PROBLEM AND PROSPECTS OF A UNITED KINGDOM BASED INVESTOR ACQUIRING A PORTFOLIO OF REAL ESTATE ASSETS IN NIGERIA IN 2016

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INTRODUCTION

Real estate is fundamental to all human development and the bedrock of all activities by man. Almost all forms of business require some form of real estate (Babalakin, 2004). The paper refers to real estate investment as the commission of capital, labour, entrepreneurship and materials to land in expectation of optimum future returns. It involves the purchase, ownership, management, rental and/or sale of real estate for profit (Alfred, 2014). The real estate industry is a major receptacle of foreign direct investment and the extent of its development determines the extent to which it can contribute and buoy a nation's economy. Investment therein is generally recognized as a key diversifier of portfolio and sure hedge against inflation.

Usually, one significant factor influencing investors' decision to diversify real estate investment is risk. Certain properties that are well-occupied and contain long-term leases will have very stable income streams and perform like annuity or low risk bond investments (Stammers, 2016). Therefore, in consideration of risk, a rational investor may prefer long term investments in real estate so as to reduce impact of risk. In doing so, the investor normally goes for a location which enjoys a stable political and economic environment to ensure security of capital. This decision may come at an opportunity cost of tapping into real estate gains from inflationary periods. Therefore, in consideration of these elements, an investor may choose to diversify his real estate portfolio across various countries as each country offers unique opportunities and threats to the investment. Study by Eichholtz (1997) shows that international real estate investment provides additional diversification benefits over international stocks. One such scenario is a UK investor contemplating diversification of his real estate assets through an expedition into the Nigerian real estate market. The paper focuses on the problem and prospects of a United Kingdom based investor acquiring a portfolio of real estate assets in Nigeria in 2016.

THE REAL ESTATE INDUSTRY IN NIGERIA

According to Knight Frank's recent Africa Report (2015), international investors are increasingly looking for opportunities in Africa's real estate markets (Ejimofo, 2015). The report suggests that in the past year alone, property searches from outside Nigeria have increase from under 30 percent to well over 45 percent of all searches on Knight Frank website. This suggests a wave of serious interest from international real estate portfolio observers in the Nigerian property market.

One may ponder the intricacies of the real estate industry in Nigeria and its ability to draw such attention. Going by Ejimofo's (2015) assertion that the primary drivers of increasing investor interest in the industry are positive macroeconomics and stability; this increased attention may not be unconnected with the status of the Nigerian economy as Africa's biggest economy. A development which has been aided by diversification into agriculture, telecommunication, banking and real estate.

Lending credence, a 2015 report by Detail Commercial Solicitors on the Nigerian real estate sector opines as follows:

"The Nigerian Real Estate Sector has recorded steady and consistent growth over the last four years becoming one of the greatest contributors to the Nation's rebased GDP from the non-oil sector - having contributed 8.03% and 11% in 2013 and 2014 respectively. The market which is currently valued at approximately N6.5 Trillion is estimated to grow at an average of 10% over the next few years. The major growth drivers in the sector have been credited to: an increased inflow of foreign investment (especially from South Africa, MEA and the United States); increased institutional investment from local companies including PFAs and Mutual Funds; the growing population of High Net Worth Individuals; and the targeted intervention of the Federal Government in the housing finance sector."

Astoundingly, there is renewed confidence in the industry, particularly from local investors, high demand from a young aspiring population, rapid urbanization and increased rural-urban migration. According to Ejimofo (2015), the impact of this development could be negative due to mounting pressure on infrastructure with government struggling to keep up with the demand pressure. The implication is rising costs of real estate investment as investors bear the burden of not just providing real estate but necessary infrastructure and basic amenities such as roads, street lights, water, security etc.

Despite these challenges which is a prevalence in other developing countries, the Nigerian real estate industry is filled with promise. Over 75% of property seekers are looking for rental accommodation in Nigeria with about 35 percent of such properties available (Lamudi Real Estate Report, 2015). This shows a very strong demand for the residential market. The fast rate of population growth coupled with the significantly slower supply rate of housing in Nigeria has led to a startling housing deficit of millions of units. This inevitably led to sharp increases in rent prices. The reality is a call for more real estate investment to satisfy the existing demand while this demographical segment (75%) of real estate demand may graduate from property renters to buyers of real estate adding more vibrancy to the market. However, a casual observer will still find that the bulk of interest in the Nigerian real estate industry centers mainly on its residential and commercial sectors.

