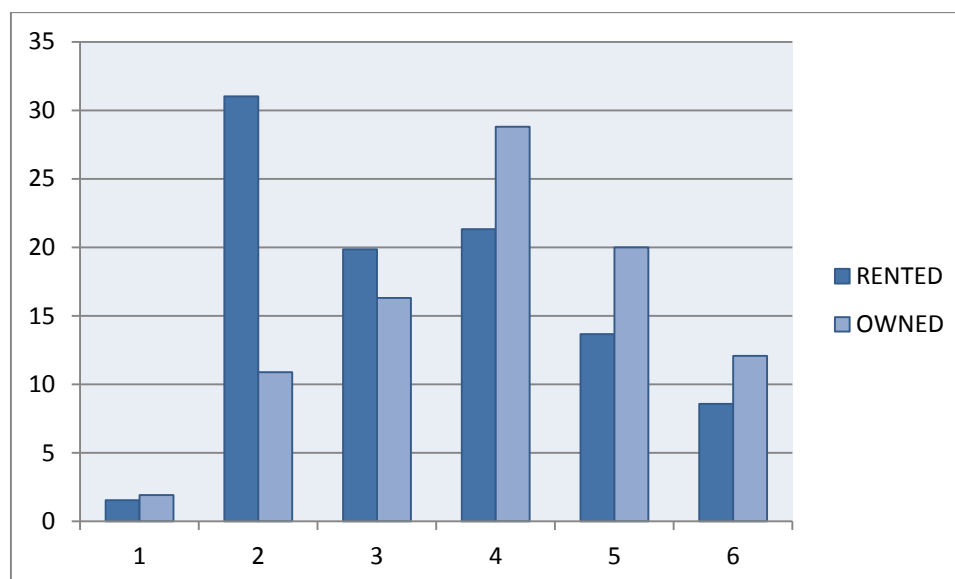
⁹⁹ The MBA market analytics company, which monitors the market for Central Bank of Azerbaijan is relying mostly on data from the Association of Realtors.

¹⁰⁰ See LITS (2010).

¹⁰¹ See World Bank (2014).

almost half of them (49 percent) have no children. Renters work slightly more than home owners in the past 12 months, but are more likely to be 'informal' workers without a contract with employer. Their education attributes are skewed, as renters are both less educated and more educated than owners.

Figure 47: Household Size of Renters and Owners

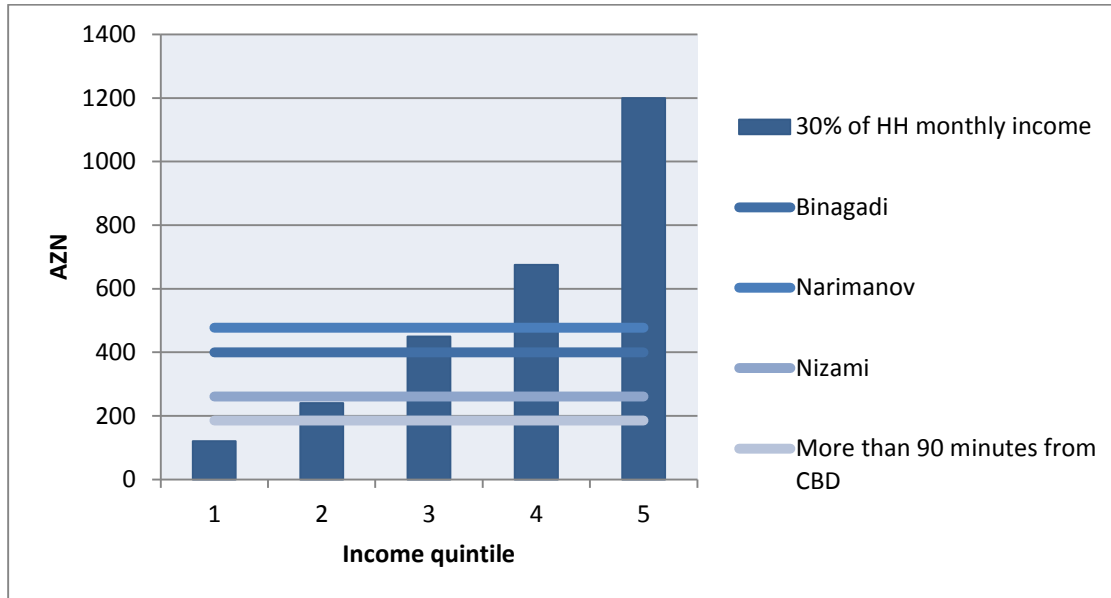


Source: Living in Transition Survey, LITS (2010)

The above figure shows clearly that renters tend to form smaller 2-person households more often than owners (31.03 percent to 10.89 percent). Renters also tend to form 3-person households slightly more often than owners (19.86 percent to 16.31 percent). This is consistent with renters typically being younger and also more mobile. Renters dominate the group of households with durations shorter than 10 years in the current dwellings while owners dominate where durations in the same dwellings are greater than 10 years.

As discussed in Chapter 3 (Section 3), some renters are facing affordability constraints. When analyzing affordability of renting it is customary to compare rental housing expenditures to net household income. This rental effort ratio (see Glossary) is a standard of comparison across countries and the international benchmark value of this ratio is usually around 30 percent (see Chapter 3 for more discussion). Figure 48 below compares rental affordability in different parts of Greater Baku using the benchmark affordability effort ratio of 30 percent of household monthly income for various household income categories (quintiles). As can be seen in the figure, households in the first quintile (lowest income) cannot afford to rent even in the cheapest peri-urban locations (more than 90 minutes from CBD). Households in the second quintile can only afford to rent in the peri-urban zone. The middle-income households in the third quintile can afford to rent not only in the peri-urban zone, but also in mid-urban locations of Nizami and Binagadi, while not being able to afford the core-urban location of Narimanov. Households in the fourth and fifth quintiles can afford to rent anywhere in Greater Baku.

Figure 48: Mean rental prices in different districts of Baku compared with 30% of HH monthly income



Source: Mean rental price data from World Bank, *Greater Baku Household Survey* (2014)

Means-tested Financial Subsidies are Not Available to Renters

Social and public housing are ways to help qualified households satisfy their need for affordable housing. The notion of affordable rent depends on the acceptable ‘effort ratio’ – share of household income spent on qualified housing expenditures as mentioned above and as discussed in Chapter 3. The ratio is difficult to accurately measure due to the prevalence of unrecorded incomes. Despite the high effort ratios signalling problems with affordability for some household categories, there is no means-tested subsidy program targeting households struggling with the too high effort ratios. In effect, households tend to adjust their effort ratios by reducing expenditures on maintenance and repairs, which contributes to the ongoing and profound ‘decapitalization’ of much of the housing stock as will be discussed in Chapter 5.

Supply and Profitability

In Azerbaijan, like in many other ECA countries still in transition, informal rental housing is provided by individual dwelling owners, who manage their ‘rental business’ and who cannot leverage any form of finance beyond their own home equity typically acquired through the micro-privatization of the 1990s. The rental units are typically of poor quality and small in size, are mainly informal, and are prone to numerous landlord-tenant conflicts that are not supported by institutionalized dispute-resolution mechanisms. Little is known about these suppliers of rental housing in Azerbaijan and in Greater Baku. Not only do official statistics not provide any information and data, but the recent household surveys have not focused on this issue by interviewing renters (besides owners), but not landlords.¹⁰²

Individual and small-scale owners supply most informal rentals that dominate the rental market in Greater Baku. Individual dwelling owners who rent to others form the most numerous landlord category.¹⁰³ In Baku, individuals usually own one or more dwellings, but also may rent out a room in their house or an apartment in the same building in which they live. These individuals most often rent informally in order to avoid taxation and burdensome laws and regulations. Individual landlords who own more than one rental dwelling may

¹⁰² LITS (2010) and World Bank (2014).

¹⁰³ They constitute about 70% of landlords in Mexico and Germany and about half of landlords in USA and France.

seek a third-party property manager responsible for renting out, rent collection, tenant relations, and maintenance. This service does not appear to exist in the case of Greater Baku (and in Azerbaijan), but is used in some transition countries, like Poland, where private rental management companies offer integrated services to individual owners for a commission of about 7-11 percent of gross rental receipts. Such rental managers cater to the needs of individual landlords – providing security of income flow including finding a tenant, and effective enforcement of rental payments (see Box 6).

Box 6: Comprehensive Rental Management for Individual Landlords in Poland

Individual landlords who typically own one or several dwellings in Poland now have a choice of hiring a company specializing in providing comprehensive ‘rental management’ services. The company undertakes to produce a stable income stream to the landlord by renting out the dwelling, re-renting if it becomes vacant, taking care of operating and maintenance activities, and effectively collecting rents at own risk. The landlord pays 11% of gross rental receipts for this service. The company was founded by an entrepreneur who started to purchase dwellings for rent and once he accumulated close to twenty of them, could not find a rental manager to take care of his portfolio. This prompted him to establish his own company and soon he offered this service to other individual landlords. These landlords soon found out that they were getting good returns and began asking the company to seek out additional dwellings to be purchased for rental income, so a sister company was established to provide rental acquisition services to existing landlords. The company has been successful by offering comfort to individual landlords and allowing them to ‘scale up’ their portfolios. It has professionalized the market for rental agency services at the level of small and medium rental investors.

The rental market, despite its widespread informality, has developed a measure of investment profitability that landlords go by when investing purposefully in dwellings for rent. They often compare the expected Gross Rental Yield (see Glossary) to return rates from term deposits in banks. Currently, for example, the Gross Rental Yield stands at about 5.5 percent¹⁰⁴, which indicates a relatively balanced rental investment market. This GRY compares closely with Ukraine (5.2-6.5 percent), is slightly higher than in Poland (4.1-5.0 percent), and much higher than in France and Germany (3.0-3.8 percent).¹⁰⁵

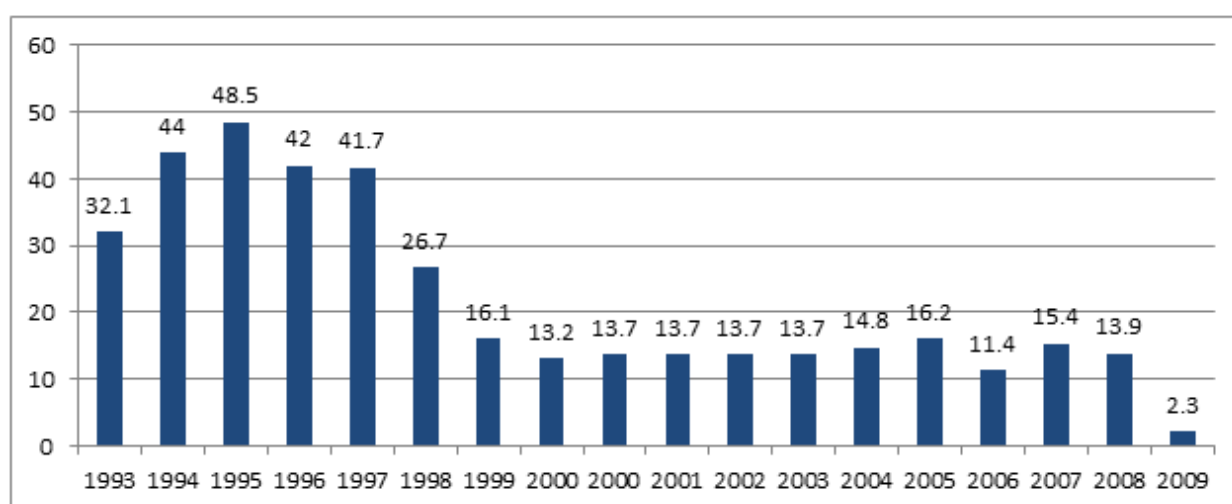
¹⁰⁴ Immovable Property Market Indicators for Greater Baku; see MBA (2015).

¹⁰⁵ Recent data for these countries is in BEST (2011); Ukraine’s indicator predated the current wartime conditions.

CHAPTER 5: Housing Maintenance & Management

While housing units in MFBs were massively privatized in the early 1990s, the maintenance structure of common areas has remained – mostly – unchanged since Soviet times. As per official statistics, 98 percent of the total housing stock in Azerbaijan as of 2009 was privately owned.¹⁰⁶ As estimated by the Bank's household survey in 2014, in Greater Baku ownership levels are at 92 percent. The maintenance function however, proved to be more difficult to privatize (as was the case in many ECA countries – see Box 7). To date, it is estimated that 90 percent of multi-family housing in Greater Baku is still in the hands of ZhEKs, Soviet-era housing management companies overseen by local governments. The very low maintenance fees charged by these companies, as well as their capital repair funding mechanisms, have led to deferred capital repairs of common areas and to the rapid “decapitalization” of the MFB housing stock due to chronic under-maintenance.

Figure 49: Privatization of Housing Stock in Azerbaijan (in thousands of units)



Sources: UNECE Housing Profile for Azerbaijan (2010); State Statistical Committee of the Republic of Azerbaijan

As a result, the housing stock in Azerbaijan has suffered from severe under-maintenance and a capital repairs backlog resulting in successive deterioration of MFBs. More than 77 percent of households surveyed¹⁰⁷ living in MFBs in Greater Baku reported having one or more housing quality issues and a similar percentage indicated their dissatisfaction with ZhEK management. Despite the passage of a new Azeri Housing Code in 2009, which essentially proposed the replacement of ZhEKs with market options for housing management, adoption has been slow by both government agencies as well as by homeowners who remain unaware and/or unwilling to adopt cost-recovery housing maintenance principles. As a result, it is estimated that 30 percent of the stock is reaching the end of its useful life and requires major rehabilitation or demolition.¹⁰⁸

Furthermore, recent housing management reform initiatives have failed to materialize on the ground. While steps have been taken towards modifying and modernizing national housing policies and clarifying property rights of common areas in MFBs to ensure homeowners are responsible for financing their maintenance, legislation has not been fully implemented at the city level due to the lack of secondary enforcement regulations. There are other dynamics fostering *de-facto* management of MFB housing stock in the hands of ZhEKs: reluctance on the part of owners to take on responsibility; lack of awareness regarding the homeowner's role versus the role of the local government; and existing bottlenecks in registering

¹⁰⁶ State Statistical Committee of the Republic of Azerbaijan.

¹⁰⁷ Data from World Bank's *Greater Baku Household Survey* carried out as part of Phase I of this study in 2014.

¹⁰⁸ European Commission - Support to Azerbaijan Housing Sector - "Gap Analysis Report: Support to Housing Policy Reform," November 2013.

homeowners associations (HOAs) and other management alternatives allowed by law. According to the housing survey, in Greater Baku only 9 percent of MFBs are self-managed and just 1 percent are managed by recently-established homeowner associations (HOAs) or private companies.¹⁰⁹

Box 7: Mass Privatization and MFB management in Eastern Europe and Central Asian (ECA) Countries

Privatization became a cornerstone of the initial housing policy reforms in most Eastern Europe and Central Asian (ECA) countries. It resulted in massive and often rapid, give-aways of dwellings (micro-privatizations) to sitting tenants in Multi-Family Buildings (MFBs). In fact, it was the single largest capital asset transfer in ECA during the transition period. These tenure-based reforms were underpinned by the high expectations that they would lead to strong growth of market-driven private MFB investments (construction and modernization) and to a visible increase in asset management (maintenance) efficiency. The passage of time, however, showed that these expectations were generally not met and the physical condition of MFBs continued to deteriorate in many countries.

A number of factors contributed to the generally sub-optimal performance of MFB housing in ECA. First, after governments withdrew from direct provision of housing, including supply-side (construction) subsidies, new investments dropped dramatically and did not recover for over a decade. The region still lags in this respect behind others with comparable housing needs and income levels. Second, modernization of the MFB stock – already an acute issue at the outset of transition (early 1990s) – proved ineffective under the newly-privatized ownership structures, leaving common-property in these buildings and surrounding areas without proper management. Third, turning tenants into owners at virtually no cost to them did little to change the inherited social and cultural mentality that housing is a merit good with rights trumping responsibilities. The “common wisdom” continues to hold that common areas of MFBs and surrounding grounds are “extensions of the street,” and thus count as public space to be maintained, modernized, and paid for by municipalities.

Source: World Bank, Knowledge Note: “Moving Housing and Communal Services into the 21st Century in Europe and Central Asia” (2013)

1. Legislative and institutional framework

1.1. Housing Management and Maintenance Legislative Framework

Efforts to privatize the management and maintenance of MFBs and clarify property rights and responsibility for common areas’ maintenance started as early as 1993¹¹⁰ and were further developed in 2000 with the establishment of the Civil Code.¹¹¹ The Azeri Civil Code passed in 2000 clarified that homeowners of MFBs had rights over the common property serving other dwelling units in a building. These included staircases, lifts, roofs, halls, basements containing equipment for service provision such as electricity, water/supply meters, heating, etc. This move, however, did little to change the behavior of residents, who still believe that common areas belong to the government and that the government is primarily responsible for their maintenance though ZhEKs.

The clarification of common property rights in the Civil Code was an incomplete and insufficient means to bring the reforms needed to improve housing management and maintenance. The Civil Code could not solve

¹⁰⁹ Data from World Bank’s *Greater Baku Household Survey*, carried out as part of Phase I of this study in 2014.

¹¹⁰ Law “On Privatization of the Apartment Stock” (1993); Azerbaijan’s Civil Code that came into force in September 2000; and the new Housing Code of 2009.

¹¹¹ European Commission - Support to Azerbaijan Housing Sector - “Gap Analysis Report: Support to Housing Policy Reform,” November 2013.

the monumental challenges facing both central and local authorities, namely, the ever-growing backlog of capital repairs in the old housing stock; continuing poor quality of maintenance and repair services; unaccountable and unresponsive ZhEKs (considered inefficient and corrupt by homeowners); and the lack of adequate management structures in a majority of MFBs, even those constructed recently. The legislation passed in Azerbaijan has been mainly in reaction to the new housing market situation with its predominantly privatized housing stock, rather than proactive at the on-set of change as occurred in the Czech Republic (see Box 8).

Box 8: Management of Common Property in ECA

Management of common property is a critical area of the legal framework following housing privatization. The forerunners of privatization (Moldova, Lithuania, and Albania) were among the first countries to introduce legislation in 1991, with legal acts governing the basic provision of management of common property introduced only a decade later. In Lithuania, only 20 percent of the MFB stock has HOAs even after 25 years. This is because of the existence of the constitutional freedom of association – residents do not have to join. In Poland, however, there is 100 percent membership, since by law HOAs are created at the moment of first sale of an apartment in a building. The Czech Republic was the only exception, where the establishment of condominium associations was a requirement for the transfer of a multi-family building and individual privatization was not allowed.

