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HOUSING FINANCE INTERNATIONAL

The Quarterly Journal of the International Union for Housing Finance

- Dubai's Real Estate Boom and Bust of 2002 – 2008
- The Revitalisation of Brazil's Housing Finance System
- Towards a Sustainable Housing Finance in Nigeria
- Northern Ireland's Housing Market
- Housing Policy Realignment in East Asia
- The Impact of the Financial Crisis on UK Mortgage Funding

International Union for Housing Finance

Housing Finance International

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Editor's Introduction

↳ By Friedemann Roy

It is my pleasure to present you the Summer 2010 edition. It is the last edition in which I assume the function of the editor. I would like to take the opportunity to thank you for your interest in the journal. I also would like to thank all contributors for the articles, as well as the experiences and insights they shared with us in their work.

The last years have been a fantastic journey through the economic cycles of the housing finance markets. Our contributors helped us to better understand the booms and busts of these cycles and their repercussions on individual housing finance systems as well as national and regional markets. We also learnt about new innovations in housing finance and how they aim to address affordability constraints in housing and housing finance.

I would like to introduce to you the new editor, who already helped to prepare this edition. He will resume full responsibilities for the future editions: Andrew Heywood is a consultant specialising in housing and mortgage markets, regulation, governance and European issues with significant clients in the housing and mortgage sectors. In his former role as Deputy Head of Policy at the Council of Mortgage Lenders (CML), Andrew had specific responsibility for lending for social and affordable housing, for low-cost home ownership products as well as for the private rental sector. In his free time, he is a keen jazz saxophonist and leads his own quintet Afinado. I would like to wish Andrew all the best for his new position and I hope he will enjoy the work as I did.

Our first article is presented by Bertrand Renaud and deals with Dubai's Real Estate Boom and Bust during the years 2002 – 2008. During this period, Dubai experienced a massive real estate boom and bust. As a rapidly growing open economy located in a strategic region of the world, Dubai emerged as one of the most visible global cities and found ready access to finance during the global credit boom. Real estate projects exceptional in nature and scale shaped the image of the emirate around the world. However, this growth was not a mere desert mirage. He discusses the factors behind this remarkable transformation of a sleepy fishing village into a global city in a time span of about five decades and how the global credit boom contributed to Dubai's massive real estate boom. In addition, he discusses how Dubai is now adjusting to the real estate bust triggered by the global financial and economic crisis. He believes that Dubai and the other emirates of the UAE are today at an inflexion point in their growth strategy. Therefore, he analyses the responses to the crisis triggered by the Dubai World debt standstill announcement of November 2009 and the actions being taken to strengthen the Dubai economy and the financial system of the entire UAE federation in a far more risky and uncertain global environment.

In our second article, Claudia Magalhaes Eloy takes a perceptive look at Brazil's housing finance system. She points to the rapid growth in the provision of mortgage finance since the 1980's but also draws attention to the fact that as a percentage of GDP, mortgage credit is still only half the 10% average for developing countries. Ms Eloy highlights changes to the housing finance system and identifies key challenges and limits on the speed of future growth, including the limited role so far played by securitisation in mortgage funding. She also examines the impact of the banking crisis and recently emerging trends in housing finance.

The positive and negative links between the capacity of developers to increase new housing supply and the growth in mortgage credit is not always made explicitly. Timothy Olugbenga Nubi, who is the author of our third article, focuses on Nigeria in making these connections. As in Brazil, the development of mortgage credit is an ongoing issue and mortgage credit as a percentage of GDP stands at just 1%. Mr Nubi identifies the problem of new housing supply capacity as a key factor in the emergence of the Nigerian mortgage market and as a problem in itself. He uses the results of his own survey of housing developers to highlight the lack of capacity of the industry and the preponderance of small firms (judged by the standards of the developed world). Mr Nubi points to the key factors underpinning this situation and in particular to the problems faced by developers in gaining access to adequate levels of finance, and discusses the reasons behind what appears to be a major limiting factor on development.

The Northern Ireland housing market is the focus of our fourth article. It is in many ways unique, influenced as it is by both the UK and Irish markets. It is the only region of the UK with a land border on the Euro zone. Joe Frey and Paddy Gray use their deep knowledge of Northern Ireland and its housing market to provide a detailed analysis of the key drivers and trends, drawing on recent research by the Northern Ireland Housing Executive, the strategic housing authority in Northern Ireland and the main social landlord. Frey and Gray analyse the spectacular boom and bust in the Northern Ireland market since 2000, touch on future prospects and contrast this experience with that in the Republic of Ireland and with the rest of the UK.

In our fifth article Richard Ronald examines housing policy in East Asia. He identifies the East Asian economic crisis of 1997 - 1998 as a turning point in Government economic and housing policy in the way it undermined the reliance of policy makers on raising home ownership to further growth and to promote social stability. Drawing on the experience of Hong Kong, Singapore, Japan, South Korea, China and Taiwan, Mr Ronald analyses the often contradictory pressures on Governments in relation to a range of policy imperatives including the extension of home ownership, affordability, pension provision and housing key workers. His article also assesses the recent impact of the banking crisis and economic downturn of 2008 - 2009 on housing policy in the region.