The real estate industry in Nigeria is not filled with flowers and roses as investors have witnessed fraudsters, inflation of values, speculative pricing and stringent land policies. Such land policies encourage long term lease of properties instead of outright and absolute freehold interest with an *infinitum* term. The unpredictability of the land use act and its susceptibility to hijack by corrupt elements in government is another issue worthy of consideration. This act is seen by most real estate stakeholders as the primary constraint on the growth of the sector, as red tape around acquisition significantly slows down projects and increases costs (Ejimofo, 2015). The market is very imperfect in nature and due to the poor communication and power infrastructure, it is difficult to coordinate activities simultaneously.

Other features of the Nigerian property market are surging rents, significant housing deficits, and over-regulation; these transform the Nigerian property market into a matrix of opportunity and unique challenges, which only optimistic investors would be able to successfully convert into viable, long-term profits.

INVESTING IN THE NIGERIAN REAL ESTATE INDUSTRY: ISSUES TO PONDER

Africa's economy is growing and rapidly so. Nigeria occupies a key place in this exponential growth as the biggest economy in the continent. As the most populous country in Africa, the seventh most populous country in the world offers a strategic market for all manner of foreign investments. One of such markets is the real estate industry. In recent years the real estate industry in Nigeria has been among the world’s fastest growing, forecast to have expanded by 13% in 2014 on the back of a diverse array of demand drivers, including substantial state investment in infrastructure, rising levels of foreign direct investment and rapidly increasing urbanisation rates (Oxford Business Group, 2016). Lending credence, a recent research by PricewaterhouseCoopers (PwC) suggests that Nigeria's real estate industry value is going to hit $13.65 Billion by 2016 (Emiedafe, 2015).

With surging rents, significant housing deficits, and over-regulation, the Nigerian property market is a matrix of opportunity and unique challenges, which only optimistic investors would be able to successfully convert into viable, long-term profits. Without doubt, this is a clear indication that Nigeria real estate industry is viable and rapidly expanding. This rapid expansion has led to a continuing upward trend fueled by rising per capita incomes (due to the recent increase in the national minimum wage), steadily increasing foreign direct investment, urbanisation and strong corporate demand. According to the Oxford report, Nigerian authorities have launched a host of initiatives aimed at addressing many of the industry's steepest challenges – high building costs, delays in public contract payments, lateness in project delivery, lack of a national building code, reliance on state infrastructure projects and poor quality standards. The efficacy of these schemes has yet to be confirmed in real terms. Likewise, the fact that local and foreign developers have carried out a large number of projects in the industry in recent years, demand has continued to outpace delivery at a worrying trend. This worrisome trend reveals that housing in Nigeria has been undersupplied thus leading to a deficit in residential markets as well as high-quality office spaces.

Despite a range of pressing challenges, Nigeria's real estate sector is set to continue expanding in future, albeit at a slower pace than over the past decade (Oxford Business Group, 2016). This assertion is consistent with a World Bank report (2015) which has projected that despite its current fiscal travails occasioned by huge losses of revenue on crude oil exports, Nigeria would begin to experience economic growth recovery as from next year. The report notes that although the nation's economy would suffer, growth is expected to rebound in 2016 and beyond. Given the passage of the budget with its attendant increase in capital expenditure allocation, it is expected that a significant improvement will be recorded in the provision of infrastructure and diversification of the economy. This prediction is predicated on the expected impact of the reforms to diversify the economy. A situation that will open up new areas and markets which invariably expands the boundaries of real estate investment.

Notwithstanding the sugar coatings of investing in the industry, a prospective foreign investor will still be faced with a myriad of issues with significant influence on their decision making. A brief review of these issues arises:

- ***Weakening Local Currency***

A lot about currency risk in the world of overseas property investment has been prevalent in the international real estate portfolio discourse. This is occasioned by the frequency of volatility experienced in the foreign exchange market and the present instability in oil pricing. This is a crucial consideration for a foreign investor with plans for the Nigerian real estate industry given that oil remains the major foreign exchange earner for the country. It is no longer news that the fall in oil prices has negatively affected the Naira, significantly diminishing its spending power relative to the dollar.