Source: European Commission - Support to Azerbaijan Housing Sector – Report 2: “ Recommendations on Housing Management Options of Common Properties,” February 2014.

The Civil Code was therefore followed by the passage of the new Housing Code in 2009 which further modernized the legislative environment with respect to management and maintenance of MFBs and their common areas. The Housing Code lays the obligation of financing capital repairs and maintenance of common areas squarely on homeowners of dwelling units in privatized MFBs, and in doing so also provides homeowners with three management options to select from to ensure capital repairs and regular maintenance functions are implemented. The most progressive among these options (further explained in the next section), is the establishment of Homeowner’s Associations (HOAs), or MMMCs as they are known in Azerbaijan.

However, implementation of the new Housing Code has been very slow: to date only 7-8 HOAs have been registered nationally, most of which are in the Greater Baku Region. One of the key problems is that the formation of HOAs is not obligatory under this law, as in the case of the Czech Republic and Poland (see Box 8 above), and remains voluntary. In addition, the following shortcomings were identified by a European Union-funded Housing Management study carried out between 2013-2015 under the leadership of the Ministry of Economy and Industry (MOEI), and were further confirmed by the World Bank housing diagnostic:

- *Lack of bylaws and specific procedures on how to set up an HOA and lack of recommendations to homeowners as to which is the most appropriate management option to choose based on their tenure type.* The result has been that very few homeowners are willing to form an HOA, and those that do face tedious and mostly unclear application procedures and red tape during registration at the Ministry of Justice.
- *Lack of various types of housing management services being offered in the market.* There has been a lack of interest by the private sector in filling the housing management and maintenance gap, primarily due to ambiguous and non-market oriented procedures. The result is that HOAs have few professional and accredited options in the market to which to contract maintenance services. This has partly deterred HOA formation.

- *Fear of ZhEK redundancy due to new Housing Code rules, followed by reluctance by local governments to change their way of doing business.* The result is that ZhEKs remain the fall-back option for homeowners, and they continue to dominate housing management services.
- *Existing ZhEKs lack the knowledge, comprehensive techniques, and management skills to cater to this newly-created market and demand from HOAs.* The consequence is that ZhEKs continue with 'business as usual' and provide either sub-standard or no service at all.
- In addition to the above observations, the study also notes that *professional property management training and accreditation programs do not exist and are not offered in Azerbaijan.* As a result, Azerbaijan lacks a cadre of professionally-trained and licensed property managers.

Within this context of legislative change, Azerbaijan critically requires a comprehensive Housing Policy at the national level and the development of Local Housing Strategies at the local Raion/district levels. This is needed to tie all elements of the housing market together to ensure a well-functioning system that caters to the needs of different stakeholders – tenants, homeowners, IDPs and vulnerable groups, private developers, the construction industry, management companies, local governments, and the national government. According to the Ministry of Economy and Industry, there is a draft State Program on Development of the Housing Sector for the period 2013-2017 with the objective of improving the legal and regulatory framework, which is currently under review by the Cabinet of Ministers of Azerbaijan; however, it was not made available for the purposes of this study.

1.2. Institutional Framework Supporting Housing Management and Maintenance

The current institutional framework for housing sector development and management, though improved on paper, remains fragmented. Responsibilities are divided between different branches and levels of government (legislative and executive, local and national), leading to ambiguity, duplication of effort, and structural challenges to implementing the new Housing Code in Azerbaijan. At the national level the Executive consists of the Ministry of Economy and Industry, mandated by Presidential decree to be in charge of Housing Sector development, and the Ministry of Emergency Situations, in charge of issuing building permits. At the local level, the Executive bodies responsible for housing are the District/Raion Executive Committees (ExComs). Municipalities surprisingly have little to no role, as ZhEKs come directly under the ExComs. At the Legislative level, the Ministry of Justice is responsible for reviewing and registering HOAs.

There are no clear allocation of powers/responsibilities between municipalities and State executive powers. In fact, contrary to best practice, presently municipalities have little to no power related to housing in Azerbaijan. Interviews with local mayors and deputy mayors in Greater Baku identified their frustration particularly since they understand the housing needs and challenges of their community better than the Raion level Executive Committees. Since municipalities also do not have regulatory powers in the sector, they cannot monitor the performance of ZhEKs.

The new Housing Code allows three management options: (i) direct management of buildings by owners of buildings; (ii) management of buildings by a condominium association (HOA) or specialized co-operatives; and (iii) management by management entities. It is expected that ZhEKs would over time be phased out and replaced by one of these options. However, currently ZhEKs maintain the monopoly over management and maintenance of the MFB housing stock. ZhEKs in Baku city operate under the Housing and Communal Economic Department (HCED), which itself is under the Baku City Executive Power. A fourth existing management option are the Housing Cooperatives that have been established by construction companies that have built new MFBs or by owners of former employee housing provided by former soviet era enterprises/companies. This type of management does not currently fall under any of the options outlined by the Housing Code.

Box 9: Housing Management Options Available to Homeowners

As per the Housing Code of 2009, three multi-family housing management options are available to homeowners:

Option 1: Direct management by owners. Owners of the MFB may sign a contract with a property management company to render housing maintenance and management services. Each apartment owner agrees under the contract to pay the fees for such a service. Alternatively, several owners of a particular MFB could vote to select one homeowner occupying the same premises to render management and maintenance services.

Option 2: Management by condominium associations (HOAs) or specialized consumer co-operations. The most common form of MFB management is the establishment of HOAs; however, they are considered legal entities only when they are registered by the Ministry of Justice. This implies that all potential HOAs in Azerbaijan would have to travel to Baku to get registered; given the 70-day waiting period and the complicated procedures to obtain a registration, it is unlikely that homeowners outside of Greater Baku would be incentivized to register. Once registered, HOAs may collect fees. Housing-construction Cooperatives that provide management services mainly to new buildings, and Employee Housing Cooperatives all fall under this category. Both types also need to be registered by the Ministry of Justice.

Option 3: Management of a building by a management entity. At the moment ZhEKs fall under this category, due to lack of private sector interest. However, in the medium-term it is envisaged that market demand for MFB management and maintenance services would prompt property management companies to be set up.

Source: Housing Code 2009; European Commission - Support to Azerbaijan Housing Sector: "Report 2: Recommendations on Housing Management Options of Common Properties" (2014)

Unlike in other countries with a similar Soviet legacy, ZhEKs have failed to professionalize their services, lack the skills needed to develop their functions, and remain largely inefficient. Poland, a few years after privatization of the housing stock (see Box 10 below), privatized municipal services companies similar to ZhEKs, thereby establishing property management services based on competitiveness early in the housing transition process. The Greater Baku Region, for example, relies heavily on 150 ZhEKs (112 ZhEKs and 42 special purpose ZhEKs) for maintenance services due to lack of alternative management options. In total, only 7-8 HOAs have been registered in the Greater Baku Region. The reality is that ZhEKs have extremely low capacity, are underfunded, are unresponsive to homeowners'/tenants' needs, are inefficient, and do not monitor their staff's performance. The consequence is that under-management, mismanagement, and lack of management (in some cases) of MFB stock perpetuates the system of rapidly "de-capitalizing" existing stock.

In addition, the registration of Homeowners Associations (HOAs) has been constrained by red tape, deterring homeowners from organizing themselves as HOAs. The process of registering a HOA at the Ministry of Justice takes 50 to 70 days. HOA representatives reported that applications are rejected multiple times for minor errors, requiring several re-submission cycles that essentially extend the registration process to more than a year in some cases. Moreover, the Property Committee does not maintain sufficiently detailed building 'passports.'¹¹²

¹¹² Property boundary maps and other details that are essential documents for the registration process.

Box 10: Privatizing MFB Management in Poland

Micro-privatization of multi-family dwellings was often accompanied by privatization of housing management/maintenance services in Poland as a way of ensuring the reduction of housing expenditures by local governments. For instance, in 1993, the Kraków city government encouraged employees of municipal service companies to create private entities by assuring them 3-year initial contracts with the city. Kraków liquidated housing maintenance companies and retained only a strategic management (board) for contracting out building management to privatized (formerly municipal) and newly private property management companies. Private property management companies competed amongst themselves on the level of maintenance fees and offered differentiated fees to privatized owners and rents to remaining tenants. The end result of this reform was *increased cost-coverage (by tenant/owners), more competition in services, fewer city employees, fewer arrears, fewer disputes, and no political pressure by tenant-owners on the municipality to maintain and upgrade common property.*

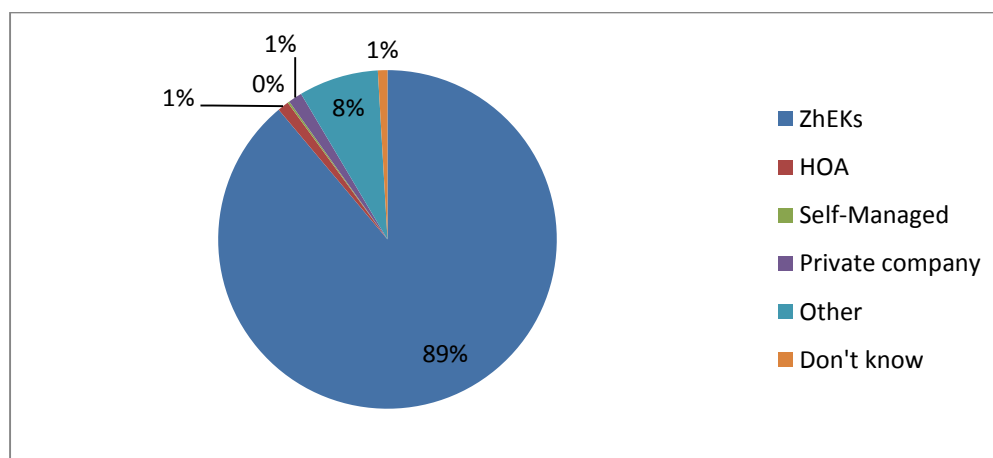
Source: World Bank, Knowledge Note: "Moving Housing and Communal Services into the 21st Century in Europe and Central Asia" (2013)

2. Housing Maintenance and Management Challenges

2.1. Performance of Housing Management Options

As previously mentioned, despite provisions in the new Housing Code, the predominant form of MFB management in Greater Baku is ZhEKs. HOAs as an alternative have yet to catch on among homeowners (Figure 50). ZhEKs still manage privatized MFBs under contractual obligations at locally-controlled prices. It is estimated that 89 percent of households rely on ZhEKs. As mentioned earlier, only 7 HOAs have been formed, two of which are still pending registration. This dominance is further supported by surveys showing that only 1.1 percent of households reported living in buildings managed by HOAs (1 in Binagadi, 1 in Khatai, 5 in Narimanov districts).

Figure 50: Type of Management in Greater Baku (GB)

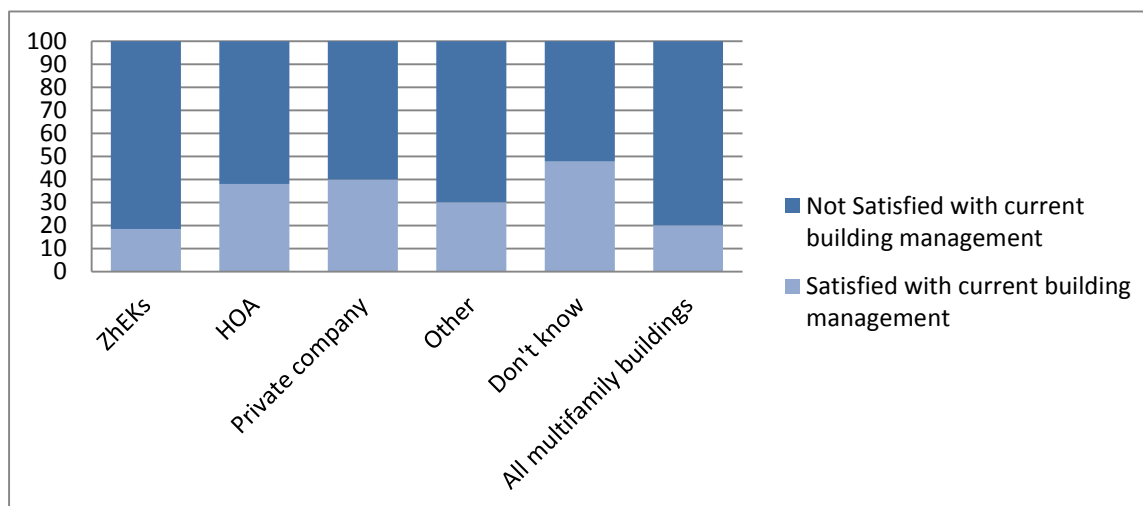


Source: World Bank, *Greater Baku Household Survey* (2014)

The majority of households surveyed (80 percent) are dissatisfied with the way their apartment buildings are being maintained and managed by ZhEKs (Figure 51). While the survey indicates that Baku residents are slightly more satisfied with HOAs and other management companies, given that there are only a handful of HOAs in Greater Baku, it is difficult to determine their efficiency versus other management forms. Focus

group meetings with homeowners and renters living in ZhEK-managed buildings confirmed the findings of the survey. Residents indicated that they cannot rely on ZhEKs for regular maintenance and have in numerous occasions carried out repairs on their own initiative and expense. Owners do not trust ZhEKs and find what little service they provide to be of poor quality and infrequent. These results confirm the need to professionalize management of MFBs.

Figure 51: Satisfaction with different Building Management Options



Source: World Bank, *Greater Baku Household Survey* (2014)

However, homeowners lack the incentives to adopt one of the three permissible housing management options. In particular, changing to a more efficient building management option will mean that homeowners will have to face the prospect of having to inherit the already dilapidated building stock and bare the full cost and responsibility of maintenance. In addition, there are high transaction costs and information gaps for HOA registration that make it difficult to move forward for those willing to do so. Finally, registering HOAs requires concerted collective action among homeowners of MFBs, an effort usually hard to achieve when homeowners continue to believe that common areas are an extension of the street and are to be managed by the State. Hence, there are only 7-8 HOAs registered in the Greater Baku region and only 1-2 private management companies whose main focus is in cleaning.

2.2. Constraints Faced by ZhEKs

The tariffs for maintenance remain very low and households do not pay the true cost for services. According to the 2014 EU housing sector support study, “Inhabitants are paying very low housing maintenance fees (at the level of 0.02 manats/m²/month).” Tariffs collected by ZhEKs are determined on the basis of Resolution № 40 of the Cabinet of Ministers dated March 10, 2000.¹¹³ According to this Resolution, service fees for maintenance were as follows: 1.5 Copecks per month for each square meter of residential area, 20 Copecks per person per month for the use of the elevator in residential buildings, and 1 Copeck per month per square meter of personal garage space.¹¹⁴ Interviews and the Household Survey confirm the specific fees above and confirm that they range between 3-5 AZN per household per month, depending on the size of the dwelling unit and facilities provided (elevator, parking, etc.). Given this, the revenues are not sufficient to cover day-to-day maintenance and ZhEKs do little more than solid waste collection and general administration. Repairs are mostly deferred and capital repairs are in arrears. ZhEK employees are underpaid, receiving on average USD 100 per month. The government provides only material assistance to ZhEKs, but no funding or salary

¹¹³ Resolution No. 40 “On the approval of tariffs according to the housing and communal services and fee for the use of residential area (housing fee) in the houses with state and private housing fund in the Republic of Azerbaijan.”

¹¹⁴ There are 100 Copecks per 1 Azeri Manat.

assistance, and therefore most of the fees collected go towards meeting operational costs. Typically, funds collected are pooled by the ZhEK and then redistributed to meet the maintenance needs of the buildings they collectively manage. However, given that the fees collected are extremely nominal, there are very few funds available to carry out any substantial capital repairs in any of the buildings.

ZhEKs as management entities are not legal entities, but are part of the local government apparatus and are delegated by the State to manage MFBs. The Housing Code of 2009 essentially removes the role of the local government in housing management, thereby making ZhEKs effectively redundant on paper. In order to comply with the law, ZhEKs would need to be restructured and registered as private legal entities/companies in order to continue providing services. This would introduce competition in the property management services business in Azerbaijan, which could in turn lead to an improvement in the quality of maintenance services.

2.3. Constraints on Formation and Operation of HOAs

The registration process of HOAs is slow, confusing, and plagued with red tape. Available information regarding the application and registration process is unavailable or unclear and ambiguous at best. In addition, HOAs face a bureaucratic hurdle in getting Ministry of Justice (MoJ) approval. Discussions conducted during the qualitative assessment revealed that HOAs are requested to revise applications several times, with each subsequent submission taking up to 70 days every time. Furthermore, there is no clarity on which institutional body in government is responsible for HOAs with respect to monitoring their activities, ensuring a certain standard of service provision, and providing guidance to homeowners who want to establish an HOA.

In addition, MFBs assets cannot be easily transferred to registered HOAs. This is the main cause of delays in registration. In order for HOAs to have full management, maintenance, and fee collecting rights over their buildings, the property needs to be transferred; however, authorities are yet to identify the relevant law that would legitimize such transfers. In many cases, the local ZhEKs or municipality do not have the relevant documents, such as the building passport, that is needed to determine the building footprint and the surrounding areas which would fall under HOA management.

Given the state of disrepair of buildings, many of which having not been renovated in 40 years or more, HOAs are reluctant to take over responsibility. Interviews indicate that most potential HOAs are reluctant to take on responsibility without buildings first being renovated by local authorities, and it appears only Benegadi local government is prepared to renovate buildings before they are turned over to the HOAs. Finally, newly-formed HOAs have not moved towards cost-recovery principles and are still applying very low collection fees.

2.4. Common Financing Challenges

The old MFBs are in dire need of capital improvements. The financial burden of major capital renovations currently rests solely on the homeowners or ZhEKs. Given the state of disrepair of most of these buildings, there is an urgent need for major capital improvements. However, the cost of such repairs is prohibitive given the years of deterioration and lack of maintenance. The ZhEKs are traditionally responsible for the common areas of such buildings, but do little more than trash removal and, on occasion, emergency repairs. ZhEKs attribute their inability to maintain these buildings on the extremely low monthly management fees of about AZN 3 per month per household. ZhEKs have two sources of financing: i) the funds allocated from the State budget, and ii) fees collected from homeowners. For example, between 2012 and 2014, 17.8 million Azeri Manats were transferred and distributed to the city and district executive committees and further allocated to respective ZhEKs.¹¹⁵ In addition, utility fees are another source of income for ZhEKs. Despite these sources of revenue, ZhEKs are unable to meet the cost of maintenance as the capital repair costs have become prohibitive over time due to lack of regular maintenance in the past. Homeowners, on their part, are not

¹¹⁵ European Commission - Support to Azerbaijan Housing Sector - "Gap Analysis Report: Support to Housing Policy Reform," November 2013.

organized in most cases: there are only 7 registered HOAs in Baku out of an estimated 10,000 eligible MFBs. They are also incapable, both technically and financially, to undertake such repairs.