Our last contributor in this edition is Rob Thomas. Mortgage funding in the UK is the focus in the first of two articles by Mr. Thomas, looking at the impact of the financial crisis on funding markets. He examines the rise in wholesale funding in the UK since the 1980's and identifies the very rapid rise in the volume of securitization in the period 2000 - 2007. He assesses the structural vulnerabilities of the UK in relation to wholesale funding, including the lack of an adequate UK- based pool of investors. After looking at the key elements and effects of the government response to the banking crisis, Mr Thomas examines the consequences of the crisis for the mortgage market in the UK, which has been unable to restore retail lending volumes. He then goes on to assess the outlook for 2010 - 2015 and the prospects for a return to normality.

I hope you will enjoy reading these articles. Please do not hesitate to come up with your comments to stimulate a wider debate which will allow for a broader exchange of ideas and concepts. They are more than welcome!

Friedemann Roy[1]

[1] The Findings, interpretations, statements and conclusions expressed herein are those of the editor alone and do not necessarily reflect the views of the International Bank for Reconstruction and Development/The World Bank and its affiliated organisations, or those of the Executive Directors of The World Bank. The same applies for the authors and their findings, interpretations, statements and conclusions presented in this HFI edition.

Contributors' Biographies

Dr Bertrand Renaud is an international consultant and President of Renaud and Associates. He specialises in financial development, real estate finance and urban development issues. He has been Advisor for the Financial Sector Development Department at the World Bank, Head of the Urban Affairs Division at OECD (Paris), full time professor at the University of Hawaii and professor at MIT, Seoul National University and the University of Hong Kong. Dr. Renaud holds M.S. and Ph.D degrees from the University of California at Berkeley and received the degree of Ingénieur INA in Paris, France.

Claudia Magalhães Eloy is currently a PhD student in Urban Planning/Housing at the University of São Paulo (USP), developing research on the National Housing Finance System. She holds a Masters in City Planning at the University of Pennsylvania, a Masters in Public Administration at Bahia's Federal University (UFBA), a specialisation in Real Estate Finance at the Brazilian Economists Order (OEB) and a BA in Architecture and Urban Planning (UFBA).

Dr Timothy Gbenga Nubi Heads the Department of Estate Management at the University of Lagos, Nigeria. He has over 20 years experience in research and teaching. He is the Vice President of the Real Estate Developers Association of Nigeria, an organisation set up by the Federal Government to solve housing problems in Nigeria.

Joe Frey's qualifications include an MSc in Town and Country Planning, the IoH Professional Qualification and more recently an MSc in Urban Policy and Practice from Glasgow University. He is currently Head of Research in the Northern Ireland Housing Executive, the strategic housing authority, and is a part-time lecturer in housing finance and planning at the University of Ulster.

Paddy Gray has worked in housing in various posts for 30 years. He has wide experience of academic and applied research in the UK and Republic of Ireland through research grants, consultancy and applied research contracts for governments, private and voluntary organisations. Paddy was appointed Professor of Housing at University of Ulster in 2009 and is President of the Chartered Institute of Housing.

Richard Ronald is Associate Professor in Urban Studies in the Department of Geography, Planning & International Development Studies, University of Amsterdam, and a visiting scholar at the Department of Housing & Interior Design, Kyung Hee University, South Korea. He is review editor of the International Journal of Housing Policy and also author of the 'The Ideology of Home Ownership' (Palgrave Macmillan, 2008) as well as numerous other articles on housing, urban and social change in Europe and East Asia.

Rob Thomas gained undergraduate and masters' degrees in economics before joining the Bank of England as an economist in 1989. He moved to UBS in 1994. In 2001 Abbey National recruited him to manage a pan-European mortgage funding project. In 2005 he joined the Council of Mortgage Lenders as a Senior Policy Adviser.

Towards a Sustainable Housing Finance in Nigeria: The Challenges of Developing Adequate Housing Stock and a Road Map

By Dr Timothy Gbenga Nubi

Abstract

This study acknowledges the importance of housing in the economy of any nation and the mortgage market as a measure of economic vibrancy. While mortgages account for more than 70% of the GDP in developed economies, it is less than 1% in Nigeria. Despite several efforts that have been made to develop the mortgage system in Nigeria, very little success is recorded due to a number of restrictions. Past studies on housing finance in emerging economies rarely consider the nexus between housing supply and housing finance. The poor performance of the construction industry especially the home builders or housing developers is identified as a major hindrance to the development of a robust mortgage system (Nubi 2006). This study is a combination of a field study and the use of secondary data to examine the structure, operations and factors that restrict the operations of housing developers in Nigeria. The study revealed that Nigeria has neither a single indigenous construction company capable of handling large scale projects nor a real estate developer that builds more than 100 housing units per annum. The developers rely mostly on loans from commercial banks and cannot access the long term finance that the capital market offers: All this has contributed to the deficit of about 14 million quality homes needed to create mortgages that should considerably revive the industry. The paper therefore recommends that developers should team up to undertake large scale projects while concerted efforts should be made to encourage new entrants into the market. Construction costs should be reduced by reducing the cost of land and documentation while the use of locally sourced material and skills are promoted.