The low quality of multi-family building stock will require a huge infusion of capital to bring them up to an acceptable standard. On average, 95 percent of the monthly housing cost goes towards services and only 5 percent goes towards fees for ZhEK management (Table 14). At this rate, it is practically impossible for ZhEKs to meet their own operating costs plus finance maintenance of MFBs and/or finance cost of the demolition of condemned housing. In addition, fees have remained the same over the last 20 years and have not been adjusted for inflation.

Table 14: Sample services cost vs. housing maintenance cost Binagadi district, Baku

Service	Manats per	Total cost towards
Water Supply	18	57
Gas	5	
Heating	7	
Electricity	25	
Elevator	2	
ZhEK fees	3	-
Total	60	-

Massive investments financed by the State are focusing on improving external facades of multi-family buildings in Baku City center, while interior and common areas are not touched. The work involves major improvements, including adding external stone cladding on pre-fabricated external walls, adding balconies, repainting exterior walls, etc. While these efforts are important, the interior of the buildings and common areas, which are in much need of rehabilitation, are not being considered.

Figure 52: Façade work on “Public Beautification” projects



RECOMMENDATIONS

The main recommendations for the housing sector that have emerged from the diagnostic work are presented below.

1. Developing a comprehensive National Housing Strategy

The development of a new National Housing Strategy in Azerbaijan could provide the currently missing overarching framework necessary to address the housing needs of the whole population. While important efforts have been made in the past 15 years, such as the establishment of the AMF, the recent housing management reform, and the façade beautification campaign, these fragmented responses remain insufficient to respond to the important housing sector challenges facing the country. Thus there is a need to develop a coherent housing policy and implementation strategy with clear short-, medium- and long-term targets that can lead the way towards a more efficient and inclusive housing market. This should involve making a more detailed diagnostic of the current situation, establishing overarching goals and principles, identifying specific targets, and developing an action plan for short-, medium- and long-term horizons with identified budget sources. The development of the Strategy will also involve a review and reform of the existing housing legislation, as necessary, and will require – for the purposes of its implementation – the strengthening of existing national housing sector bodies.

2. Strengthen the legal and institutional framework

Existing sectoral institutions at the national level, such as the housing department in the MOEI, will require strengthening. By clearly defining roles and responsibilities, this department shall, in principle, have responsibility for policy development, data collection, monitoring and evaluation, and all programs to do with HOAs and building maintenance, social housing, energy efficient residential buildings, housing finance, etc. In particular, the housing department is expected to:

- *Be responsible for drafting housing policy and sector guidelines and monitoring implementation as outlined above.*
- *Be responsible for preparing budgets and playing an advocacy role for housing so as to justify the maximum allocation possible for housing. At the same time, its duty is to ensure that these funds benefit the most vulnerable sections of the population, and are properly accounted for.*
- *Monitor all housing programs to determine whether they are being implemented according to agreed cost and time parameters, the stated objectives, and in what way program design and implementation procedures can be improved. Monitoring the need of different populations for different housing solutions is also critical in targeting and adjusting housing programs for efficient budget allocation.*
- *Establish a database of all housing in Azerbaijan, and disseminate this information on a regular basis (preferably annually).* It should support knowledge creation in the housing sector (including appropriate statistical databases and tools, elaboration of housing analysis, etc.), as well as promote training for public sector employees with responsibilities in the field (e.g., mayors and public servants). This would provide policy makers and developers with a picture of what type of housing is being built, at what cost and where, and by whom. Such data would form a useful input to the monitoring and evaluation process, but would also be a useful resource for all agencies and companies – public and private – involved in housing production.
- *Play a role in building capacity of other sector stakeholders by convening national workshops or establishing committees to share experiences, both locally and internationally, or to debate policy issues or discuss implementation methodologies.*
- *Provide support to local authorities in the housing sector.*

3. Improve housing management and quality of the housing stock

The improvement of existing management practices will require a combination of improvements in existing incentive frameworks, increase in technical and financial capacity of both homeowners and public authorities, and development of the right regulatory environment for enforcing the law. It will also require an appropriate business environment for establishing HOAs. Given the lack of incentives to form HOAs, the high transaction costs to establish them, and the lack of capacity to put in practice efficient housing management systems, there is a tendency to continue the status quo where each party expects the other to take responsibility for maintenance. Changing existing practices requires a concerted effort and is likely to involve at a minimum: (i) developing missing bylaws and defining simple and transparent procedures to mainstream the establishment of HOAs; (ii) creating incentives for the establishment of HOAs; and (iii) developing a technical assistance program aimed at strengthening existing management practices and professionalizing housing management. One option to improve the incentive structure is to make HOAs mandatory by law or conditional for the reception of capital improvement laws. These recommendations are also shared by the recent EC Housing Reform study done in Azerbaijan.¹¹⁶

In parallel, it is recommended that GOA consider developing a program to provide State co-financing for capital repairs, such as a National Housing Fund (NHF). Given that the concept of HOAs is relatively new in Azerbaijan – with only 7 registered HOAs to date – the likelihood of these HOAs having adequate funds in the short-term to pay for even a small share of the capital repairs (assuming government co-financing is in place) is very low. It is thus recommended that a national-level fund (hereinafter referred to as the National Housing Fund or NHF) be established to provide long-term (10-20 years), subsidized loans to the HOAs for capital repairs of their buildings.

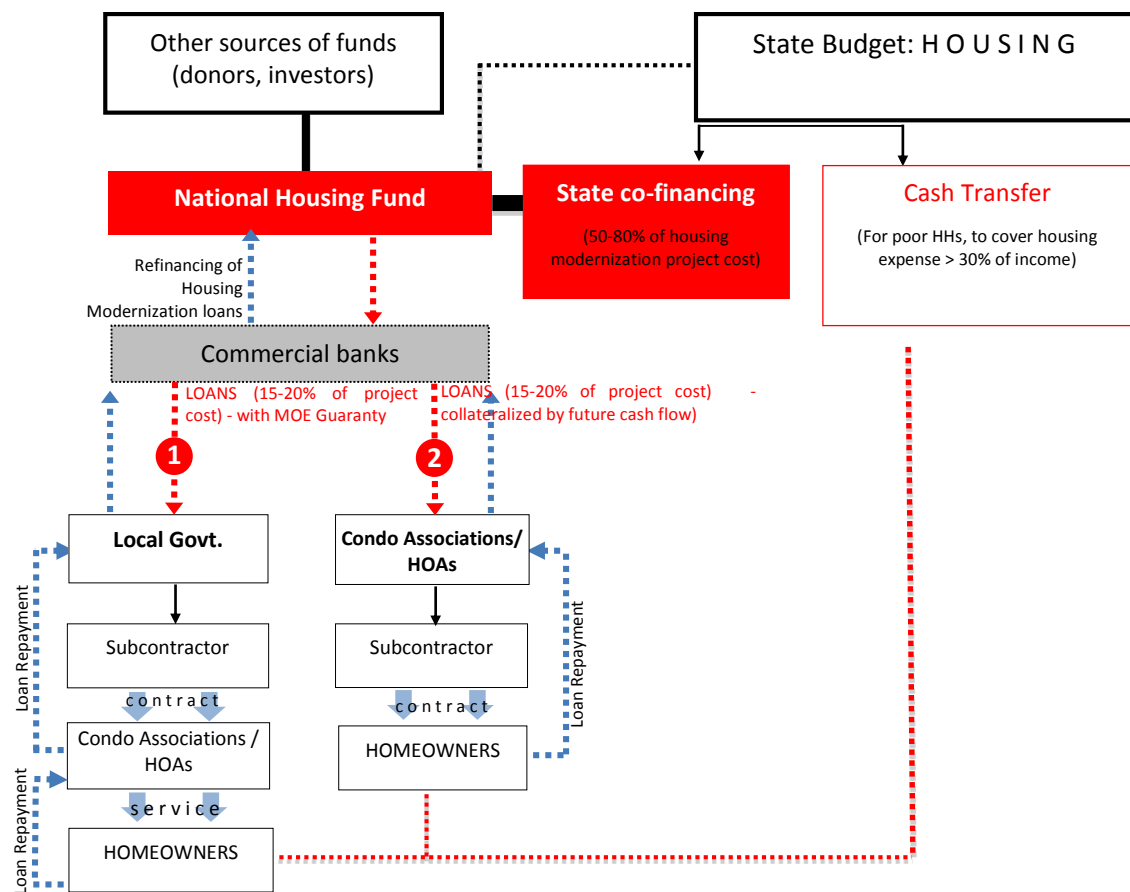
Box 11: State-funded grants for MFB repairs

In the Czech Republic, for example, there are two schemes to help with the modernization and renovation of pre-fabricated, multi-story, communist-era blocks in which many co-operatives are based. The first program was initiated in 1997 and provides grants for urgent technical upgrades for up to 40 percent of the budgeted cost. The second program is aimed at upgrading and renovating housing and is designed as an interest subsidy and a guarantee from the Czech Guarantee Development Bank. In 2006, the program's provisions made market loans effectively interest-free.

Figure 53 illustrates how these two elements of State support – together with a cash transfer program – could be channeled and phased to mobilize capital repairs of old buildings by HOAs.

¹¹⁶European Union - Support to Azerbaijan Housing Sector Report 2 - "Recommendations on Housing Management Options of Common Properties," February 2014.

Figure 53: Illustration of potential program for capital repairs of old MFBs



Key points

- Both State-funded co-financing, as well as the loans from the National Housing Fund (NHF), must be tied to an element of mandatory technical assistance – which is factored into the cost of the financing.
- For ease of administering this type of government financing, it will also be important to develop prioritization criteria – for example, related to the condition of the building, or the income levels of the residents, and so on. Also, it will be important to develop a standardized package of capital improvements that would qualify for this funding – for example, roofs, walls, windows, etc.
- It is inevitable that the formation and capacity-building of HOAs will take time, possibly 3-4 years. In the interim, this financing support (through both the co-financing as well as the NHF) could be channeled to local authorities. In other words, in the short term, local authorities could be the borrowers/recipients of these funds (channeled through commercial banks which act as the financial intermediaries). And in the medium term (i.e., 3-5 years), as more HOAs get established, the financing could be channeled directly to them. However, the involvement of HOAs in other parts of the work implementation (contractor selection, payment approvals, etc.) is critical to instill a sense of ownership.
- At least part of the financing for the proposed NHF and/or the co-financing could come from the funding currently allocated to the Public Beautification program. In addition, it is highly recommended that the beautification program be coupled with – or even (partially) replaced by – programs to address more critical capital improvements (common areas, roofs, energy efficiency, structural integrity, etc.).
- Other potential sources of funding for the HMF could be donors and IFIs, including the World Bank.

4. Improve targeting of public funds for housing

Several instruments may be considered to provide more targeted public housing assistance to lower income groups. These could include introducing new programs as well as reviewing and reforming existing programs, as described below.

(i) *Introduce a cash transfer program for poor households.* The State should consider introducing a cash transfer or housing allowance program to subsidize individual low-income households that are paying more than a certain percentage of their income (i.e., 20-25 percent) on housing and utilities combined. This is proposed as a standalone program, but could also apply for specific periods of time to those “poor” households living in buildings participating in home improvement projects. This will serve as an incentive for them to cooperate with the HOA and agree to the improvements. Ensuring these households pay their share might otherwise be a problem, especially in buildings where a large majority of residents are poor and unable to afford the added cost of the capital improvements. See Box 12 for an example of such a Housing Allowance program in Kazakhstan.

Box 12: Housing Allowances in Kazakhstan

Housing allowances are conceptually the best support instruments as they provide a boost in demand through enhancement of qualified households’ ability to pay. These are households facing excessive housing costs relative to their incomes. A monthly housing allowance lowers the effort ratio to the ‘supportable’ level adopted by the government – typically 25-30 percent in most countries. Housing allowances are portable so that households can relocate without losing them, which is more efficient than low-rent social housing that ‘locks in’ households in specific locations. This system, however, requires stable fiscal commitment and effective means-testing administration capable of collecting and updating relevant information on a household’s financial situation (both income and wealth), and on their housing parameters (to exclude high-standard dwellings). Well-designed housing allowances need to be portable across all types of rental accommodation, both market and non-market, and sometimes including also qualified homeownership.¹ Their use would also help to reduce informal renting, since informal renting contracts would not qualify for granting of housing allowances.

In Kazakhstan, any expense on housing and utilities beyond a certain percentage of the household income (10-30 percent depending on the “akimat” or local government) can be covered by a state-funded Housing Allowance program for eligible households. This provision is very good in terms of ensuring that the cost of renovation does not pose a disproportionately heavy burden on low-income households (and therefore encourages their participation). This applies particularly in the case of buildings with a large number of low-income households: with the Housing Allowance, it is easier to get the residents to agree to undertake the improvements, since much of the cost burden falls on the government. On the other hand, if a building mainly has residents who do not qualify for the Allowance for one reason or another, it may be harder to convince the owners because they would, in effect, have to bear all or a large part of the cost themselves. Other incentives – possibly in the form of subsidies – would thus need to be created for them to undertake improvements.

(ii) *Introduce a social housing program.* There is currently no social housing program in Azerbaijan (the IDP housing program is called social housing, but in fact, targets a specific group of people, is rent-free, is not income-targeted, and is allocated for an indefinite time period). While other housing programs target various non-IDP population segments, they are not targeted to low-income households. A social housing program could be a combination of (i) subsidized rentals in public housing and (ii) rental vouchers (subsidies) paid by the government for private rental housing. In terms of creating a public stock of social housing, it is important that the government mobilize and leverage the private sector to contribute to this pool. This can be done through the use of Public-Private Partnerships (PPPs) or through Development Agreements (DAs). PPPs could be entered into with private developers to develop new social housing under Build-Operate-Transfer (BOT) agreements. Under this arrangement, the local authority would provide the land and infrastructure, while the private sector would develop the housing, collect the rents, and maintain it for a fixed period (typically 30 years), where-after the ownership of the property passes to the local authority. Rents would be set at

levels sufficient to give a modest return on investment and subject to review procedures as set out in the BOT agreement. DAs can also be formed, requiring private developers to include a percentage of low-income housing in their developments as a condition for development, using instruments such as Inclusionary Zoning. Some of this may be used as social housing.

(iii) Consider reforming the IDP housing program. The housing program for IDPs is very important to the Government. Many IDP households have been accommodated in new housing built by the Government, but hundreds of thousands still remain in deplorable housing (in many cases, former dormitories, with 8-10 people in one room). While the resettlement into new Government-built housing may be one approach to address the IDPs' housing problem, it would be much more efficient and cost-effective to use a combination of options, such as rental vouchers in private housing. In addition, one issue with the current IDP housing program is that many of these large-scale projects are located at long distances from the city center. This limits the IDPs' ability to integrate with the rest of society.¹¹⁷ A more important limitation of the program, however, is that eligibility is based purely on the household's IDP status, rather than income level.¹¹⁸ The houses are owned by the government and cannot be sold or sublet by the beneficiaries. Households that have been allocated the new houses can in theory live there for life, as can their children and grandchildren, and all generations to come, "until they return to their homelands."¹¹⁹ These households are rent-free and all utilities are paid for by the government. It is common knowledge that second and third generation IDPs are increasingly economically well-off, and that some might not need this subsidy. On the contrary, many poor and even middle-income, non-IDP households in desperate need of housing assistance find that there is no social housing program to assist them. Therefore, it is recommended that the IDP housing program be reformed in a way that allocates social housing constructed for IDPs based on income criteria. This would essentially convert an exclusively IDP housing unit into a regular 'public social housing' unit, open to all applicants of social housing with eligibility determined largely by income level (i.e., regardless of IDP/non-IDP status).

(iv) Improve targeting of subsidized AMF loans. The loan products offered by the AMF are effectively a massive subsidy from the government to borrowers who are not necessarily low-income and could even afford other market-rate financial products. The terms of the AMF Social Loan need to be reformed to target those segments of the population that are creditworthy, but that do not have access to housing finance. In addition, the Standard Loan should be reformed to more closely resemble a market-based loan; this way, the AMF will better perform its role as a re-financing facility without competing with mortgage products offered by the market.

5. Strengthen and expand existing housing finance instruments

It is recommended that a Housing Microfinance Fund (HMF) be established which serves as a liquidity facility – a source of 7-10 year AZN loans for MFIs at a reasonable rate (i.e., 3-4 percent, comparable to the interest rate of the current AMF Social Loan). To be eligible for this financing from the HMF, the MFIs would need to be adequately licensed and regulated, and follow strict reporting requirements. There may be conditions attached to this financing, such as the purpose, tenure, and price of the loans made by the MFI to end-users.

Improving access to housing will also need to address access to mortgage finance. It appears that mortgage lending is still considered relatively risky in Azerbaijan; this is evident from the large down payments (40-50 percent) demanded by banks for mortgage loans, which they attribute to the "unstable" and "inflated" housing market. These high down payments together with the double-digit interest rate – which the banks

¹¹⁷ Stakeholders interviewed suggested that the current subsidy program serves political interests by improving IDPs' conditions in a tangible way (with new blocks of housing), while maintaining their physical and social identity until their anticipated return to the Nagorno Karabakh region and its environs.

¹¹⁸ As noted in section on social housing in Chapter 1, this phenomenon is common to all current 'social housing' programs; finished housing is allocated to segments of the population defined by national service or special categories, rather than based on financial need or income categories.

¹¹⁹ Interview with a high-level official in the State Committee for IDPs and Refugees.

blame on the high cost of funds and the shortage of AZN funds – make mortgage loans less attractive and less accessible to the vast majority of the population. There is a need to address the current shortage of long-term AZN funds for housing mortgage loans. Given the recent devaluation, mortgage issuance by commercial banks using their own funds has practically stopped. One possible approach during this period could be to restructure the AMF in a way that it serves as a real liquidity facility, pumping liquidity to the banks without distorting the market by offering loans at subsidized interest rates. More specifically, the terms of the AMF commercial loan might be adjusted to more closely resemble market-based loans in terms of the interest rate charged, restrictions on the loan size removed, etc. Once the market for these loans picks up with an adequate supply of AZN financing, the rates could become more competitive. This option might allow the AMF to better serve the market by filling an existing financing gap (of long-term AZN funds), rather than offering a product that effectively “competes” – while using an unfair advantage – with the banks’ internal loans. Also, the AMF funding for such commercial loans should be significantly increased to better reflect the scale of market demand. That said, this must be done with caution as flooding the market with finance could artificially inflate demand and increase prices. It is also recommended that the foreclosure laws and procedures be reviewed and reformed to make mortgage lending more efficient and perceived as less risky by the banks.

6. Facilitate the development of a robust rental market

Demand for residential rentals is bound to increase in the Greater Baku Region as urbanization pressures continue to push land and housing prices upward in expanding central cities and their core-urban and mid-urban locations, where homeownership rates tend to be lower than in suburban and peri-urban locations.¹²⁰

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There is a need to enable development of a vibrant rental segment in Azerbaijan, especially in Baku. Enabling the development of a vibrant rental housing market in Baku city is important for a number of reasons: i) it is a natural outlet for those households that lack sufficient income to afford a home or have not saved enough equity for mortgage down payment; ii) many households have only informal incomes that disqualify them from mortgage finance; and iii) fluid rental markets facilitate much-desired labor market mobility. Working far from home exacerbates commuting congestion and adds significant cost and travel time for the workforce. A vibrant formal rental housing market in the urban core can help mitigate these problems, and can even help to revitalize the city center.¹²² A vibrant rental segment needs to attain market equilibrium at higher volume (availability) and lower rents (affordability). Renting volume in Baku’s core-urban and mid-urban apartment dwellings should grow successively towards 20-40 percent as discussed in an earlier section.

Rental housing is a key component and determinant of a well-functioning housing market in Azerbaijan. While renting is not the panacea to solving the housing challenge, it does constitute a significant and vital housing tenure option that should be promoted alongside, and not in competition with, homeownership. This may be substantiated through adoption of an articulated housing policy and accompanying implementation strategy through programs aiming, *inter alia*, at provision of more public housing, more social housing, and market-based renting. The measures used in these programs should be regulatory improvements, means-tested subsidies, and direct provision of rental dwellings (public, social).

Improve the regulatory framework for landlord-tenant relations. Although a basic market-based framework for landlord-tenant relations is provided in the Civil Code (2000), it does not include regulations focused distinctly on residential tenancies including conflict resolution institutions. The key task remains effective enforcement of rental contracts by the judiciary system concerning residential tenancies. Written rental contracts should be encouraged and a broader list of clauses should be prescribed if possible to include ways

¹²⁰ In New York homeownership averages 34%; in Manhattan its is only 25%, but in Queens 45%. In Paris, homeownership averages 47%, but in central Paris 33%, while the rate is 60% in the ‘second ring.’

¹²¹ See World Bank (2014) for more details.

¹²² For more discussion on this see World Bank (2013).

of resolving conflicting claims and issues.¹²³ A distinct ‘residential tenancies law’ should be considered, building on the general provisions of the Civil Code (2000). Such a law should proactively cover potential disputes and conflicts by providing a binding regulatory framework including an expedient conflict resolution mechanism.

A system of procedures for conflict resolution is needed outside the court system, including mediation and arbitration institutions. Mediation is used to end a dispute prior to legal action by entering into a reconciliation process led by a third party who is trained and whose role is neutral. Arbitration is used to settle a dispute by means of an arbitral tribunal, an arbitrator, or a panel of arbitrators. Usually mediation is followed by arbitration. Some countries institutionalize this process through specialized ‘tribunals.’¹²⁴ Special attention is needed for an effective system of eviction of delinquent tenants, with expedient court orders and executing bailiffs.

Expand development of social rental housing with cost-recovery rents. Social rental housing typically addresses households that are ‘too poor’ for homeownership and ‘too rich’ for public housing. These are usually households in the second and third quintiles of household income distribution. They can generally afford moderate below-market rents, which requires rental landlords to relinquish profit motive and cover ‘only’ investment and operating costs. This has traditionally been done by creating budget-funded municipal housing stock rented at cost-recovery rental levels.¹²⁵ However, there are also programs for creating specialized cost-recovery housing associations that build and manage social rental buildings. They can be funded from a variety of sources, so that budgetary support can leverage a broader range of social rental dwelling projects. The key premise for their operations is that they cover operating and maintenance costs, which keeps them within the realm of the market-based housing sector.

In Austria, social rental housing is provided mostly by ‘cost-recovery’ housing associations registered as companies with Local Governments as partners, which contribute mainly land. Other partners can include charities, trade unions, and even private investors; these function as developers and later as operators. Typically, the funding spread is 5-20 percent land equity, 20-40 percent grants and soft loans, 0-15 percent tenant contribution (with buy-out option after 10 years), and finally commercial loans with government guarantees. Subsidies are conditioned in relation to construction costs and quality and the allocation to tenants (by means of testing criteria) is administered by Local Governments. Sub-renting is not allowed, while buy-out is allowed at pre-set prices.

Poland is one of the few countries in transition that has consistently supported the notion of fostering social housing within the framework of a market economy. The TBS program, highlighted in Box 13 below, was designed to strengthen the supply side of the rental market with moderate rent units.

Improve rental affordability for targeted means-tested households. If the Government intends to make rental housing more affordable at par with the international benchmark of an 25-30 percent effort ratio, rents will have to go down and/or household ability to pay will have to go up. Rents should go down with an expansion of supply, which will require (i) regulatory/tax incentives; (ii) subsidies reducing construction and/or operating costs; and (iii) direct provision of government-funded rental housing units. Homeowners’ ability to pay will go up if financial subsidies are targeted at households facing high effort ratios.

Supply-side Subsidies help reduce construction costs of rental buildings and/or reduce operating costs such as property management and building maintenance. These may be up-front grants and/or recurrent tax incentives.¹²⁶ The former are a direct, simple, and most transparent form of subsidizing the provision of new rental housing, as they reduce loan amounts.¹²⁷ Loan guarantees and tax breaks are long-term budgetary

¹²³ For example, which party is responsible for utility services, repairing the roof, insurance, etc., and to what degree.

¹²⁴ For example, Canada, USA, France, and Sweden.

¹²⁵ In some countries this has also been done by ‘rental’ cooperatives.

¹²⁶ Up-front grants have an immediate budgetary implication and are focused on fewer properties, whereas tax incentives can be spread over longer periods and have an impact on more (usually all) rental properties.

¹²⁷ This, in turn, allows lenders to reduce their lending risk.

commitments, but are often more manageable in terms of budgetary burden. In exchange for subsidies, landlords make social commitments in terms of below-market rents and income limits of their tenants for an agreed period of time.

Demand-side Subsidies enhance households' ability to pay – for example, housing allowances or vouchers. This is the most effective way to make rental housing affordable to lower-income households that do not have alternative access to low-rent public housing.¹²⁸ Such a means-tested system involves consistent fiscal commitment and requires collection and updating of information on beneficiary households, as well as adoption of a target effort ratio. It also requires recognition of assets owned by beneficiaries so that it avoids subsidizing 'income-poor' but 'asset-rich' tenants. Other parameters of housing allowance qualification are typically household and dwelling size (crowding impact), as well as the level of rent in order to avoid subsidizing renting in high-rent segments. Housing allowances need to quickly respond to changing parameters that disqualify or qualify households and adjust the level of housing allowance. Administrative effectiveness is a key factor. See Box 12 above on Housing Allowances.

Encourage small-scale landlords to legalize their activities. Small-scale landlords should be encouraged to legalize their activities. Little is known about this segment, i.e., how many have decided to 'come out' and what were their reasons for doing so, but informal renting continues to prevail. These landlords are taxed at 4 percent, which is a low tax that should encourage formal renting activity, so there are likely other reasons for staying hidden, which probably includes 'bureaucratic hassles' with reporting and tax filing as well as uncertainty regarding the process of legalizing renting activities. The landlord's lack of legalized ownership of the property, a frequent occurrence, makes this process even more complicated and discouraging 'tax registration' of such properties. A focused survey should be undertaken to understand the reasons underlying informal renting and to consider policy responses, including transition incentives containing temporary tax exemptions to the 'currently hidden' rental properties. This would encourage repair, renovation, and upgrading of these properties on the condition that they become 'tax registered.' There could also be additional tax incentives in the form of low-level flat income tax on rental income and better protection against eviction problems for individual landlords 'coming out' of the informal market. Poland uses such incentives in the form of a special law on 'occasional renting,' which encourages informal landlords to register their activities with tax authorities (see Box 14). Qualification and registration of renting activity under this law provides additional protection of individual landlords against unsuccessful or failed evictions that plague many landlords.¹²⁹ The law allows landlords to require tenants to indicate place to which they agree to be evicted upon becoming ordered (by court) to vacate premises.

¹²⁸ This segment may not be available due to lack of construction, or may have been decimated by micro-privatization to sitting tenants, as happened in Azerbaijan in the 1990s.

¹²⁹ In Poland, an eviction court order often requires that the evicted tenant has to be provided with an alternative dwelling by local government. Given that local governments lack such 'intervention' dwellings, there are thousands of eviction orders that cannot be executed. And some court orders are issued without placing the onus specifically on local governments, so that it is the landlord who has to provide alternative accommodation, which effectively defeats the purpose of pursuing an eviction order.

Box 13: TBS Social Housing Program in Poland

In Poland, a program to foster social housing development – called TBS – was introduced in 1995 and represents a unique and remarkable experience in ECA transition countries. The main operators are TBS companies; while mostly owned by municipalities, some are private and some have a public-private capital mix. Also, housing cooperatives were allowed to participate in the TBS program. In all cases, municipalities have the right to appoint members of the TBS supervisory boards. The National Housing Fund (KFM) provided subsidized, long-term investment loans to TBS and rental cooperatives. The funding of KFM relied excessively on budgetary grants, and thus was ended and new means are being sought to fund it. In exchange for favourable financing, the TBS companies were restricted in rent-setting: rents are to cover loan repayment and all operating and maintenance (O&M) and renovation expenditures. Together this should not exceed 4% of the replacement cost, which is an administrative location-specific benchmark published by the Government. They were also required to allocate rental TBS dwellings to qualified tenants so that social targeting would be retained.

TBS and cooperatives are required to provide at least 30% equity, with the KFM financing up to 70% of the project. The 30% ‘down-payment’ may derive from tenants selected through means-tested qualification procedures in order to target those households who are ‘too rich’ for public housing and ‘too poor’ for homeownership. The program facilitated construction of about 100,000 social rental dwellings till now. However, the goals of targeting the right households and promoting their residential mobility have not been uniformly achieved because of its implementation ambiguities.

Better results were achieved on the supply side as the Program created several hundred bankable TBS borrower companies skilled in both property development and management structures. These entities often manage substantial amounts of municipal housing. Efficient, multi-family rental building management and renovation solutions are rare in transition countries like Poland, so the existence of TBS operators helps preserve the country’s public residential capital stock, even if little new production is taking place in this sector at the moment.

Encourage suppliers of rental housing to expand their activities. Small-scale landlords constitute a pool of potential entrepreneurs who could consider expanding their rental business if provided incentives to do so. Those who own and rent multiple dwellings are the best ‘candidates.’ Their ‘scaled-up’ activities should be encouraged through fiscal incentives so that they are able to make deductions from gross rental incomes for the following cost categories: (i) capital depreciation allowance; (ii) deduction of operation and maintenance costs, including general overhaul costs; (iii) carry forward of rental losses into subsequent years; and (iv) offsetting of rental losses against other income. These incentives may be limited to certain rental levels (e.g., excluding the high-end segment) and dwelling standards (e.g., excluding large dwellings). Government could also consider providing small plots of public land through long-term leases with low ‘ground rents’ – for example 1 percent as in Poland¹³⁰ – on the condition of developing housing with below-market rents expressed as maximum percent of approved replacement cost, but still providing ‘reasonable profit’ to landlords.

There are large numbers of new vacant dwellings in Baku that are not part of the housing supply. They can be considered ‘wasted capital’ in terms of housing policy goals. One can consider creating incentives for dwelling owners to bring these units into the market by renting them backed with government guarantees in case of non-payment of rents. The City of Buenos Aires in Argentina offers such incentives for the first two years of rent operations by owners of vacant dwellings.

¹³⁰ Long-term ground leaseholds for residential purposes in Poland typically last 99 years, with ground rents set at 1% of market value of the land, which is *de facto* a subsidy.

Box 14: Law on Occasional Renting in Poland

The Law on Occasional Renting offers a number of advantages to individual landlords, who decide to report for income taxation their rental income from one or more properties. Contracts for occasional renting are time-limited and cannot run longer than 10 years. A key feature of an occasional renting contract is that upon its termination, regardless of the cause, landlords can remove ‘terminated’ tenants in a simplified, expedient way bypassing protracted court procedures for obtaining an eviction order. The contract has to be in writing and contain standard clauses, including one on security deposit (up to six times monthly rent). It has to abide by regulations in the Civil Code and Residential Tenancy Act to ensure that contractual provisions are in compliance. The occasional rental contract must have several annexes. The first annex, formally notarized for a nominal fee, is a formal statement by the tenant by which he/she agrees to execution and eviction. The second annex contains a legal address, provided by the tenant, to which he/she agrees to be evicted. If this address changes during the contract, the tenant has to inform the landlord of another address. The third annex contains an agreement by the owner of the dwelling to which the tenant agrees to be evicted. Upon termination of the occasional rental contract, the landlord has the right to demand possession of the dwelling within not less than 7 days. If the tenant does not vacate, the landlord can apply to the court for an execution order of the notarized annexes. Then court bailiff is then legally able to proceed with eviction.

The occasional renting contract is also not subject to some of the legal protections for tenants provided in the Residential Tenancy Act, such as, for example, rent increase limitations. However, some tenant protections still remains, for example, regarding termination notice.

The landlord can choose from two methods to be taxed for occasional rental income: a flat tax or by general income taxation. The flat tax on gross rental income is 8.5%. The general income tax rate is either 18% or 32%, together with other income, but allows the landlord to make deductions for various qualified expenses including capital repairs.

7. Improve housing data collection to inform housing policy and market actors, and allow international comparability

There is a need to develop statistical reporting on housing demand, supply, pricing, rental levels, and other trends for Azerbaijan. As previously mentioned, the lack of information on the housing sector and markets was one of the main barriers in the development of this diagnostic. Efforts to improve statistical reporting on housing could start by focusing on the largest urban areas, with more detailed locational focus by district in the Greater Baku Region. This is necessary to assess housing sector trends and monitor the implementation of housing programs and policies. The existing ‘immovable market indicators’ produced by the MBA Company for the Central Bank of Azerbaijan on Greater Baku area could serve as an example. Data collection on informal settlements’ growth and typologies can also be used to monitor its growth and for enforcement purposes.

8. Create a better environment for an efficient and transparent housing market

Reduce hidden costs and transaction costs. As reported consistently by all stakeholders interviewed for this study, the extremely high cost of housing in Azerbaijan is an outcome of several factors. Some stakeholders have reported that the “hidden costs” (20-30 percent of total price of house) and the VAT (21 percent of total price of house) are chief among these factors, especially for new housing. Of these two costs, the VAT can be adjusted more easily and quickly. It is recommended that VAT be completely eliminated for first-time home

buyers and significantly reduced for houses priced below a certain amount, for example, AZN 75K. This will help young starter households as well as middle-income households more easily afford market-based housing.

Address the problem of illegal buildings. The illegal status of newly-constructed multi-family buildings is a huge problem in Azerbaijan, particularly in Greater Baku. This is not only bad for the market in general, but also encourages corruption, whereby bribes are commonly paid at every step to get the required clearances or permits. These additional costs to the developer get passed on to the buyer, and have contributed extensively in making new housing unaffordable to the vast majority of the population. Illegality also means that the property cannot (in general) be used as collateral for a mortgage loan, which in effect means that the asset's leveraging capacity is being underutilized. The use of a Construction Contract as a proxy for a "title" means that secondary sales cannot be recorded, which distorts the understanding of real market trends. While this issue of illegality extends beyond the housing sector, it is one that needs to be addressed urgently – in terms of legalizing existing illegal buildings (which apart from the land title, conform to standards) and in terms of curbing future illegal construction.

9. Create clear policies targeted to absorb and prevent the growth of informal settlements

Informal settlements have grown exponentially in the Greater Baku Region over the last decade. It is estimated that around 20 percent of households in the Greater Baku Region do not have the required ownership documents for their housing structures and/or their land.¹³¹ A recent study, carried out for the Committee for Real Estate Registration Issues (2014), and funded by the World Bank, estimated at 51,453 the number of households living in protected areas¹³² mainly across Greater Baku.¹³³ Furthermore, an analysis of the establishment dates of a sub-sample (11,744) of these households revealed important growth from just 47 households in the 1920s and 321 in the 1970s to 4,518 households in 1990s and 6,116 after 2000.

In order to reduce the number of informal settlements, there is a need to put in place policies to prevent the formation of new informal settlements and absorb harmoniously existing ones. Preventing the growth of informal settlements needs to be preceded by a better understanding of the causes of informal housing growth. As observed throughout this diagnostic, there are important constraints in the housing market that are leaving a large portion of the population unable to afford or access formal housing. Despite having enough housing options available in terms of quantity, most available housing is targeted towards high-income households. In addition, even when households are able to secure legal tenure for land, the transaction costs for obtaining construction permits are cumbersome and high. Most of the recommendations provided herein (i.e., improve targeting of public funds for housing, expand housing finance instruments, enable the rental market, and create a better business environment) are by themselves important actions to prevent informal housing growth. In addition to these, cities in Azerbaijan need to review their current urban practices, construction standards, and more importantly, their practices for land recycling in city-centers and land-conversion in peri-urban areas.

Informal settlement absorption should take into consideration the diversity of informality and should, when possible, follow an integrated approach. Housing informality observed in Azerbaijan is diverse, including dense squatters in central areas; settlements in protected areas unsafe for humans; single-family houses in the periphery after agricultural land sub-divisions; and high-rise, multi-family buildings that were constructed without permits or are not registered. As a result, housing policies aimed at absorbing and integrating informal settlements into the urban fabric will require a diverse set of approaches. High-rise buildings, when following required building standards, can be regularized and integrated more easily and at

¹³¹ Source: World Bank, *Greater Baku Household Survey* (2014)

¹³² Protected areas consist of land around hazardous oil wells, railway lines, gas lines, sewerage lines, etc.

¹³³ Committee on Real Estate Registration Issues, "Policy Document on the Regulation of Informal Settlements in the Republic of Azerbaijan"

a lower cost. On the contrary, low-density informal settlements with poor access to services and disconnected from the rest of the city require a more integrated approach that looks both at social and basic service provision, tenure, and connection to the rest of the city. Informal settlements located in protected areas (e.g., near high-voltage electricity networks), which pose hazards for their inhabitants should be resettled. For the latter, livelihood impact assessments should be done to reduce and mitigate the negative impacts of resettlement. Social housing programs – outlined under Recommendation C – can be one of the options to house resettled households. These and more detailed recommendations and actions can be found in the recent “Strategy on regularization of illegal construction in the Republic of Azerbaijan” and accompanying Policy Document produced by the World Bank for the Committee on Real Estate Registration Issues (2014).