1. Introduction

The linkages between housing and the economy of any nation cannot be overemphasised. Even as housing serves its fundamental role as a residence, it presents very important opportunities for drawing in local investment, supporting business productivity by presenting effective demand for a whole range of products. The labour market, the construction industry, the infrastructural development industry, and the financial system are all beneficiaries of a vibrant housing market. It is little wonder then that in most developed countries, the housing market accounts for a significant proportion of the GDP. Thus residential mortgages alone contribute over 87% of the GDP in Denmark and 71% in the USA. In the UK it is slightly lower at 70%, while in Germany residential mortgages contribute 54% of its GDP, Hong Kong stands at 31% and Nigeria comparatively lower at 0.8% (Nubi 2007 and Reis 2008). With such significant contribution to the economy as a whole, it is obvious that there is a high positive relationship between the economy and the housing market. The global importance of housing investment was accentuated by Pollock (2000) when he asserted that the world wealth was estimated to be in the region of $44 trillion of which approximately half is in real estate. The study then, did not make known the value of residential real estate on a global basis, but did in the United States, where 60% of real estate value was in form of owner occupied houses. If this relationship is extrapolated, it suggests that residential real estate represents about 30% of total world wealth, making it the largest single component. This is especially true in countries that rely on the availability of credit for both household and macro-consumption.

According to (Renaud 2004), where there is a well-structured housing finance system, the city appears well organised with well built houses. Otherwise, housing construction becomes incremental or progressive, sometimes spanning well over 15 years, inevitably creating substandard homes and slum settlements (Omirin 2007). Wide spread availability of home mortgages according to Titman (2002) helps to improve living standards and poverty alleviation by impacting on the quality of home construction, increased infrastructure and urbanization. Developed countries are able to reap positive externalities: increased savings, financial market development, stimulation of housing investment, upgrading of properties, increase in housing stock and, hence, the development of the construction industry with abundant job creation opportunities - all generally accepted as benefits of the housing industry. Besides, housing provides the best and most secure collateral for further loans, with the attendant social recognition of being a home, owner and the attachment it brings to the community (Frenkel and Rapetti 2009).

Unfortunately, the housing market and mortgage sector of Nigeria are still at an embryonic stage (Nubi 2006). Experience shows that savings, incremental construction and remittances from abroad, loans and gifts from family and friends, which are the conventional methods of finance outside the formal mortgage market, can hardly meet the financial requirements necessary to provide the required quality housing. The government, despite its direct home construction policy, has proven to be an inefficient and ineffective contributor to housing supply and finance. Despite the billions in funds drawn for this purpose, limited success has been achieved. According to Agbola and Olatubara (2007), previous attempts at public housing construction in Nigeria show that in 1980 only 13% of planned construction was completed. Similarly, evidence from various planning authorities has shown that the percentage of completed units to building plan application is abysmally low. The private sector, here characterized by the informal sector, i.e. individual developers constructing incrementally with their own funds and with a few corporate builders, according to the National Housing Policy (NHP 1992), supplied about 90% of the nation total stock. As contained in the

National Housing Policy document 1992, the Federal Government of Nigeria officially abandoned its direct construction policy for a new role as facilitator and enabler to the housing industry.

It is a known fact that governments of developing countries according to Ofori (2002) are major clients and investors in the construction industry. Non involvement of government and shifting the responsibility of housing delivery to a private sector that is at its infancy, with neither financial nor technical capacity to deliver, has grossly increased the housing deficit in developing countries. This is true for Nigeria, where despite a history of direct construction, there is still a deficit of over 14 million housing units. According to Mabogunje (2007), at a conservative construction estimate of N3.5 million ($25,000) per home, about $3.5 trillion is needed annually to fund the housing deficit if 1.4 million dwelling units are to be built annually for the next ten years to defray the deficit. According to Ebie (2006), acute shortage of housing stocks as underlying asset upon which mortgages are created remain the most critical of all other restrictions. All attempts to develop the mortgage sector in Nigeria in the 1990s failed mostly due to this factor Nubi (2006). The paper draws attention to the implication of acute shortage of quality housing stock on the mortgage market development in Nigeria and the factors that are responsible for the poor performance of Nigerian housing developers. In addition, the paper also recommends key actions to be taken to increase housing supply in Nigeria.

2. Housing Finance, Housing Supply and the Housing Stock Connection

When it comes to what to do in emerging financial markets, views of mortgage market development policies according to Renaud (2004) and Nubi (2007) remain framed by the experience of a few high-income economies; especially by the remarkable rate of innovation in the US financial markets during the last thirty-five years. Experts often assume the availability of housing stock and a highly developed home building industry. So far, there has been no study on the effect of the state of construction industry on the organisation, structure and performance of housing finance systems in emerging markets such as Nigeria. Renaud (2004) identified five recurring structural issues that need to be considered when proposing a mortgage market strategy as: market size, macroeconomic stability, the degree of development of financial market infrastructure, legal and structural path-dependency in the development of this financial infrastructure, the feasibility of domestic risk-based pricing for medium and long-term financial instruments, all with the implicit assumption that housing stocks are in regular supply as it exists in developed economies.