The table below presents key recommendations ranked by their level of priority, including a brief description of policy options.

Table 15: Housing Sector Reform Recommendations and Priorities

Desired Results	Recommendations	Priority
The Government has a well-defined National Housing Strategy/ Policy	Develop a clear housing policy and implementation strategy and improve housing data collection. The Institutional and Legislative Framework for the housing sector is strengthened.	High
Existing dilapidated housing stock is modernized and housing maintenance practices are in place	Improve existing housing management practices, and develop a program to provide State co-financing for capital repairs. Modernization Fund (HMF) are also recommended.	High
The extent of the informal housing market is reduced	Put in place policies to prevent the formation of informal settlements and absorb harmoniously existing ones. Formalizing existing informal or semi-formal dwellings will require a diversity of approaches such as: (i) regularization of “formal” type property, (ii) resettlement of household in protected areas, and (iii) integral upgrading of informal settlements in slum-like conditions. In parallel hidden and transaction costs linked to the development, construction, transfer of housing are reduced.	High
Existing public funds for housing are well targeted to those in need	Provision of housing assistance can be done through multiple instruments such as: (i) introduction of a cash transfer or housing allowance system, (ii) introducing a social housing program, (iii) review existing programs targeted at vulnerable groups, such as IDP and/or (iv) improving targeting of existing AMF subsidized loans.	Medium
Azerbaijan counts with a diversity of housing finance instruments that target different sectors of the population	Strengthen housing finance instruments by: (i) establishing a Housing MicroFinance Fund and (ii) Improving mortgage financing. The later could be achieved through the restructuring of the AMF (Standard loans).	Medium
There is a dynamic rental housing market	This can be achieved through a combination of actions such as: (i) the creation of tax incentives for small informal landlords to legalize their activities, and (ii) encouraging owners of vacant dwellings to put them on the rental market by increasing taxes on vacant property.	Low

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ANNEX 1: Household Survey Methodology

A. Survey Design

The household survey was designed to be representative of the Greater Baku Region and cover the spectrum of housing typologies – both formal and informal. The survey comprised a sample of 1,200 households spread over the 14 districts of the Greater Baku Region and included Internally Displaced Persons (IDPs) living in collective centers. The survey was conducted between July and August 2014 by Synergetics under the supervision of the World Bank.

The survey design and implementation piloted a number of innovations that allow for better data collection and quality control. The survey was conducted using computer tablets and each observation (household) was geo-referenced. The tablets allowed for skip patterns and response options to be implemented automatically, avoiding mistakes in data entering or survey implementation. It was also possible to reduce the time of survey implementation as there was no need for data entering. In addition, for the IDP sampling, the team prepared an Android application to draw random samples on-site from the listing provided by the administrators of IDP collective centers. Finally, geo-referencing the data allowed having spatial visualization of results.

A very well-defined sampling procedure was implemented to assure coverage of all the population (IDPs and non-IDPs) and for the survey to be representative for Greater Baku. Two independent sampling universes (for IDPs and non-IDPs) were taken into account and outlined in cooperation with the State Committee for Refuges and Internally Displaced Persons and the Statistics Department of Azerbaijan.

B. Sampling procedure

The sampling procedure was developed as follows;

- *Non IDP-households*: a total of 1,000 households + replacements were drawn from the non-IDP household sampling universe. The initial sampling frame was outlined in cooperation with the State Statistics Committee in the following way: first, a set of 100 enumeration areas from the Census Listing of the Greater Baku Region were selected with Probability Proportional to Size.¹³⁴ Once enumeration areas were identified, the survey firm identified the geographical borders of each area and proceeded to do a listing exercise, which identified all housing structures within the enumeration area. A sample of 10 households + 5 replacement households was selected randomly in each enumeration area.
- *IDP households*: as IDP families living in collective centers are not included in the Census Listing from the State Statistics Committee, the team needed to identify other sampling frames in order to be able to include this important population. The team worked with the State Committee for Refugees and Internally Displaced Persons and each district office to identify all collective centers in the Greater Baku Region. From this list, 40 collective centers were selected using Probability Proportional to Size. In each collective center, interviewers were provided with the list of households and using random selection software five households were sampled in each collective center for a total of 200 households. IDP households were apparently oversampled in relationship to non-IDP households, as they clearly do not represent 16 percent of the population living in Greater Baku. For this reason, the team has used probability weights to adjust results from IDP households and produce representative estimates for the full sample (IDP and non-IDP).

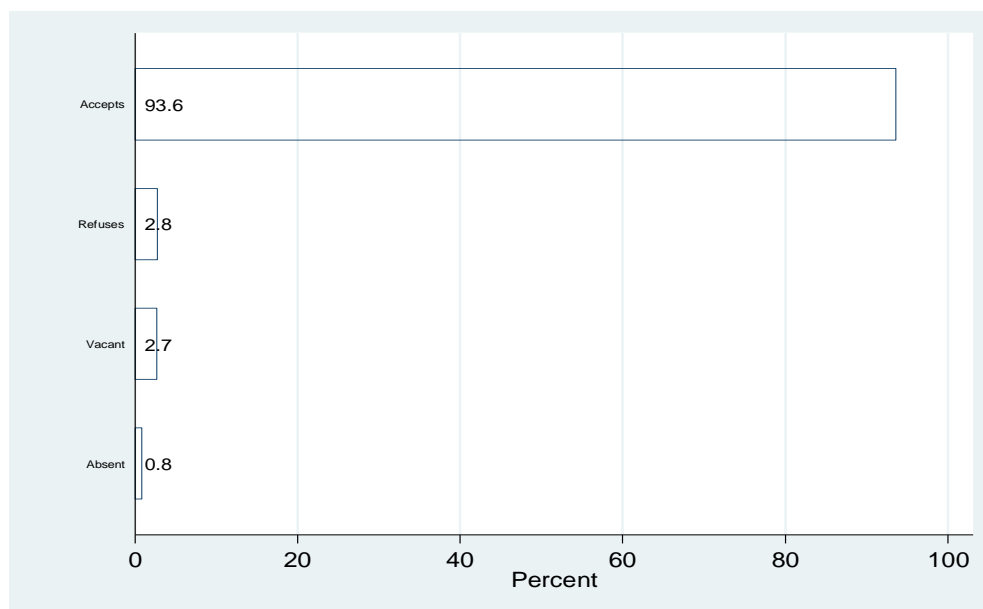
The sample was distributed across all fourteen districts. Districts with higher population densities, such as Yasamal, had a bigger sample size than those with lower densities.

¹³⁴ Under this selection method, the probability of selection is higher as the population in the enumeration area is higher. Although in principle all enumeration areas have around 100 households, in reality some are slightly bigger and others slightly smaller. Enumeration areas of greater density had higher probability of being selected for the survey.

C. Response rate

The response rate of the survey was very good with more than 93 percent of selected households participating in the survey. As expected, a higher response rate – 99 percent – was found for the IDP group. Households considered as being middle income represented the majority of non-respondents (See Figure 54 below). However as the survey did not collect income or wealth information from respondents, it is not possible to compare their distribution.

Figure 54: Survey participation rate



D. Survey instrument

The survey instrument was broadly discussed with sector stakeholders and designed to answer the following research questions;

- (i) What is the current state of the housing stock in Greater Baku? In particular, looking at housing type (house, apartment), housing quality (materials, reported damages in structures), condition of common areas in multi-family buildings and general characteristics of the stock (age, spatial distribution, size, inside amenities, etc.). This topic was covered mainly in *Module B* of the household survey.
- (ii) What is the current situation in terms of access to basic services and accessibility to essential amenities (i.e., schools, hospitals) and transport nodes (i.e., buses or metro stop)? Covered in *Module C* of the household survey.
- (iii) How mobile are households currently living in the Greater Baku Region? Covered in *Module D* of the household survey.
- (iv) What types of tenure are predominant in Greater Baku? In particular, looking at the different types of tenure for owners (informal, semi-formal, formal) and the existing rental markers (formal and informal). Covered in *Module E* of the household survey.
- (v) How do households obtain their dwellings and finance the purchase of their dwellings and recent housing improvements? Covered in *Module E* of the household survey.
- (vi) What are the predominant multi-family building management structures and how are they performing? Covered in *Module E* of the household survey.

Limitations: The survey instrument also intended to analyze how the current housing market was segmented and whether housing was affordable to the middle-income and low-income groups. However, modules linked to socio-economic characteristics of households were dropped upon request from the Ministry of Economy and Industry. For this reason it is not possible to respond to these questions.

E. Summary Results

Module B – Housing Structure

Year of construction and type of dwelling

Date in which dwelling was constructed	Baku	Eastern	Absheron	Sumgayit	Western	Greater Baku
Before 1940	10.86	7.19	5.97	0	0	13.7
Between 1940 and 1969	33.78	33.75	31.27	37.58	43.39	32.4
Between 1970 and 1989	47.77	32.48	35.6	60.18	34.71	42.9
Between 1990 and 1999	5.98	16.67	16.81	2.24	19.26	7.9
After 2000	1.6	9.9	10.35	0	2.63	3.2
Total	100.0	100.0	100.0	100.0	100.0	100.0

Type of dwelling	Baku	Eastern	Absheron	Sumgayit	Western	Greater Baku Region
SINGLE FAMILY HOUSE	11.8	35.9	55.8	0.5	13.2	16.7
APARTMENT	83.2	49.7	39.9	93.6	61.3	76.1
ROOM IN HOUSE/APARTMENT	0.4	3.3	0.0	0.5	22.1	1.5
COLLECTIVE CENTER	4.6	11.1	4.3	5.4	3.4	5.8
Total	100.0	100.0	100.0	100.0	100.0	100.0

Type of dwelling vs. year of construction	Before 1940	Between 1940 and 1969	Between 1970 and 1989	Between 1990 and 1999	After 2000	Total
HOUSE	26.82	28.83	20.89	11.87	11.6	100
APARTMENT / FLAT	4.82	36.92	50.42	6.07	1.77	100
ROOM IN A LARGER HOUS	0	18.22	67.37	14.41	0	100
COLLECTIVE CENTERS	4.36	22.1	48.61	24.93	0	100

Surface, rooms and overcrowding indicators

	Number of rooms	Surface (sq.mts)	Household size	PPS	People per room (PPR)	Percentage overcrowded (PPS)
BY DISTRICT	AVERAGE	AVERAGE	AVERAGE	AVERAGE	AVERAGE	PERCENTAGE
Nizami	2.1	45.6	3.8	14.2	1.9	57%
Yasamal	2.0	44.4	3.7	14.0	2.2	54%
Suraxani	2.9	68.5	4.6	17.2	1.9	54%
Khazar	2.8	67.5	4.1	16.8	1.7	51%
Sumgayit	2.4	46.5	4.0	13.0	1.9	49%
Sabunchu	2.7	67.4	4.1	17.6	1.8	47%
Absheron	2.8	62.3	4.4	16.6	1.7	42%
Garadagh	2.6	52.3	4.0	14.1	1.6	42%
Pirallahi	2.3	48.1	3.7	17.3	1.7	40%
Nasimi	2.6	50.4	3.7	15.5	1.5	38%
Sabail	2.9	62.3	4.2	18.4	1.6	36%
Binagadi	2.5	56.7	3.5	19.6	1.5	36%
Khatai	2.5	44.6	3.6	14.1	1.7	33%
Narimanov	2.8	66.0	3.7	22.3	1.5	32%
BY ZONES						
Baku	2.4	51.5	3.7	16.6	1.7	41%
Eastern suburbs	2.8	67.5	4.3	17.3	1.8	51%

	Number of rooms	Surface (sq.mts)	Household size	PPS	People per room (PPR)	Percentage overcrowded (PPS)
Absheron Sat. City	2.8	62.3	4.4	16.6	1.7	42%
Sumgayit Sat. City	2.4	46.5	4.0	13.0	1.9	49%
Western Suburbs	2.6	52.3	4.0	14.1	1.6	42%
BY IDP CATEGORY						
NON-IDP	2.6	56.0	3.8	17.0	1.6	40%
IDP	2.0	43.1	4.2	11.5	2.5	69%
BY YEAR BUILT						
before 1940	2.4	44.8	4.0	12.7	1.8	46%
1940-1969	2.4	51.9	3.8	15.7	1.8	47%
1970-1989	2.5	53.4	3.8	16.6	1.7	42%
1990-1999	3.2	75.7	4.4	20.3	1.6	35%
after 2000	3.0	77.8	4.1	20.8	1.7	42%
BY EMPLOYMENT STATUS OF HEAD						
FULL EMPLOYMENT (FULLDAY WORK)	2.6	55.3	3.9	15.5	1.7	42%
INCOMPLETE EMPL. (PART-TIME)	2.4	53.7	3.4	18.3	1.7	46%
UNEMPLOYED	2.2	46.0	3.9	14.0	2.1	52%
PENSIONER	2.4	51.6	3.7	18.3	1.7	43%
OTHER INACTIVE PEOPLE	3.0	72.3	4.4	18.0	1.6	43%
Greater Baku Region	2.5	54.2	3.9	16.2	1.7	44%
IDP in collective center	1.8	37.7	4.1	9.9	2.8	77%
BY DISTANCE TO CBD						
Less than 15minutes	2.9	68.1	4.0	19.9	1.5	37%
15-30minutes	2.5	54.2	3.7	17.6	1.7	40%
30-45minutes	2.5	54.9	4.0	15.3	1.8	47%
45-60minutes	2.5	53.1	3.9	15.3	1.9	47%
60-90minutes	2.5	47.5	3.9	13.3	1.7	46%
More than 90minutes	2.4	42.8	4.3	11.1	2.0	53%
BY TENURE TYPE						
Renter	2.0	42.6	3.4	14.9	1.9	54%
Owner	2.6	56.1	3.9	16.4	1.7	42%
BY PROOF OF OWNERSHIP DOCS.						
No document	1.8	37.3	4.2	9.8	2.9	76%
Registration card	2.4	56.6	4.2	15.5	2.0	57%
Contract builder*	3.0	75.0	4.0	18.8	1.3	0%
Notarized contract	2.5	27.2	3.8	12.1	1.5	39%
Homestead land title	3.8	103.1	4.5	24.5	1.3	25%
Real Estate Registry	2.6	56.8	3.8	17.1	1.6	38%

*Too few observations of households having contract with building were found in the same. Therefore statistical inference cannot be assured.

Housing quality and satisfaction

	Leak roof, walls, floors or ceiling	broken windows, frames or floor	visible cracks in floor or walls	lift not working	common areas dirty	common areas in dilapidated state	building façade in a bad state	housing quality index
BY DISTRICT	PERCENTAG	PERCENTAG	PERCENTAG	PERCENTAG	PERCENTAG	PERCENTAG	PERCENTAG	PERCENTAG
Absheron	13%	18%	26%	0%	36%	30%	34%	43%
Binagadi	6%	7%	13%	78%	17%	20%	53%	80%
Garadagh	13%	19%	33%		28%	28%	41%	57%
Khatai	27%	32%	22%	55%	57%	26%	25%	91%
Khazar	32%	44%	43%	100%	43%	43%	56%	55%
Narimanov	9%	7%	10%	61%	39%	27%	31%	58%

	Leak roof, walls, floors or ceiling	broken windows, frames or floor	visible cracks in floor or walls	lift not working	common areas dirty	common areas in dilapidate d state	building façade in a bad state	housing quality index
Nasimi	25%	10%	19%	100%	19%	12%	75%	82%
Nizami	20%	25%	23%	56%	28%	31%	36%	67%
Pirallahi	70%	80%	80%					80%
Sabail	14%	6%	13%	10%	27%	22%	44%	52%
Sabunchu	34%	21%	30%	11%	72%	61%	60%	53%
Sumgayit	29%	38%	20%	95%	50%	40%	45%	80%
Suraxani	36%	35%	30%	65%	31%	30%	35%	71%
Yasamal	35%	41%	48%	2%	33%	43%	45%	53%
BY ZONES								
Baku	20%	20%	21%	58%	35%	26%	40%	72%
Eastern suburbs	36%	33%	34%	60%	44%	40%	46%	62%
Absheron Sat. City	13%	18%	26%	0%	36%	30%	34%	43%
Sumgayit Sat. City	29%	38%	20%	95%	50%	40%	45%	80%
Western Suburbs	13%	19%	33%		28%	28%	41%	57%
BY IDP STATUS								
NO (Non-IDP)	17%	19%	18%	61%	33%	24%	35%	67%
YES (IDP)	59%	60%	60%	70%	72%	70%	80%	84%
BY YEAR BUILT								
before 1940	25%	24%	28%	87%	24%	16%	27%	64%
1940-1969	24%	28%	28%	39%	43%	36%	52%	68%
1970-1989	19%	23%	18%	66%	39%	30%	38%	78%
1990-1999	39%	32%	37%	44%	43%	37%	46%	59%
after 2000	18%	5%	10%	0%	0%	0%	0%	18%
BY EMPLOYMENT STATUS								
FULL EMPLOYMENT	15%	19%	18%	61%	35%	26%	36%	66%
INCOMPLETE EMPL. (PART-	32%	26%	32%	56%	35%	20%	44%	68%
UNEMPLOYED	40%	40%	37%	45%	58%	53%	65%	74%
PENSIONER	35%	35%	31%	66%	44%	39%	49%	79%
OTHER INACTIVE PEOPLE	28%	27%	30%	67%	27%	24%	43%	66%
Greater Baku Region	23%	25%	24%	61%	38%	30%	42%	69%
IDP in collective center	79%	80%	83%	39%	68%	75%	89%	96%
BY DISTANCE TO CBD								
Less than 15minutes	32%	25%	12%	28%	26%	23%	32%	47%
15-30minutes	19%	18%	22%	68%	29%	28%	46%	74%
30-45minutes	27%	25%	27%	67%	38%	30%	45%	74%
45-60minutes	25%	34%	22%	48%	65%	42%	42%	67%
60-90minutes	19%	29%	34%	85%	35%	26%	30%	72%
More than 90minutes	17%	27%	33%	73%	43%	27%	34%	64%
BY OWNERSHIP STATUS								
Renter	24%	27%	34%	86%	32%	38%	64%	82%
Owner	22%	23%	21%	61%	37%	28%	38%	68%
BY PROOF OF OWNERSHIP								
No document	71%	73%	73%	65%	70%	75%	87%	87%
Registration card	38%	34%	32%	22%	72%	57%	46%	72%
Contract builder*	0%	0%	0%					0%
Notarized contract	14%	28%	31%	0%	24%	0%	52%	56%
Homestead land title	14%	3%	13%					19%
Real Estate Registry	16%	18%	16%	61%	33%	22%	33%	67%

*Too few observations of households having contract with building were found in the same. Therefore statistical inference cannot be assured.

Level of satisfaction with housing

	Very satisfied	Satisfied	Neutral	Dissatisfied	Very dissatisfied
BY DISTRICT	PERCENTAGE	PERCENTAGE	PERCENTAGE	PERCENTAGE	PERCENTAGE
Absheron	0.0	56.4	28.4	13.5	1.7
Binagadi	3.0	62.0	11.9	22.2	0.9
Garadagh	0.0	73.3	14.2	12.5	0.0
Khatai	4.7	34.3	30.4	20.1	10.5
Khazar	0.0	34.5	32.4	19.9	13.3
Narimanov	14.8	48.0	15.6	20.6	0.9
Nasimi	4.9	75.1	15.5	4.3	0.3
Nizami	2.4	46.3	16.6	19.2	15.6
Pirallahi	0.0	10.0	20.0	70.0	0.0
Sabail	9.7	73.3	11.7	5.4	0.0
Sabunchu	0.5	40.0	19.1	27.2	13.3
Sumgayit	5.8	47.7	27.9	14.4	4.2
Suraxani	8.4	50.6	7.7	12.0	21.3
Yasamal	8.9	35.4	18.5	19.9	17.2
BY IDP STATUS					
NO (Non-IDP)	6.2	53.6	21.4	16.7	2.2
YES (IDP)	1.0	23.0	7.8	21.3	46.9
BY YEAR BUILT					
before 1940	7.7	50.4	20.1	13.7	8.1
1940-1969	1.9	47.6	21.5	22.5	6.5
1970-1989	5.4	48.4	20.7	16.7	8.7
1990-1999	8.1	53.9	9.4	10.6	18.1
after 2000	24.5	60.1	10.2	5.2	0.0
BY EMPLOYMENT STATUS OF HEAD					
FULL EMPLOYMENT (FULLDAY WORK)	5.4	56.0	19.4	15.3	4.0
INCOMPLETE EMPL. (PART-TIME)	5.4	45.3	31.7	12.3	5.3
UNEMPLOYED	3.2	22.9	23.0	20.3	30.6
PENSIONER	5.5	41.9	17.3	24.0	11.3
OTHER INACTIVE PEOPLE	10.7	50.7	9.9	12.1	16.6
Greater Baku Region	5.4	49.2	19.7	17.3	8.4
IDP in collective center	0.0	2.7	4.8	22.6	69.9
BY DISTANCE TO CBD					
Less than 15minutes	18.1	56.7	11.5	11.4	2.3
15-30minutes	5.2	56.6	15.7	17.1	5.4
30-45minutes	3.7	49.4	19.5	12.3	15.1
45-60minutes	3.5	33.7	25.8	27.8	9.1
60-90minutes	3.7	48.7	24.4	14.7	8.6
More than 90minutes	1.2	45.6	31.3	10.3	11.7
BY TENURE TYPE					
Renter	1.2	47.9	15.3	29.4	6.2
Owner	6.0	51.0	19.8	15.8	7.4
BY PROOF OF OWNERSHIP DOCUMENTS					
No document	0.0	9.9	9.3	18.5	62.2
Registration card	2.0	30.3	24.2	30.5	13.0
Contract builder*	0.0	0.0	0.0	100.0	0.0
Notarized contract	0.0	22.7	47.0	30.3	0.0
Homestead land title	10.1	68.5	8.9	12.5	0.0
Real Estate Registry	6.8	55.9	21.0	14.7	1.7

*Too few observations of households having contract with building were found in the same. Therefore statistical inference cannot be assured.

Module C – Access and quality of services

Access to services

	Piped water (individual)	Electricity	Piped gas	Sewer	Toilet (individual)	Heating	Solid Waste collected regularly
BY DISTRICT	PERCENTAGE	PERCENTAGE	PERCENTAGE	PERCENTAGE	PERCENTAGE	PERCENTAGE	PERCENTAGE
Absheron	100%	100%	100%	94%	88%	30%	67%
Binagadi	97%	100%	96%	100%	92%	59%	100%
Garadagh	100%	100%	97%	100%	63%	0%	69%
Khatai	99%	100%	98%	99%	88%	30%	61%
Khazar	50%	96%	74%	65%	54%	45%	57%
Narimanov	98%	100%	91%	99%	92%	46%	84%
Nasimi	100%	100%	100%	100%	91%	10%	97%
Nizami	84%	100%	82%	93%	86%	51%	69%
Pirallahi	100%	100%	100%	90%	10%	0%	30%
Sabail	100%	100%	100%	98%	81%	56%	96%
Sabunchu	91%	100%	95%	88%	60%	24%	83%
Sumgayit	96%	100%	100%	100%	95%	7%	93%
Suraxani	84%	100%	94%	77%	84%	46%	58%
Yasamal	99%	100%	96%	99%	79%	44%	84%
BY ZONE							
Baku	96%	100%	94%	98%	87%	43%	81%
Eastern suburbs	80%	99%	91%	79%	69%	38%	65%
Absheron Sat. City	100%	100%	100%	94%	88%	30%	67%
Sumgayit Sat. City	96%	100%	100%	100%	95%	7%	93%
Western Suburbs	100%	100%	97%	100%	63%	0%	69%
BY IDP STATUS							
NO (Non-IDP)	97%	100%	97%	96%	89%	39%	83%
YES (IDP)	75%	100%	78%	85%	54%	15%	54%
BY YEAR BUILT							
before 1940	93%	99%	98%	92%	73%	25%	83%
1940-1969	94%	100%	96%	97%	85%	30%	81%
1970-1989	94%	100%	93%	96%	86%	40%	77%
1990-1999	96%	100%	95%	93%	89%	49%	67%
after 2000	83%	100%	75%	72%	87%	60%	80%
BY TYPE OF DWELLING							
HOUSE	91%	99%	98%	84%	48%	34%	68%
APARTMENT / FLAT	98%	100%	97%	99%	97%	39%	85%
HOUSE/APARTMENT OR DORM	59%	100%	81%	67%	21%	0%	62%
COLLECTIVE CENTERS	48%	100%	54%	80%	43%	2%	35%
BY EMPLOYMENT STATUS OF							
FULL EMPLOYMENT (FULLDAY	97%	100%	97%	97%	89%	37%	82%
INCOMPLETE EMPL. (PART-TIME)	96%	100%	97%	96%	85%	32%	84%
UNEMPLOYED	76%	99%	82%	79%	58%	24%	47%
PENSIONER	91%	100%	93%	94%	83%	33%	83%
OTHER INACTIVE PEOPLE	87%	100%	92%	90%	81%	62%	67%
Greater Baku Region	93%	100%	94%	95%	84%	36%	79%
IDP in collective center	53%	100%	57%	77%	47%	2%	34%
DISTANCE TO CBD							
Less than 15minutes	99%	100%	99%	94%	97%	35%	90%
15-30minutes	97%	100%	95%	99%	89%	46%	89%
30-45minutes	88%	100%	87%	94%	82%	38%	72%
45-60minutes	91%	100%	95%	90%	77%	32%	66%

	Piped water (individual)	Electricity	Piped gas	Sewer	Toilet (individual)	Heating	Solid Waste collected regularly
60-90minutes	91%	99%	98%	89%	75%	12%	78%
More than 90minutes	94%	100%	97%	94%	85%	9%	59%
BY TYPE OF TENURE							
Renter	93%	100%	94%	97%	85%	27%	88%
Owner	94%	100%	95%	94%	85%	37%	78%
BY PROOF OF OWNERSHIP DOCS							
No ownership documents	70%	100%	74%	80%	53%	13%	35%
Registration card	87%	100%	91%	91%	54%	21%	71%
Contract builder*	100%	100%	0%	100%	100%	0%	0%
Notarized contract	100%	100%	100%	97%	74%	35%	66%
Homestead land title	60%	100%	93%	39%	66%	37%	74%
Real Estate Registry documents	98%	100%	97%	98%	91%	41%	84%

*Too few observations of households having contract with building were found in the same. Therefore statistical inference cannot be assured.

Quality of services

	Piped Water			Electricity			Solid Waste Collection		
	Good	Average	Bad	Good	Average	Bad	Good	Average	Bad
BY DISTRICT	%	%	%	%	%	%	%	%	%
Absheron	59.6	15.3	25.1	91.0	9.1	0.0	61.8	15.0	23.2
Binagadi	79.2	16.7	4.2	89.8	10.2	0.0	86.5	13.5	0.0
Garadagh	50.4	27.4	22.3	92.6	7.5	0.0	68.9	1.3	29.8
Khatai	29.3	42.4	28.3	73.0	26.1	0.9	35.2	22.6	42.3
Khazar	1.9	15.1	83.0	69.9	23.2	7.0	4.2	66.1	29.8
Narimanov	54.1	20.8	25.1	95.2	4.9	0.0	80.2	6.0	13.8
Nasimi	81.5	13.9	4.6	100.0	0.0	0.0	94.3	5.0	0.8
Nizami	44.4	29.9	25.7	83.1	14.4	2.6	63.7	13.5	22.8
Pirallahi	10.0	0.0	90.0	10.0	90.0	0.0	10.0	40.0	50.0
Sabail	27.6	20.1	52.3	96.9	3.2	0.0	79.8	20.2	0.0
Sabunchu	36.0	19.5	44.5	92.1	7.6	0.3	72.1	15.5	12.4
Sumgayit	56.1	23.8	20.1	98.0	2.1	0.0	76.6	18.7	4.7
Suraxani	36.2	23.1	40.7	78.4	11.1	10.5	47.6	20.6	31.8
Yasamal	72.7	11.1	16.3	93.3	5.3	1.3	70.3	16.8	12.9
BY ZONES									
Baku	53.3	24.7	21.9	87.5	11.7	0.8	68.0	14.8	17.2
Eastern suburbs	28.8	19.8	51.4	79.5	14.3	6.3	46.1	28.3	25.6
Absheron Sat. City	59.6	15.3	25.1	91.0	9.1	0.0	61.8	15.0	23.2
Sumgayit Sat. City	56.1	23.8	20.1	98.0	2.1	0.0	76.6	18.7	4.7
Western Suburbs	50.4	27.4	22.3	92.6	7.5	0.0	68.9	1.3	29.8
BY IDP STATUS									
NO (Non-IDP)	52.3	22.7	25.0	91.3	8.2	0.5	68.6	17.4	14.0
YES (IDP)	32.5	26.8	40.7	65.4	25.7	8.9	42.2	17.6	40.2
BY YEAR BUILT									
before 1940	49.1	18.0	32.9	87.5	11.7	0.8	58.2	30.2	11.6
1940-1969	49.3	23.2	27.6	88.8	10.5	0.7	71.2	14.8	14.0
1970-1989	50.4	27.3	22.3	87.3	10.6	2.1	63.3	15.7	21.1
1990-1999	42.1	17.9	40.1	80.9	14.5	4.7	59.2	12.7	28.1
after 2000	58.8	10.4	30.8	96.0	3.4	0.6	64.2	23.0	12.8
BY TYPE OF DWELLING									
HOUSE	57.1	11.3	31.6	88.2	11.2	0.6	52.5	24.6	22.9
APARTMENT / FLAT	50.3	25.0	24.8	91.0	8.6	0.4	70.5	16.4	13.1
HOUSE/APARTMENT OR DORM	44.3	12.1	43.6	63.1	4.0	32.9	57.5	7.2	35.3
COLLECTIVE CENTERS	18.0	40.8	41.2	47.9	39.5	12.7	29.0	11.9	59.1

	Piped Water			Electricity			Solid Waste Collection		
	Good	Average	Bad	Good	Average	Bad	Good	Average	Bad
BY EMPLOYMENT STATUS									
FULL EMPLOYMENT (FULLDAY	54.3	22.0	23.7	90.2	9.2	0.6	68.8	18.1	13.0
INCOMPLETE EMPL. (PART-TIME)	46.9	25.1	28.1	91.2	6.8	2.0	57.8	30.5	11.7
UNEMPLOYED	30.7	24.2	45.1	72.4	18.0	9.7	34.2	14.9	50.9
PENSIONER	47.2	25.8	27.0	88.6	9.8	1.6	71.0	12.2	16.7
OTHER INACTIVE PEOPLE	35.3	28.7	36.0	69.5	30.1	0.5	54.0	17.6	28.5
Greater Baku Region	49.5	23.4	27.1	87.6	10.8	1.6	64.9	17.4	17.8
IDP in collective center	15.9	41.0	43.1	44.8	41.1	14.1	27.0	12.9	60.2
BY DISTANCE TO CBD									
Less than 15minutes	55.3	19.4	25.3	98.4	1.6	0.0	79.5	14.2	6.3
15-30minutes	62.7	20.3	17.0	93.4	6.2	0.4	77.9	14.1	8.0
30-45minutes	45.7	28.0	26.3	81.8	15.0	3.2	61.2	17.2	21.6
45-60minutes	25.0	30.3	44.7	78.7	19.0	2.3	46.1	20.5	33.4
60-90minutes	44.2	24.0	31.8	83.8	14.3	1.9	55.3	29.7	15.1
More than 90minutes	66.9	5.8	27.3	90.2	4.9	5.0	50.7	14.1	35.2
BY TYPE OF TENURE									
Renter	57.3	19.3	23.4	96.0	3.6	0.5	86.4	7.2	6.4
Owner	49.8	23.2	27.0	87.3	11.2	1.5	63.5	18.2	18.3
BY PROOF OF OWNERSHIP DOCS									
No document	29.0	24.8	46.3	56.1	29.1	14.8	28.8	11.3	59.9
Registration card	42.7	21.0	36.2	82.9	17.2	0.0	58.1	25.5	16.4
Contract builder*	0.0	0.0	100.0	100.0	0.0	0.0	0.0	0.0	100.0
Notarized contract	14.1	49.6	36.3	78.6	21.4	0.0	58.6	18.4	23.1
Homestead land title	41.4	8.5	50.1	100.0	0.0	0.0	39.1	53.4	7.5
Real Estate Registry	52.4	23.9	23.8	90.9	8.8	0.3	68.2	17.9	13.9

*Too few observations of households having contract with building were found in the same. Therefore statistical inference cannot be assured.

Accessibility and neighborhood characteristics

	Secondary school < 15 minutes	Bus stop < 15 minutes	Hospital < 15 minutes	Paved road	Safe walk outside Women & Children)	Streets well lit	Sufficient public spaces
BY DISTRICT	PERCENTAGE	PERCENTAGE	PERCENTAGE	PERCENTAGE	PERCENTAGE	PERCENTAGE	PERCENTAGE
Absheron	66%	93%	40%	23%	85%	60%	65%
Binagadi	70%	100%	73%	55%	93%	85%	88%
Garadagh	100%	49%	61%	71%	100%	69%	66%
Khatai	95%	100%	37%	54%	87%	62%	25%
Khazar	55%	95%	36%	38%	91%	17%	31%
Narimanov	97%	91%	65%	67%	95%	86%	79%
Nasimi	81%	100%	28%	47%	93%	98%	92%
Nizami	98%	97%	19%	46%	69%	39%	42%
Pirallahi	0%	100%	0%	0%	70%	0%	40%
Sabail	28%	100%	20%	24%	95%	23%	89%
Sabunchu	93%	98%	24%	49%	79%	26%	37%
Sumgayit	90%	99%	33%	57%	87%	72%	68%
Suraxani	68%	92%	23%	26%	65%	27%	16%
Yasamal	93%	100%	42%	58%	81%	71%	82%
BY ZONES							
Western Suburbs	84%	98%	42%	52%	86%	66%	64%
Baku	72%	95%	25%	35%	75%	24%	26%
Absheron Sat. City	66%	93%	40%	23%	85%	60%	65%

	Secondary school < 15 minutes	Bus stop < 15 minutes	Hospital < 15 minutes	Paved road	Safe walk outside Women & Children)	Streets well lit	Sufficient public spaces
Sumgayit Sat. City	90%	99%	33%	57%	87%	72%	68%
Eastern suburbs	100%	49%	61%	71%	100%	69%	66%
BY IDP STATUS							
NO (Non-IDP)	83%	96%	38%	52%	89%	62%	62%
YES (IDP)	79%	94%	34%	25%	60%	40%	36%
BY YEAR BUILT							
before 1940	79%	99%	38%	51%	86%	61%	71%
1940-1969	82%	96%	34%	49%	85%	60%	64%
1970-1989	88%	96%	43%	51%	86%	62%	50%
1990-1999	66%	96%	31%	32%	72%	39%	55%
after 2000	69%	87%	29%	50%	91%	44%	45%
BY TYPE OF DWELLING							
HOUSE	63%	90%	23%	15%	83%	23%	43%
APARTMENT / FLAT	87%	98%	43%	59%	89%	70%	64%
HOUSE/APARTMENT OR DORM	77%	78%	13%	44%	63%	54%	50%
COLLECTIVE CENTERS	83%	95%	25%	15%	37%	20%	20%
BY EMPLOYMENT STATUS							
FULL EMPLOYMENT (FULLDAY)	83%	96%	38%	55%	90%	66%	66%
INCOMPLETE EMPL. (PART-TIME)	77%	97%	34%	40%	90%	56%	46%
UNEMPLOYED	79%	91%	31%	18%	66%	35%	31%
PENSIONER	81%	98%	43%	44%	80%	52%	53%
OTHER INACTIVE PEOPLE	92%	98%	34%	58%	67%	47%	42%
Greater Baku Region	83%	96%	38%	49%	85%	59%	58%
IDP in collective center	81%	95%	23%	14%	36%	17%	17%
BY DISTANCE TO CBD							
Less than 15minutes	74%	98%	43%	48%	86%	73%	72%
15-30minutes	80%	100%	46%	52%	89%	70%	76%
30-45minutes	83%	91%	33%	45%	72%	53%	39%
45-60minutes	91%	96%	33%	43%	85%	38%	42%
60-90minutes	80%	98%	23%	49%	90%	59%	57%
More than 90minutes	83%	83%	30%	61%	89%	54%	43%
BY TYPE OF TENURE							
Renter	80%	100%	39%	42%	86%	69%	72%
Owner	83%	96%	39%	50%	85%	59%	57%
BY PROOF OF OWNERSHIP DOCS							
No ownership documents	87%	92%	33%	29%	50%	40%	35%
Registration card	67%	96%	27%	38%	85%	47%	36%
Contract builder*	0%	100%	0%	0%	100%	0%	0%
Notarized contract	72%	100%	19%	37%	89%	35%	75%
Homestead land title	61%	86%	11%	0%	96%	4%	3%
Real Estate Registry documents	84%	96%	40%	54%	89%	63%	62%

*Too few observations of households having contract with building were found in the same. Therefore statistical inference cannot be assured.