In England for instance there were an estimated 22,564,000 dwellings as at 31 March 2009, an increase of 0.74 per cent on the previous year. The house building industry often responds well to the challenge of increasing housing supply, with supply in 2007/08 reaching 207,500 additional homes, an increase of 59 per cent compared with 130,000 in 2001/0 (Community and Local Government 2010). This is not the case in Nigeria where the biggest housing corporations like the Federal Housing Authority (FHA) with access to basic resources built only 30,000 houses in 34 years. No private developer can boast of 1000 units of houses in 10 years in Nigeria. Most of the so called mortgage loans given in Nigeria were construction loans. These were often secured with land titles. Such loans often carry both construction and credit risk. In most cases due to the volatility of the economy the loans were never enough to complete the constructions, leading to abandoned projects and a high rate of defaults. Foreclosure is rare in Nigeria because of legal restrictions but where foreclosure is possible, there is hardly a market for uncompleted and abandoned houses (Adewole, 2010).

3. Property Development Agencies and the Operating Environment in Nigeria

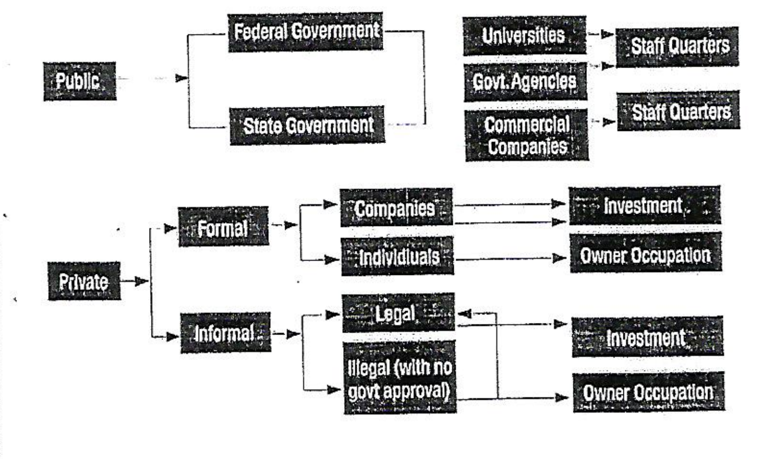
As stated earlier the nation in the last ten years has attempted to restructure housing policy to deliver the required 14 million housing stock in line with the demand of global best practice. The policy thrust was to have a private sector driven housing system. The Government in the year 2000 realised that this could only be achieved by introducing policy reforms and re-engineering the existing institutions, hence the shifts that emphasised a(n):

- Establishment of a Real Estate Developers Association (REDAN);
- Establishment of a Ministry of Housing;
- Restructuring the housing finance system through Federal Mortgage Bank of Nigeria (FMBN) - introduction of Secondary Market); and
- Land reform.

In line with the above, REDAN was inaugurated in 2002 by the president of the country with the following aims and objectives:

1. To provide a central, national organisation, which will articulate the aspiration, activities, target and aims of Real Estate Developers in Nigeria in order to facilitate, enhance and realise those aspirations activities, targets and aims.
2. To promote the development of residential estates in order to increase the stock of housing units available at affordable costs for all classes of Nigerians.
3. To promote the rehabilitation, refurbishment and general improvement or upgrading of existing housing units and residential facilities, in both the urban and rural localities, which are deemed to be dilapidated, substandard or otherwise of inferior quality.
4. To promote the development of commercial, industrial and agricultural estate, as a complement to the development of residential estate to ensure a balanced land use pattern in the country.
5. To liaise with financial institutions to develop an effective home ownership mortgage facilities to provide more realistic long-term mortgage facilities for prospective homeowners.
6. To set targets, in line with government policy objectives with a view to fully mobilising the private sector, for participating in the development of set targets.
7. To liaise with interested foreigners in both the private and public sectors, who want to participate in the Nigerian housing program as financiers, builders, and technological innovators or in any other capacity that is deemed likely to enhance the delivery of good and affordable housing to the Nigerian people.
8. To pool the resources of all potential investors, local and foreign, towards achieving economies of scale in real estate development and ensuring that the products of participants conform with National Building Standards and Regulations.
9. To provide a united front in making recommendation to the government on ways of promoting real estate development and in seeking solutions to practical problems in the property market.
10. To provide the use of local inputs and financial research into the suitability of local building materials in the country.
11. To establish links with the Real Estate Institutions and Allied bodies at home and abroad with the aim of promoting the development of the industry.

Figure 1 Housing Producers in Nigeria



Source: Omirin M. M. (1992) and Nubi (2006)

12. To publish and/or disseminate relevant information through bulletins, seminars, workshops, lectures etc. for the education of members of the association and the general public.

3.1 Who is a Real Estate Developer?

Mabogunje (2002) defined a Real Estate Developer during the inauguration of REDAN as not just a construction company or just a contractor. He/she is not even just a real estate investor or a professional like an architect, an estate surveyor or valuer, a quantity surveyor, an engineer or a town planner interested in housing. Rather, a real estate developer must share some of the attributes of all of these professional or corporate individuals but he/she must be more besides them. The best definition of a real estate developer is that he/she is an entrepreneur who is committed to assuming the risks of mass housing production in advance of sale.

Ibeh (1990) identifies four categories of Real Estate Developers in Nigeria. These as shown in Figure 1 include:

i. Private individuals (non corporate)

ii. Corporate bodies registered under the respective Companies Acts e.g. Odua Investment Company; Imani Estate, and Crown Estate.

iii. Government Corporate entities established by law such as Federal Housing Authority (FHA) Lagos State Property Development Corporation (LSDPC), Ogun State Property Investment company (OPIC), Sokoto Urban Development Authority (SUDA), etc.

iv. State Ministries and Local Government Councils.

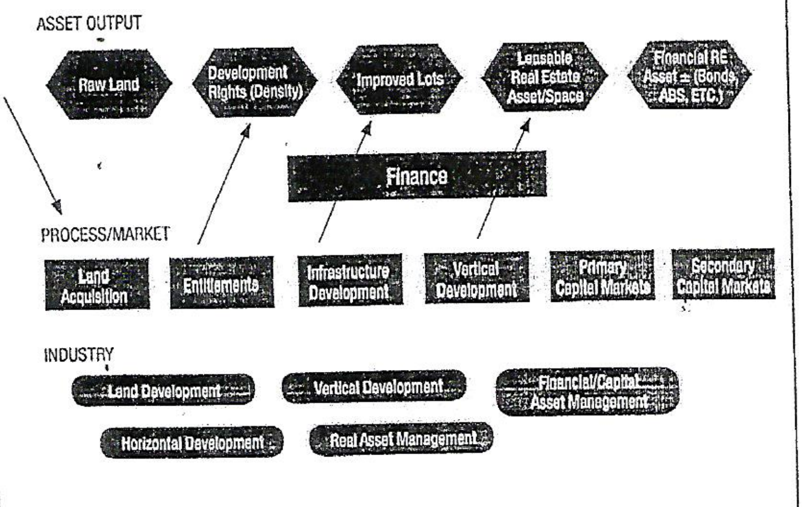
3.2 Property Development Process in Nigeria

Like in most parts of the world, the main operation of developers in Nigeria are: site selection, development appraisal, development research and design, arranging development finance, building contract/construction management and disposal of finished products. Where the economy has fully developed the real estate value chain, as shown in Figure 2, with each part of the chain well integrated, investing in real estate becomes a calculated risk but where the entire process is in disarray, investing in this sector is a big gamble. Each of the stages in real estate development poses different challenges to an average developer in Nigeria. The developer's ability to manoeuvre these challenges goes a long way to determine the success of the project.

4. The Study Approach

The survey was tailored towards assessing the operations of some selected registered residential property companies. Corporate housing developers like any other stakeholders in the construction industry in Nigeria attract a large number of entrants, as is also the case in many countries. Before 2002, there was no means of obtaining a comprehensive list of developers in any part of the country. The size was dynamic and indeterminate. It is, therefore, out of sheer luck that REDAN was inaugurated in 2002 and a comprehensive list that was used in this study was compiled. From the list of 450 companies on the REDAN list, only the 50 that have operated for 5 years and are directly involved in housing development for sale were selected. Data was collected from senior representatives of selected organisations with a structured questionnaire. Secondary data was derived from respondents' in-house publications and documentary analysis. The questionnaire was designed to collect information on REDAN members, their operations, funding, and level of accessibility to mortgage

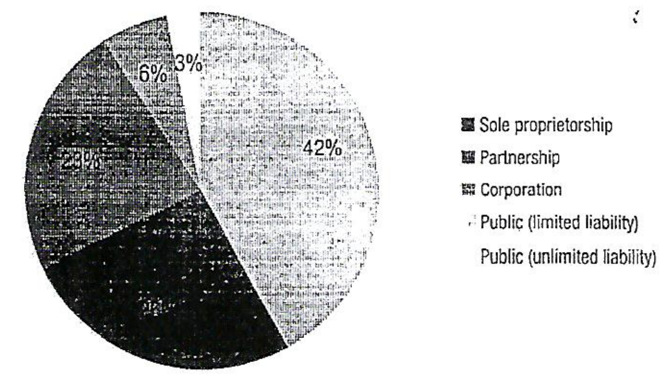
Figure 2 Real Estate Development Value Chain