Module E – Tenure and Housing Finance

Tenure types and documents to proof ownership

	Owner (percentage)	Renters	Among those declaring themselves owners: Available documents to proof ownership					
			No documents	Registration card	Contract with builder*	Notarized contract	Homestead land title	Extract from Real Estate Registry
BY DISTRICT								
Absheron	99.56	0.44	8.97	7.64	0.00	0.00	3.84	79.55
Binagadi	87.92	12.08	1.34	1.54	0.00	1.13	0.67	95.33
Garadagh	96.56	3.44	0.00	22.91	0.00	0.00	0.00	77.09
Khatai	97.23	2.77	13.06	5.92	0.00	0.17	0.00	80.84
Khazar	99.45	0.55	4.67	12.81	0.00	0.00	0.00	82.53
Narimanov	86.31	13.69	0.00	3.46	0.00	0.00	0.00	96.54
Nasimi	74.39	25.61	5.20	3.00	0.00	0.00	0.00	91.80
Nizami	89.89	10.11	16.35	4.87	0.00	2.04	3.64	73.10
Pirallahi	100.00	0.00	10.00	0.00	0.00	0.00	0.00	90.00
Sabail	95.42	4.58	1.25	5.92	0.00	4.32	0.00	88.51
Sabunchu	86.50	13.50	9.36	18.48	0.32	1.89	0.00	69.94
Sumgayit	90.65	9.35	2.17	6.88	0.00	0.00	0.00	90.94
Suraxani	95.90	4.10	28.51	4.21	0.00	0.00	11.73	55.56
Yasamal	95.17	4.83	25.58	7.36	0.00	2.93	0.00	64.13
BY ZONE								
Baku	90.47	9.53	10.22	4.73	0.00	1.36	0.73	82.95
Eastern suburbs	93.83	6.17	17.29	10.20	0.10	0.57	5.44	66.40
Absheron Sat. City	99.56	0.44	8.97	7.64	0.00	0.00	3.84	79.55
Sumgayit Sat. City	90.65	9.35	2.17	6.88	0.00	0.00	0.00	90.94
Western Suburbs	96.56	3.44	0.00	22.91	0.00	0.00	0.00	77.09
BY IDP STATUS								
NO (Non-IDP)	91.94	8.06	1.98	6.01	0.02	0.91	1.75	89.34
YES (IDP)	89.14	10.86	60.68	10.46	0.00	1.26	0.93	26.69
BY YEAR BUILT								
before 1940	96.62	3.38	6.42	4.96	0.00	1.79	0.74	86.10
1940-1969	86.76	13.24	9.34	7.22	0.06	1.56	0.85	80.97
1970-1989	93.21	6.79	9.33	6.66	0.00	0.49	0.38	83.14
1990-1999	94.98	5.02	26.95	5.02	0.00	0.00	1.92	66.11
after 2000	89.37	10.63	5.42	11.76	0.00	0.00	30.79	52.02
BY TYPE OF DWELLING								
HOUSE	95.99	4.01	4.06	12.75	0.10	2.86	9.37	70.85
APARTMENT / FLAT	91.31	8.69	5.67	3.83	0.00	0.60	0.00	89.89
HOUSE/APARTMENT OR	84.54	15.46	44.40	55.09	0.00	0.00	0.00	0.50
COLLECTIVE CENTERS	80.80	19.20	83.23	12.86	0.00	0.00	0.00	3.91
Employment status of Head								
FULL EMPLOYMENT (FULLDAY	91.47	8.53	6.98	5.11	0.03	0.70	1.20	85.98
INCOMPLETE EMPL. (PART-	73.79	26.21	7.08	7.61	0.00	5.57	3.79	75.94
UNEMPLOYED	93.02	6.98	31.75	8.80	0.00	0.00	5.23	54.22
PENSIONER	96.57	3.43	8.48	10.14	0.00	1.13	0.84	79.41
OTHER INACTIVE PEOPLE	93.74	6.26	21.01	4.35	0.00	0.00	1.62	73.02
Greater Baku Region	91.62	8.38	10.23	6.61	0.02	0.95	1.63	80.56
IDP in collective center	82.47	17.53	87.04	12.96	0.00	0.00	0.00	0.00
BY DISTANCE TO CBD								
Less than 15minutes	93.70	6.30	2.55	5.56	0.00	0.00	4.30	87.59

	Owner (percentage)	Renters	Among those declaring themselves owners: Available documents to proof ownership					
			No documents	Registration card	Contract with builder*	Notarized contract	Homestead land title	Extract from Real Estate Registry
15-30minutes	87.10	12.90	7.74	2.92	0.00	1.51	1.12	86.71
30-45minutes	94.64	5.36	19.02	5.63	0.00	0.64	0.32	74.40
45-60minutes	93.70	6.30	12.60	10.92	0.00	1.39	3.29	71.80
60-90minutes	95.64	4.36	3.36	15.91	0.00	0.00	0.35	80.39
More than 90minutes	94.28	5.72	9.23	3.27	0.36	0.00	0.63	86.50
BY AGE OF HEAD OF HHD.								
16-25 years	79.28	20.72	9.63	2.17	0.00	0.00	0.00	88.20
26-35 years	70.98	29.02	7.62	2.91	0.00	0.00	1.38	88.09
35-54 yrs	91.63	8.37	11.55	7.38	0.00	0.89	2.92	77.27
55-65 yrs	96.14	3.86	11.29	6.00	0.05	1.64	0.71	80.31
65+ yrs	98	2.00	6.66	8.36	0.00	0.33	0.76	83.89
BY YEARS SINCE LIVING IN GB								
Less than 10 years	73.8	26.20	5.96	4.54	0.00	1.03	4.56	83.91
11-20 yrs	97.76	2.24	8.69	3.04	0.00	1.08	0.58	86.61
21-40 yrs	97.41	2.59	15.14	9.10	0.04	0.55	0.86	74.31
40+ yrs	100	0.00	2.63	9.96	0.00	2.13	1.70	83.58

*Too few observations of households having contract with building were found in the same. Therefore statistical inference cannot be assured.

BY PEOPLE APPEARING IN DOCUMENT PROOF OF OWNERSHIP	Registration card	Homestead land title	Extract from Real Estate Registry
Head of Household	98.13	95.97	96.96
Spouse	1.6		2.17
Head of Household and spouse	0.03	2.18	0.03
Other	0.24	1.85	0.83

Housing financing (Purchase, construction and improvements)

	No documents	Registration card	Contract with builder*	Notarized contract	Homestead land title	Extract from Real Estate Registry
Form used to obtain dwelling – All owners included						
Privatized	8.0	8.2	0.0	14.7	4.7	74.4
Purchased without mortgage	1.3	4.0	0.0	29.3	66.7	10.0
Cooperative	0.0	4.3	0.0	0.0	0.0	1.2
Inherited/Gift	5.9	48.5	0.0	56.0	28.7	13.9
Other	1.7	7.1	0.0	0.0	0.0	0.5
Occupied	67.8	15.2	0.0	0.0	0.0	0.0
Provided by state/company	15.4	12.8	100.0	0.0	0.0	0.2
Mortgage	0.0	0.0	0.0	0.0	0.0	0.0
Sources used to purchase dwelling – only those who purchased without mortgage						
EXCHANGED FOR ANOTHER	0.0	0.0	0.0	0.0	4.2	3.6
GIFT FROM FAMILY/FRIENDS	0.0	0.0	0.0	0.0	4.1	3.4
If the respondent did not want to	0.0	0.0	0.0	0.0	0.9	0.8
MICROCREDITS	0.0	0.0	0.0	7.1	0.0	0.7
OWN SAVINGS	100.0	87.0	74.1	81.2	66.6	69.1
SAVINGS+EXCHANGED	0.0	0.0	0.0	0.0	1.4	1.2
SAVINGS+GIFT FAM/FRIENDS	0.0	13.0	0.0	0.0	6.7	6.0
SAVINGS+LOANS FAM/FRIENDS+ GIFT	0.0	0.0	0.0	4.5	6.9	6.2
SAVINGS+LOANS FAMILY/FRIENDS	0.0	0.0	25.9	0.0	4.7	4.7
SAVINGS+MICROCREDITS	0.0	0.0	0.0	7.1	4.1	4.1

	No documents	Registration card	Contract with builder*	Notarized contract	Homestead land title	Extract from Real Estate Registry
Household constructed the house – All owners included						
NO	97.2	91.6		96.8	28.2	95.8
YES	2.9	8.4		3.2	71.8	4.2
Household obtained construction permit – All those who constructed						
NO	60.9	56.0		0.0	4.2	5.1
YES	39.1	44.0		100.0	95.8	95.0
Time construction of house						
Mean years - all constructed	3.4	1.6			2.0	2.0
Mean years - permit not obtained	3.1	1.7			1.0	2.7
Mean years - permit obtained	4.0	1.5		2.0	2.1	1.5

*Too few observations of households having contract with building were found in the same. Therefore statistical inference cannot be assured.

	No documents	Registration card	Contract with builder*	Notarized contract	Homestead land title	Extract from Real Estate Registry	All owners
Made improvements to the housing in the last 12 months							
YES	6.1	9.9	0.0	7.6	43.0	13.2	12.7
Type of improvements							
Added an extra room, floor to the	0.0	0.0	0.0		0.0	1.2	1.0
Major improvements (repair walls,	24.7	31.0	0.0		9.3	19.7	19.7
Minor improvements (painting	75.3	69.0	0.0		83.7	76.7	76.3
Major and minor improvements	0	0	100		7.07	2.36	3.0
Type of financing used for improvements							
GIFT FROM FAMILY/FRIEND	0.0	0.0	0.0		0.0	1.0	0.9
Does not want to respond	18.4	0.0	0.0		0.0	0.0	0.9
LOANS	0.0	0.0	0.0		9.3	0.0	0.5
LOANS FROM FAMILY/ FRIEND	0.0	0.0	0.0		0.0	0.6	0.5
MICROCREDITS	0.0	10.3	0.0		7.1	8.3	7.9
OWN SAVINGS	66.3	80.4	0.0		83.7	71.1	71.6
SAVINGS + GIFTS FAMILY	0.0	3.1	0.0		0.0	0.4	0.5
SAVINGS + LOANS	0.0	0.0	100.0		0.0	7.0	6.4
SAVINGS + LOANS FAMILY	0.0	0.0	0.0		0.0	6.8	5.7
SAVINGS + MICROCREDIT	15.3	6.2	0.0		0.0	4.9	5.2

Housing Maintenance

	ZhEKs	HOA	Self-Managed	Private company	Other	Don't know	All multifamily buildings
Type of management structure	88.9	1.1	0.2	1.3	7.6	0.9	
Maintenance payment (Various)							
Pays maintenance fee (percentage)	65.5	100.0	0	100	65.73	0	65.93
Has discount in maintenance fee (percentage)	1.6	0.0	0	11.53	2.15	0	1.74
Mean (monthly) maintenance fee AZN	5.09	7.68		16.87	3.95		5.30
Mean frequency of billed maintenance fee - in times per year	7.9	2.2		2.1	4.2		7.4
In arrears of payment of maintenance fee	4.3	0.0	0.0	5.4	9.2	0.0	4.7
In arrears of payment of utilities (percentage)	7.6	0.0	0.0	10.3	0.0	47.0	7.3

	ZhEKs	HOA	Self-Managed	Private company	Other	Don't know	All multifamily buildings
Satisfaction with current management							
Satisfied with current building management	18.5	38.0	0	40	30.08	47.8	20.11
Not Satisfied with current building management	81.5	62.0	100.0	60.0	69.9	52.2	79.9

Renters: various

	Oral rental agreement	Written rental agreement	All renters
Type of agreement	72.38	27.62	
Monthly rent			
Manhat (mean)	259.6	240.2	249.7
Manhat per sq.mt (mean)	5.7	6.3	5.8
Various			
Rent includes utilities (percentage)	0.0	4.4	1.0
household receives a rent discount (percentage)	1.38	4.79	2.15
how did you found rental dwelling			
WORD OF MOUTH	18.4	5.2	14.71
REALTOR	49.0	17.8	40.35
AGENCY	2.74	17.92	6.93
SIGNS/ADVERTISEMENT	1.6	3.2	2.1
IT WAS ASSIGNED	5.4	27.2	11.4
through friends/ relatives	23.0	25.4	23.6
OTHER	0.0	3.4	0.93
Payments at time of rental agreement			
gave advanced payment (percentage)	9.7	4.1	8.17
Paid fee to real estate agent (percentage)	2.85	7.19	4.07
Gave security deposit (percentage)	2.26	4.12	2.78
Security of tenure			
Likely owner asks renter to leave without prior notice or a valid reason (percentage)	28.59	51	33.62

Renting and owning housing prices

	Selling price Manhat (mean)	Selling price Manhat per sq.ft (mean)	Selling price Manhat per room (mean)	Renting price Manhat (mean)	Renting price Manhat per sq.ft (mean)	Renting price Manhat per room (mean)	Renting price Manhat (mean) - RENTERS	Renting price Manhat per sq.ft (mean) RENTERS	Renting price Manhat per room (mean) RENTERS
Absheron	64133.5	1122.8	26287.16	247.7	4.4	102.9			
Binagadi	78186.0	1451.5	31623.3	399.5	7.4	160.9	304.1	6.5	140.8
Garadagh	20880.0	394.6	8140.2	70.6	1.3	27.0			
Khatai	74077.6	1337.2	28938.4	270.7	4.9	108.5	200.0	4.5	80.7
Khazar	69584.7	990.4	23489.9	252.6	3.9	94.1			
Narimanov	128016.8	2200.7	56512.5	477.8	7.7	192.5	396.3	7.0	159.5
Nasimi	61126.7	1025.5	21528.4	374.2	6.2	128.9	204.1	6.8	142.6
Nizami	76074.4	1700.5	35944.0	260.5	5.9	131.3	279.2	5.9	123.8
Pirallahi	40500.0	885.2	18833.3	155.0	3.3	69.2			
Sabail	81217.4	1373.9	30060.1	353.5	5.7	128.8	221.1	4.2	86.8
Sabunchu	79028.6	1217.1	29296.7	256.2	4.2	103.4	218.9	3.5	88.7

	Selling price Manhat (mean)	Selling price Manhat per sq.ft (mean)	Selling price Manhat per room (mean)	Renting price Manhat (mean)	Renting price Manhat per sq.ft (mean)	Renting price Manhat per room (mean)	Renting price Manhat (mean) - RENTERS	Renting price Manhat per sq.ft (mean) RENTERS	Renting price Manhat per room (mean) RENTERS
Sumgayit	53383.0	1198.5	23239.5	203.2	4.8	90.6	154.6	4.0	85.0
Suraxani	55089.5	950.7	20227.8	170.5	2.9	63.2	231.4	4.2	89.5
Yasamal	93787.5	2173.4	48173.3	336.8	7.2	159.3	103.2	4.3	72.0
Zones									
Baku	84279.8	1617.3	36136.3	342.1	6.4	142.4	265.7	6.2	131.3
Eastern suburbs	65243.5	1042.8	23744.3	211.8	3.5	81.4	227.0	4.0	89.2
Absheron Sat. City	64133.5	1122.8	26287.2	247.7	4.4	102.9			
Sumgayit Sat. City	53383.0	1198.5	23239.5	203.2	4.8	90.6	154.6	4.0	85.0
Western Suburbs	20880.0	394.6	8140.2	70.6	1.3	27.0			
Idp category									
NO (Non-IDP)	80271.1	1506.7	33520.2	305.0	5.7	126.2	258.6	6.0	127.5
YES (IDP)	39836.4	797.6	17030.4	164.4	3.1	69.4	64.9	1.0	21.6
Year built									
before 1940	90538.9	1819.2	40077.1	297.1	6.4	133.1	165.9	5.4	102.6
1940-1969	66278.3	1344.9	28807.0	271.0	5.5	119.0	220.1	5.5	117.5
1970-1989	77252.6	1460.1	32482.4	293.6	5.4	120.9	309.8	6.4	139.2
1990-1999	70239.6	906.7	21263.8	317.1	4.1	94.4	231.4	4.2	89.5
after 2000	85231.9	1205.1	33242.9	294.8	4.2	120.3	276.7	5.7	111.6
Type of dwelling									
HOUSE	86726.7	1218.3	30072.9	287.7	4.1	98.0	201.2	5.6	111.2
APARTMENT / FLAT	78509.5	1565.6	34070.2	311.7	6.1	133.7	257.3	5.9	125.3
HOUSE/APARTMENT OR DORM	2048.4	82.4	1352.1	14.3	0.3	6.1	0.0	0.0	0.0
COLLECTIVE CENTERS	7284.3	286.6	5189.4	35.5	1.2	23.7			
Employment status of Head of household									
FULL EMPLOYMENT (FULLDAY WORK)	80044.2	1478.6	32776.6	311.1	5.7	125.8	274.2	5.6	122.0
INCOMPLETE EMPL. (PART-TIME)	60892.0	1246.6	27028.3	270.3	5.6	124.9	231.6	6.8	138.8
UNEMPLOYED	51114.6	965.1	20703.9	203.8	4.0	84.6	174.7	5.9	122.6
PENSIONER	74683.5	1510.6	33826.3	257.7	5.3	116.6	77.4	1.8	39.3
OTHER INACTIVE PEOPLE	77881.8	1146.6	27099.0	334.1	4.4	109.6	261.9	6.7	130.9
Greater Baku Region	74935.0	1412.1	31317.4	289.0	5.4	119.6	249.7	5.8	122.6
distance to Central Business District									
Less than 15minutes	91034.9	1674.4	40511.9	378.5	6.2	143.9	145.6	3.6	83.4
15-30minutes	85588.7	1610.6	35674.7	346.3	6.3	140.4	267.3	6.2	132.3
30-45minutes	69014.1	1321.7	28364.1	228.7	4.5	98.9	247.3	6.1	125.4
45-60minutes	66520.9	1208.8	27610.0	258.7	4.9	112.7	250.9	4.8	105.4
60-90minutes	50937.7	1048.9	20552.8	201.7	4.2	84.0	250.0	7.1	125.0
More than 90minutes	54804.6	1078.0	22590.4	185.8	3.9	84.1	0.0	0.0	0.0

*In purple are expressed prices (of owners and renters when asked how much they thought a similar dwelling in the neighborhood would rent or sell for). In yellow are revealed prices (actual prices paid by renters).