Source: Megbelugbe 2007

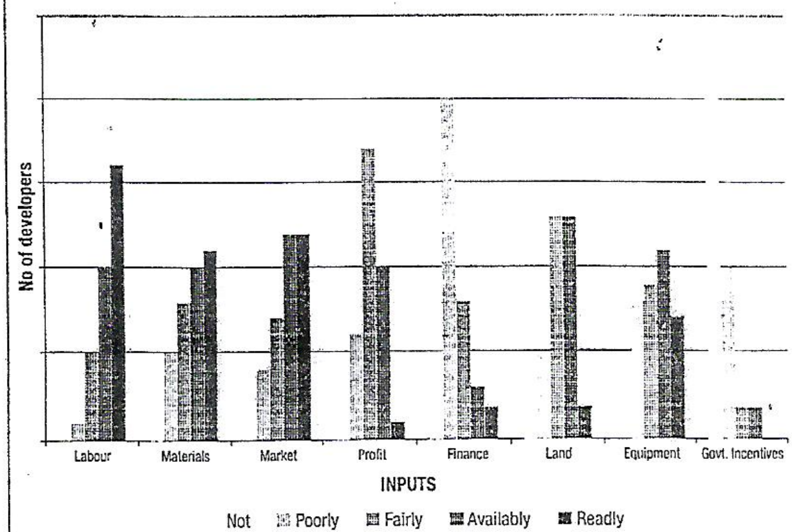
finance. The structure, capacity for growth and methods of overcoming problems, managerial style and capacity to meet customer demand was investigated to identify constraints. This was set against the governmental requirements for the private development and governmental policies on property finance. There were 20 items altogether in the questionnaire. Variables 1-7 measured the name, address and age of the organisation, category of professionals in the organization, nature of business, age of business and number and categories of employees. Variables 8-14 probed into operations and level of accessibility to factors of housing production, the number of houses, and types built. Annual turnover, source of fund, and nature of the portfolio were also measured. In relation to the problem of accessibility to finance, measurements were taken using five criteria which included: required equity, collateral, insurance, interest rate and number of years.

Figure 3 Ownership Structure



Source: Field Survey (Nubi 2006)

Figure 4 Responses on Availability of Housing Construction Inputs and Motivations.



Source: Field Survey (Nubi 2006)

5. Findings and Discussion

5.1. Nature and Operation of Real Estate Developer in Nigeria

The study revealed in Figure 3 that about 26% of the Real Estate Developers are sole proprietorships, 23% are partnerships, 6% are corporate developers, 42% are public limited liability companies while 3% are public companies. This has a lot of effect on management, volume of work and access to funding. None of these firms has more than 100 employees. In fact, almost 50% have less than 10 workers on their pay roll. Lack of permanent staff, which is caused by low volume of work and irregularity of work, often robs the company of the benefit of organisational learning. Some 60% of these organisations have no in-house experts like Architects, Civil Engineers, Mechanical Engineers, Builders, Estate Surveyors, etc. On availability of construction input presented in Figure 4 below, some 57% of the respondents claimed that finance is poorly available. This is the lowest rank amongst all other inputs, with only 5% responding that it is readily available. Land is even believed to be fairly available. On the type of houses often developed, the responses are 5% semi-detached, 7% Duplex, 13% Bungalow. About 34% high-rise and 20% block of flats and rated 21% for others. This shows a preference for housing for high-income earners and not mass housing. These are often produced on an average of less than 20 per developer per annum. The low volume of construction in this sector significantly contributes to the shortage in housing stock, high cost of housing and over concentration in high-brow neighbourhoods.

5.2 Source of Capital for Operation and House Building Activities

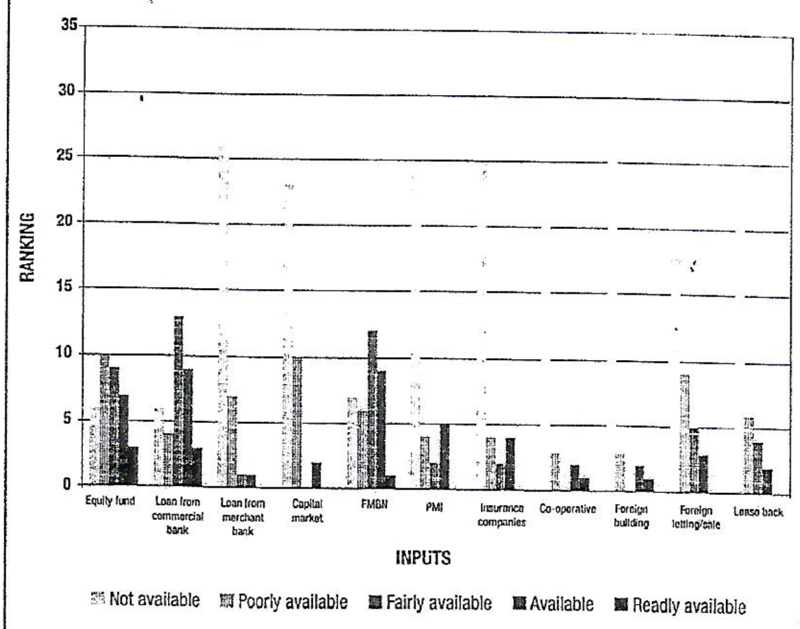
In terms of the type of houses being built, 21 (20%) build bungalows, 30 (29%) semi-detached, 28 (26%) Duplex and 14 (13%) blocks of flats were constructed. No member of the Real Estate Developer has attained more than 100 units per annum. Most developers sold less than 25 units.

On the availability of construction inputs like labour, building materials, availability of market for finished goods, profit from business, finance, land, equipment and government incentive, the responses are as follows: Finance stands out as an input that is not readily available, labour is rated as being readily available while government incentive was rated as not being available at all. Real Estate Developer also ranked the level of availability of different forms of finance for financing their housing development projects. They rated Primary Mortgage Institution very poor, but equity funding and loans from commercial banks enjoyed better rating, as shown in Figure 5 (see next page).

On factors that inhibit access to finance, particularly the developers loan facilities offered by the Federal Mortgage Bank of Nigeria (FMBN), the developers rated high interest rate (which was put at about 27% after the administrative charges had been built in) as highly problematic. Also rated as very problematic by most developers was the need to repay loans within 2 years. This is not unconnected with the limited sources of finance in the market. The predominant source today is the commercial bank as shown in the ranking in Tables 1 and 2. Commercial banks in Nigeria with their short-term deposits could only give short term loans while housing development requires long term facilities. The few loans that were given also required credit insurance or bank guarantee thereby increasing the cost of capital. Since most of the developers are not listed, they could not enjoy the opportunities that the capital market offers. This also presents the rating of demand for insurance and bank guarantee as problematic.

This is not unconnected with the depression and high rate of inflation resulting in high cost of building materials, high wage rate etc., the delay in getting the Certificate of Occupancy and running of building approvals ranking third could however be blamed on administrative bottlenecks and bureaucratic procedures.

Figure 5 Accessibility of Funds



Source: Field Survey (Nubi 2006)

5.3 Problems of Property Development Companies in Nigeria

Property development is sensitive to both micro and macro economic climate due to its poor response to change in supply or to demand, the effect of economic policies is often grievous on housing project common economic problems include:

5.3.1 Increase in Poverty Level

Poverty is a major problem in Nigeria. With about 70 percent of the population operating in the informal sector of the economy earning about $1 dollar daily, saving is almost impossible. It is not only that a robust mortgage system hinges on appreciable population with regular and reasonable income to create effective demand, but must also be able to generate sustainable long term savings that accrue to the capital market where such is eventually offered as products to home buyers and developers. The absence of this is a big constraint to the growth of the sector in Nigeria.

5.3.2 Problem of Raising Finance from the Capital Market

The capital market or secondary market is usually one of the most important sources of finance for housing development in developed economies especially where the real estate value chain has been developed. The prevalent business structure of housing developers in Nigeria prevents them from tapping into the opportunities that the capital market offers. The nation in the last five years witnessed unprecedented capital accumulation through the pension reform, with about 1.2 trillion naira ($80billion) accumulated into the Pension Fund. The pension act allows 40% of the fund to be invested in Real Estate but strictly through Real Estate Investment Trust (REIT) and Mortgage Back Security (MBS). Unfortunately this great opportunity cannot be annexed because the Primary Mortgage Bank's (PMI's) portfolios are ridiculously low with the giant among them (Union Homes) having less than 10,000 mortgages originated over a ten-year period. Only 6% of property development companies are listed on the Stock Exchange (see Figure2) hence their inabilities to neither float REIT nor go to the capital market for other products. In the absence of demand from real estate developers, approximately 80% of the fund has been invested in government bonds making the Government the sole beneficiary of the pension fund meant to develop the real estate sector of the nation's economy.

Table 1: Ranking of Sources of Finance for Housing Projects by Developers

S/No	Source of housing finance	Ranking by developers in order of significance
1	Loan from commercial bank	1st
2	Equity	2nd
3	Credit facilities from building materials supplier	3rd
4	Shares (Capital Market)	4th
5	Foreign loan	5th
6	Mortgage loan	6th
7	Gift from friends	7th
8	Loan from Thrift and Credit Societies	8th

Source: Field Survey (Nubi 2006)

Table 2: Ranking of Constraints in Housing Production Effort Developers

CONSTRAINTS	RANK
Fund shortage/high cost of fund	1st
High cost of construction	2nd
Delay in Certificate of Occupancy and building plan approval	3rd
High cost of building materials	4th
Land acquisition problem	5th
Route of infrastructure	6th
Manpower shortage	7th
Government Policy (LUA ETC.)	8th
Poor demand	9th

Source: Field Survey (Nubi 2006)

5.3.4 Galloping Inflation on Estimated Project Costs

According to Windapo and Iyagba (2001) and Nubi (2006), approximately 60% of the building materials in Nigeria are imported. Since the prices of these materials are subject to the exchange rate of other foreign currency, which changes almost daily, construction cost and house prices remain unpredictable. Many projects in Lagos and Abuja have being abandoned while many companies have gone into liquidation because of their inability to cope with the uncertainty of the market. Also, some developers that built to capture the high-income market have difficulties in disposing of the few houses built.

5.3.5 High Cost of Capital

Most of the developers interviewed expressed their awareness of the availability of fund in the capital market (see Figure 5) but it was ranked fourth as a source of funding while loans from commercial banks was ranked first. Long-term loans are usually not favoured by the commercial banks in Nigeria due to the short-term nature of their deposits. The best term any developer can get from these banks is four years. Funding a long-term investment with short-term fund with no possibility of take out finance is generally believed to be a mismatch. This mismatch has a far-reaching implication on the cost of capital. The short-term loans are usually more expensive in Nigeria with interest rates usually between 35% and 45%. This high interest rate on capital has not only killed real estate projects in Nigeria but, also, the borrowers. Despite the abysmal interest rate the banks also demanding about 20-30% of the value of the loan as deposit and always insist on collateral of equal value of the loan.