Socio-economic status of renters versus owners

Number of people living in house	Renter	Owner	Total
1	7.47	5.66	5.81
2	20.83	13.02	13.67
3	22.26	20.05	20.24
4	31.86	30.89	30.97
5	8.31	17.02	16.29
6	7.05	7.62	7.57
7	1.95	2.84	2.77
8	0	1.55	1.42
9	0.22	0.53	0.51
10	0	0.19	0.17
11	0	0.33	0.3
12	0.04	0.12	0.11
13	0	0.11	0.1
15	0	0.07	0.06
age of head of household	Renter	Owner	Total
Less than 15	4.03	1.17	1.42
16-25 yrs	72.11	42.1	44.66
25-35 yrs	8.02	17.76	16.93
More than 36 yrs	15.84	38.96	36.99
IDP status	Renter	Owner	Total
NO	84.46	88.1	87.79
YES	15.54	11.67	11.99
Non Response	0	0.24	0.22
gender of head of household	Renter	Owner	Total
Man	76.75	76.53	76.55
Woman	23.25	23.47	23.45
Married status of head of household	Renter	Owner	Total
MARRIED	69.75	78.74	77.98
SINGLE	12.6	2.06	2.94
DIVORCED	8.15	3.81	4.18
WIDOW/WIDOWER	8.25	15.17	14.59
respondent did	0	0.22	0.21
answer is inap	1.25	0	0.1
Employment status	Renter	Owner	Total
FULL EMPLOYMENT (FULL	61.79	60.59	60.69
INCOMPLETE EMPL. (PAR	19.92	5.13	6.37
UNEMPLOYED	6.93	8.45	8.32
PENSIONER	8.39	21.6	20.49
OTHER INACTIVE PEOPLE	2.97	4.07	3.98
If the answer is inap	0	0.16	0.15

Module D – Residential Mobility

Years since living in current dwelling

Years since living in current dwelling (Mean)	Less than 10 years	11-20 years	21-40 years	more than 40 years
Absheron	27.0	25.8	26.7	20.7
Binagadi	32.4	30.2	35.5	2.0
Garadagh	1.8	28.0	52.5	17.7
Khatai	22.0	40.0	35.1	2.9
Khazar	7.2	28.7	51.3	12.9
Narimanov	37.9	17.7	39.7	4.7
Nasimi	43.9	21.0	16.9	18.2
Nizami	25.0	12.0	52.5	10.6
Pirallahi	20.0	20.0	50.0	10.0
Sabail	12.9	40.3	37.0	9.9
Sabunchu	30.1	17.5	34.1	18.3
Sumgayit	28.1	26.9	36.8	8.3
Suraxani	22.8	9.2	64.7	3.3
Yasamal	17.5	30.3	34.7	17.5
Zones				
Baku	26.9	27.7	37.2	8.2
Eastern suburbs	22.0	16.0	51.8	10.2
Absheron Sat. City	27.0	25.8	26.7	20.7
Sumgayit Sat. City	28.1	26.9	36.8	8.3
Western Suburbs	1.8	28.0	52.5	17.7
Idp category				
NO (Non-IDP)	26.8	25.7	36.8	10.8
YES (IDP)	18.2	23.1	58.2	0.5
Year built				
before 1940	20.2	34.6	29.9	15.4
1940-1969	22.7	22.7	34.5	20.1
1970-1989	25.2	22.4	50.8	1.5
1990-1999	23.2	42.5	33.5	0.8
after 2000	88.3	11.7	0.0	0.0
Employment status of Head of household				
FULL EMPLOYMENT (FULLDAY WORK)	30.1	30.0	33.5	6.4
INCOMPLETE EMPL. (PART-TIME)	47.7	23.8	27.5	1.1
UNEMPLOYED	20.0	23.9	51.7	4.4
PENSIONER	9.4	13.3	55.3	22.1
OTHER INACTIVE PEOPLE	17.6	24.9	44.4	13.2
Greater Baku Region	25.5	25.4	39.7	9.4
IDP in collective center				
distance to Central Business District				
Less than 15minutes	24.4	23.8	33.5	18.3
15-30minutes	29.2	25.6	35.8	9.4
30-45minutes	18.6	24.5	51.2	5.7
45-60minutes	29.4	20.8	40.6	9.2
60-90minutes	22.5	37.6	27.9	12.1
More than 90minutes	16.7	28.6	52.3	2.4

Years since living in current dwelling (Mean)	Less than 10 years	11-20 years	21-40 years	more than 40 years
Owner or Renter				
Renter	81.2	6.9	12.0	0.0
Owner	20.9	27.4	41.1	10.5
Formal status				
No document	12.0	23.0	62.4	2.6
Registration card	14.2	12.4	58.1	15.3
Contract builder	0.0	0.0	100.0	0.0
Notarized contract	22.3	30.7	24.3	22.7
Homestead land title	57.7	9.6	22.1	10.6
Real Estate Registry	21.5	29.1	38.9	10.6
Renter				
Oral agreement	90.8	6.3	2.9	
Written agreement	68.7	4.5	26.8	

Previous place of residence, future movements, ownership of secondary residence/investment property

	Less than 10 years	11-20 years	21-40 years	more than 40 years	ALL
Where did you moved from?					
INSIDE GREATER BAKU A	61.9	57.5	42.5	46.0	52.9
OUTSIDE GREATER BAKU	35.3	39.1	47.8	42.8	41.2
OUTSIDE THE COUNTRY	2.9	3.4	9.8	11.2	5.9
Living in a rural or urban area before (Outside GB)					
Urban	43.8	42.4	20.0	28.5	32.8
Rural	56.2	57.6	80.0	71.5	67.2
Planning to move in the next 12 months and to where					
Yes planning to move?	8.9	5.6	4.3	2.9	5.7
Where are you planning to move?					
Plan to move INSIDE GREATER BAKU	78.1	95.7	93.1	100.0	88.1
Plan to move OUTSIDE GREATER BAKU	11.6	4.3	6.9	0.0	7.8
Plan to move OUTSIDE THE COUNTRY	10.3	0.0	0.0	0.0	4.1
Do you own another dwelling?					
YES	7.5	6.4	4.2	1.7	5.3
Where is the other dwelling located					
INSIDE GREATER BAKU A	25.6	68.7	60.5	59.0	51.4
OUTSIDE GREATER BAKU	74.5	27.7	39.5	41.0	47.5
OUTSIDE THE COUNTRY	0.0	3.6	0.0	0.0	1.1
Current use of secondary/investment property?					
RENTED TO ANOTHER FAMILY	35.3	32.2	7.0	17.1	24.7
RENTED (FREE OF CHARG	26.8	6.1	0.0	41.0	12.2
USED AS SECONDARY HOME	10.4	26.5	15.0	41.9	17.9
VACANT	22.5	35.2	41.1	0.0	31.8
CURRENTLY UNDER CONSTRUCTION	5.0	0.0	36.9	0.0	13.5

ANNEX 2: Legislative & Institutional Framework

This Annex presents a brief review of the existing legislative and institutional framework in regards to housing and summarizes existing Government housing programs. Regulations specific to the housing market and financing, linked to the rental market and linked to management and maintenance of multi-family buildings, are further analyzed in Chapter 3, Chapter 5, and Chapter 6, respectively.

The legal and institutional framework concerning residential property in Azerbaijan provides broad coverage of housing issues. The housing sector in Azerbaijan is regulated by relevant legislation, presidential orders/decrees, and secondary legislation. The legal-institutional framework affecting housing can be stratified into several distinct activity areas: (1) establishing and executing property rights; (2) alienation of property rights; (3) physical planning and construction; (4) management and maintenance of building stock; (5) taxation of housing-related activities; and (6) financing of the housing sector.

However, some gaps remain in regards to rental tenure, subsidy targeting, protection of developers' clients, and illegal construction, as well as implementing regulations of the Housing Code. Civil Code regulation of landlord-tenant relations is focused on 'commercial tenancies' with their emphasis on freedom of contract, while the Housing Code (2009) focuses on social rentals. Consequently, market-based residential tenancies are not covered by specialized regulations on landlord-tenant relations, including dispute resolution mechanisms. Subsidy programs are not explicitly targeted to low-income household categories and focus on other 'vulnerability' criteria. Clients of residential developers are not explicitly protected by separate regulations recognizing specific risks of pre-sale contracting and financing of the development process. The Housing Code has not been fully implemented with numerous secondary regulations still not issued.

Currently, there is no housing strategy or policy framework in Azerbaijan, but there is a set of institutionalized programs. Among this set of fragmented Government programs is the Azerbaijan Mortgage Fund (AMF) that provides social mortgage loans to qualified households, building façade beautification programs, and public housing provision for vulnerable groups such as IDPs and refugees. These are further discussed in Section 2 of Chapter 2 and in the Housing Finance section of Chapter 3.

1. Legal framework and in charge institutions

Below is a summary of the distinct activity areas and the main institutions in charge of them:

1.1. Establishing and Exercising Civil Code Property Rights

Property rights establishment and exercise is governed by the Civil Code (2000), which is overseen by the Ministry of Justice. These include full ownership rights, rental tenure rights, and land leasehold (usufruct) rights. Contracts regarding these rights are defined as well, although the Code guarantees also a 'freedom of contracts,' allowing the parties to design 'unnamed' contract types as long as these do not contradict general provisions of the Code.

Property Ownership Rights. When a physical/legal person erects residential dwelling on a plot of land and holds it in ownership possession, this person has to register it in order to obtain the title of property right. The Civil Code (2000) stipulates that a property right to a newly-created residential dwelling/home arises at the moment of registration in the State registry (Art. 178.2). Registration of property ownership rights is regulated by the *Law on State Registration of Real Estate* (2014). Property owners are obliged to pay recurrent property tax on their real estate property as stipulated in the Tax Code (2000) (Chap. XIII).

Land leasehold rights. A somewhat lesser property right, recognized in Article 250 of the Civil Code (2000) consists of a long-term land leasehold, sometimes referred to as a "land development right," wherein some person other than the landowner holds a long-term right (often up to 99 years) to develop land with

improvements like residential buildings.¹³⁵ It is a State-registered right, which is alienable (tradable) and inheritable. This right may be granted by a State or municipality on its own land for a period not exceeding 99 years. A large up-front payment is required through negotiation or tender bidding, and no annual ground rent is payable. Additional regulations are embodied in the *Law on Land Leases* (1998) and in the *Law on the Land Market* (1999). Since the landowner is a public entity, no tax obligation exists in reference to this arrangement.

Rental Tenure Rights. Rental tenure of residential dwellings is popularly referred to as a commercial apartment lease (agreement) and is regulated by Chapter 34 of the Civil Code (2000) under the requirement of a written form, which is often disrespected and not registered as required by the Code (Art. 139). Additional regulations are embodied in the specific *Law on Leases* (1992). There is no separate definition and regulation for residential renting, so there are no special rules governing rental housing activities except for those pertaining generally to leases (Chap. 34). Residential rentals are recognized as commercial activity and thus subject to Article 679 of the Tax Code (2000), which requires the landlord to pay income tax. In practice, most landlords enter into verbal (unwritten) agreements and thus avoid income tax liability. This means that rights and obligations in rental tenancy agreements embodied in the Civil Code (2000) are not effective.

Social Rental Tenure.¹³⁶ The Housing Code (2009) defines and regulates special tenancy situations, called social hiring, for qualified categories of socially-vulnerable households (Art. 50), which can apply for an allocation of State or municipal housing. The use of the term ‘social hiring’ may be misleading since this concerns public housing – see the Acronyms and Glossary section at the beginning of this report. Qualified households enter into a social apartment lease agreement, but its legal form is stipulated in Chapter VII of the Civil Code (2000). Before such an agreement can be executed a decision of a local executive authority has to be issued in respect to allocation of a residential dwelling. The agreement is for an unlimited period of time, which stems from the Soviet period. Since the owner remains the State or municipality, no tax liability pertains to such arrangements.

1.2. Alienation (Transfer) of Property Rights

Property transfer. The property rights established and exercised under the Civil Code (2000) may be alienated (transferred) through a number of market and non-market mechanisms sanctioned by the Code: (i) sale and purchase agreements (Chaps. 29, 30); (ii) property swap/barter (Chap. 31); (iii) property gift/donation (Chap. 32); or (iv) property hire (Chap. 33).¹³⁷ All of these forms involve complete alienation of full ownership rights and are subject to taxation regulated by the Tax Code (2000).

Privatization of apartment dwellings. During the early years of the transition period, most of the apartment dwellings were privatized, so that the new owners (i.e., sitting tenants) obtained ownership rights to their apartments. This was, and still is, governed by special legislation – *Law on Privatization of the Apartment Stock* (1993). The right to privatize is codified and upheld by the Housing Code (2009) (Art. 146).

Acquisition of ‘new’ land. Access to land for residential development is specifically regulated in the Land Code (2000), which deals with land relations for different types of land ownership; exercise of land-related owner responsibilities; users and lessees of land; protection of the right to land; creation of relevant conditions for rational use of lands and their protection; restoration and increase of the fertility of land; re-cultivation of land which have become unusable as a result of pollution and destruction; and preservation and improvement of the natural environment (Art. 2). Initial land reforms, especially regarding agricultural land, were embodied in the *Law on the Land Reform* (1996). More specific issues regarding allocation of municipal lands are embodied in the Regulation On Preparation of Documents and Agreeing on the Rules for the Allocation of Municipal Lands (2002).

¹³⁵ This institution dates back to Roman law where it was called “*superficies*” and is used in many countries of the world.

¹³⁶ Although it is called *social rental tenure*, it refers to what is known as public housing rather than social housing – see the Acronyms and Glossary section at the beginning of this report.

¹³⁷ This involves alienation to another person for providing in-kind or material assistance by the beneficiary to the grantor.

Expropriation. A process of taking (expropriating) land ownership for public use is regulated in the *Law about Withdrawal of Lands for the State Needs* (2010). Some aspects of this process are covered by the Civil Code (2000) and the Housing Code (2009). Alienation of land ownership can take the form of voluntary sale and purchase or a forced taking, and in the latter case a just compensation is payable.¹³⁸

Condemnation. A considerable part of the housing stock continues to quickly deteriorate due to profound under-maintenance and lack of capital repairs. Some of it is ripe for condemnation and the portion will only grow, so there will be more closures and demolition orders for dilapidated buildings. The Ministry of Emergencies is working on regulating and streamlining this process. Each district in Baku is supposed to implement an assessment of its existing housing stock by a joint commission. The local executive powers play a central role in this process. The local executive power prepares the list of buildings that need renovation/demolition and introduces the list to the higher level executive bodies. There is no centralized process for this, and it is not clear that the Ministry of Emergencies is attempting to regulate or streamline this process. Condemnation of buildings results often in alienation of property rights, especially if the building gets demolished. Compensation issues arise as much of the 'cleared' land after demolition is expropriated per the *Law about Withdrawal of Lands for the State Needs* (2010).

1.3. Physical planning and construction process

Every physical/legal person is entitled to build any residential dwelling over a plot of land in his/her ownership. Development of land has to proceed in accordance with conditions of physical planning and construction permits issued by the pertinent authorities and governed by the Town Building and Construction Code (2012), which is overseen by the Ministry of Emergencies. There are different levels of requirements for buildings, which do not exceed three floors, where the height does not exceed 12 meters, and the span between weight-bearing walls does not exceed 6 meters. Such smaller projects require only a preparation of an architectural-planning element for construction permitting. Residential development projects, larger than the above, require prior project planning permission.

1.4. Regulation of illegal construction

During the last five years, the Azerbaijan Government has made an effort to prepare the legal basis for regulation of illegal constructions in the Republic of Azerbaijan. But there are still important gaps that leave many existing illegal settlement unable to regularize.

Article 178.6 of Azerbaijan's Civil Code provides that: "Where a person has possessed property not registered in the State register of immovable property and such possession was continuous for thirty years without any objection being made, such person may demand registration as the owner." However, this article has been superseded by a recent Presidential Decree.

One of the main steps toward regulation of illegal construction was the Presidential Decree of January, 2015 "On approval of the list of documents confirming the acquisition of rights over immovable accommodation facilities merged and acquired before the entry into force of the *Law on State Registration of Rights to Real Estate*." According to the Decree, registration of real estate will be valid if at the time of establishment the property was not located in areas featuring main pipelines, electricity networks of high voltage, transport infrastructure, and water protection zones, or land plots owned by business entities for the use of oil and gas. This decree also states that the registration will be valid for property rights arising on the basis of municipality decree or on some other official document (not registered in the State Committee for Registration of Rights on Immovable Property). According to the laws of Azerbaijan, all property rights on immovable property should be confirmed by official documents.

¹³⁸ On one hand, the State's laws for eminent domain, i.e., for acquiring privately-owned property, are very strong. One might have all the papers and the valid ownership documents, but the public sector can come and demolish the housing unit at any time. By law, compensation for such acquisition should be market value plus 20 percent, or a comparable or better apartment within 100-500 meters from the site border.

However, in Azerbaijan, many people live in houses without any official document received from the municipality and other bodies. This is particularly true for people who were refugees in the early 1990s, who were forced to settle in protected areas.

1.5. Management and maintenance of the housing stock

Management of the privatized apartment stock is regulated as common property serving more dwellings in multi-family buildings.¹³⁹ The Civil Code (2000) defines the rights of apartment owners over this common property/areas (Art. 227). The Housing Code (2009) reinforces this right (Art. 35.2) and imposes obligations on the apartment owners to maintain and repair common areas in the multi-family buildings (Chap. XV) as well as provides options for property management models (Art. 141), the most prominent of which is the homeowner association (HOA), referred to as MMMC in Azerbaijan. However, specific bylaws and procedures for this are still missing to make this option workable (for further discussion, see Chapter 6). Another key implementation gap in the Housing Code (2009) is the continued role of the inefficient public companies ZhEKs for management of multi-family buildings even though the Code envisions their elimination.

1.6. Market financing of housing

Construction finance is mostly done through pre-sale arrangement with buyers paying in advance. This can be a risky business for buyers, since there is no specific protection against default by developers besides the general provisions in the Civil Code (2000) in Chapter 39 on Works Contract as well as the *Law on Protection of Consumer Rights* (1996). Some larger developers do not use pre-sale contracts, as they are able to access 'project finance' from commercial banks, but these are still rare and governed by general rules for bank financing, including enforcement of collateral.

While construction financing remains unregulated in terms of protecting the end buyer of a newly-constructed apartment dwelling, the business of mortgage lending by commercial banks is regulated in the *Law on Mortgage* (2005), through the Presidential Decree On the Creation of the System of Mortgage Loans (2005), and through the Government Decree (Cabinet of Ministers) On Approval of the Form for Mortgage Securities (2005). Further enhancement of mortgage lending through mortgage insurance is embodied in the Presidential Decree On Improvement of Mechanisms for Mortgage Credits Issuance (2007).

¹³⁹ This typically includes roofs, facades, staircases, lifts, corridors, basements, conduits and piping for utilities.