5.3.6 Access to Land

Land is a major input in property development. The cost of acquisition and documentation as well as its administration is essential to property development and financing. From simple holding in traditional settings, land holding has become a complex system in the 20th and 21st century in Nigeria. The land in any state in Nigeria according to the Land Use Decree of 1978 is vested in the governor who holds it in trust for the people. Ownership or use of urban land requires the governor's endorsed Certificate of Occupancy [C of O], or Governor's consent for any transaction including mortgages, while rural land requires a Statutory Right of Occupancy issued by Local Government Chairman. It is the prerogative of the governor to determine the extent of urban land in the state that will require his consent or C of O. The Land Use Decree of 1978 and other regulatory policies have created serious problems for residential property development in Nigeria. Among these problems with direct and indirect implications on housing finance are:

- High cost of land which ranges from N5 million ($30,000) to N500 million ($1.8million) between Epe, Ikorodu, Ikeja, Ikoyi in Lagos, Abuja, Port Harcourt, Warri and Kano.
- Delay on the part of states to issue Certificate of Occupancy.
- High consent charges for transfer of interest. These include fees payable as professional fees, stamp duty, capital gain tax and registration charge. These are usually more than 50% of land value (Nubi 2001).
- Dual payment for land, first to the landowner called 'omo onile's' and secondly to the government for registration of title.
- Endless court injunctions over ownership, which often delay projects for years. When ownership is effectually determined, the developer could be ordered off the site thereby loosing huge investment. Unfortunately, a Certificate of Occupancy issued by the governor does not confer ownership, but the root of title as determined by the court.
- Non recognition of private property development companies in the Land Use Act of 1978 which limited large land holding to agricultural use alone
- Political insecurity of the Certificate of Occupancy due to Governors power to revoke allocation.
- Since the act conceded the land to the state, compensation after revocation is limited to the development on such land excluding the residual value of the land. The statutory valuation method in this case is Cost of Replacement, which ignores the land value. Compensating only for physical development on land in accordance to the decree creates a disincentive to investment especially in areas where land alone is worth millions of Naira.

5.4. Managerial/Entrepreneurial Constraints

The real estate developers in Nigeria often experience high labour turnover and high-level filtration of qualified manpower and labour to other more attractive employment sectors such as banking/finance industry. This can be attributed to the low volume of projects, which trickles in seasonally. Most developers are idle for most part of the year or for some years and building teams are often put together when there is a project to be executed and quickly disbanded as soon as the project is completed. Managerial and entrepreneurial advancement are also impeded by increased entrepreneur risk due to the volatile nature of the Nigerian economy. This is exacerbated by the fact that most companies are sole proprietorships and family businesses disallowing the development of sound management structure devoid of the owner's interference.

6. Conclusion

In Nigeria today, the private sector controls about 70 –90% of total housing stock. However, private individuals who build incrementally at informal level causing multiplication of substandard housing, housing collapse and slum, dominate the private sector. This has contributed to the shortfall in housing supply, as this does not allow for housing industrialization and the benefits accruable from scale of production. The only way out of the housing dilemma is industrialisation and privatisation of housing which can only be achieved through the re-engineering of housing development companies. Taking a cue from the banking sector, development companies should be made to recapitalize, go into merger and finally go public to take advantage of the growth in the capital market and create access to the international market.

From the study, it is clear that the problems facing the property development companies in Nigeria are complex. The significance of their contribution to national housing stock cannot be disputed. They should therefore be encouraged to deliver more housing units to the nation. This study has hence suggested a number of useful remedies to activate their operations. This sub-sector should be equipped and supported to meet the housing deficit, especially the one created by the Government's withdrawal from the direct construction of houses:

- The growth of the Pension Fund to over 1trillion Naira in the last four years is unprecedented in the history of capital accumulation in the country. The Pension Fund Act allows 40% of the Fund to be invested in Real Estate Sector. But this can only be through Bond, Mortgage Back Securities (MBS) and Real Estate Investment Trust (REIT). It is unfortunate that government is yet to give legal support to these instruments. This should be done without further delay;
- Amendment of the Land Use Decree, especially the controversial and regressive sections e.g. sections on revocation, acquisition and compensation, lease holding and Governor's Consent;
- The use of a geographical information system – computer software for land and property management to remove the existing bottleneck in the processing of Certificate of Occupancy process and transfer of right in land.;
- Providing land to real development companies at encouraging terms;
- Subsidising infrastructure costs of development companies, including water, electricity, telephone and roads;
- Compulsory housing loans to staff of medium and large companies to boost demand for development properties;
- Removing tax on mortgage repayment to encourage and boost demand for house purchase;
- Reducing of construction costs and encouraging a better building industry through housing standardisation, mass construction to enjoy the advantage of economy of scale, promotion of local building materials and mobilising end users into Cooperatives and Associations;
- Creation of a business environment that is friendly to aspiring real estate investors;
- Need for regular census to have statistics of housing stock;
- Implementation of the 1991 National Housing Policy; and
- Government should embark upon affordability gap financing to ensure spread and marketability of the houses developed.

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