Ceteris paribus, an investor from the UK with aspirations of purchasing a portfolio of real estate assets in the Nigerian real estate industry with foreign currency in the present economic dispensation will need fewer outlay to come up with the purchase price; since the dollar or pound will buy more of the naira. Therefore, he intends to reap from the currency risk and given the positive forecasts of an economic revival for Nigeria, such investor may likely make a huge profit from any future sale if timed rightly.

- ***Stringent Property Laws***

Through the enactment of the NIPC Act No. 15 (2005), Nigeria opened up all sectors of the Nigerian economy to foreign participation except those businesses contained in the negative list. However, in many states in Nigeria, foreigners cannot generally acquire any interest or right in or over land unless the transaction under which the interest or right is acquired has been previously approved by the Governor in writing (Ogba, 2013). That consent is customarily granted upon the payment of prescribed fees and satisfaction of certain other conditions.

- ***Taxation***

In Nigeria, the most common taxes relevant to the real estate industry are capital gains tax (10%), withholding tax (5% - 10%), tenement rating and stamp duties (assessed and payable on a nominal or ad valorem basis). The problem with real estate taxation in Nigeria is its susceptibility to corruption which may lead to overpaying or double-taxation especially with Nigeria's precarious current ranking by Transparency International.

- ***Infrastructure Decay***

Almost all parts of the country have problems with steady power supply, inadequate housing, poor transport system and bad network of roads (Ogba, 2013). The implication is that the investor will likely partake in government's responsibilities of providing basic amenities which support his real estate investment. Such additions to the cost of investment include provision of portable water supply, backup electricity and security, sanitation services etc.

PROSPECTS OF A UK BASED INVESTOR ACQUIRING A PORTFOLIO OF REAL ESTATE ASSETS IN NIGERIA

The International Monetary Fund has forecast that over the next few years, around 70% of world growth will come from developing countries. Emerging economies - such as Nigeria, Indonesia, the Philippines, Saudi Arabia and Mexico - are expected to see significant growth over the coming decade (Lamudi, 2015). The emerging markets present an impressive number of opportunities for investors. Foreign Direct Investment Intelligence (2013) reports that Africa saw an increase of 10.76% in inward capital investment from 2012 to 2013, attracting $51.98 billion; and according to the report, the top five sectors by capital investment in 2013 were: coal, oil and natural gas; communications; renewable energy; business services; and real estate (Lamudi, 2015).

Nigeria is renowned for her abundant mineral resources and oil reserves. This outlook for great investment and future growth has been recognised globally. Goldman Sachs Economic Group ranked Nigeria as one of the next eleven (N-11), after the BRICS countries. The BRICS and N-11 are emerging economies presently experiencing rapid economic growth. Nigeria, the 12th global producer of petroleum is also ranked the 26th best economy in the world in terms of GDP in 2014 thus making it the largest economy in Africa. Also, a number of countries expected to become economic powerhouses of the future, have been grouped into the so-called MINT – Mexico, Indonesia, Nigeria and Turkey – and PINE countries - the Philippines, Indonesia, Nigeria and Ethiopia. *Note the recurring factor in each – Nigeria.* The characteristics of these countries are growing population combined with significant industrial capacity (Enghbal, 2008).

This young population, increasing wealth and economic stability and attractive geographical locations make these particularly good options for investment, infrastructure development, and construction.

The Nigerian population of over 170 million has witnessed 60% growth rate between 1990 to date and this is indicative that the market growth will provide more customers (Enghbal, 2008). Also, the fact that Nigeria has recorded major deficits in housing can only be music to the ears of an avid investor. Lending credence to the foregoing, Oteh (2011) concurs with the assertion that the shortfall of housing in Nigeria is estimated as 17 million, requiring an investment of N59.5trn ($380b) net of investment multiplier and this represents 180% of the country's GDP. This is surely not a burden the government can bear alone.

Ideally, there are several reasons to include real estate in a multi-asset portfolio, including potential enhancement, risk diversification, long-term inflation protection, income generation and low volatility. All these advantages of real estate investment hold sway in Nigeria and as such investment in real estate in Nigeria has the potential of creating stability in an investment portfolio. As well as having attractive rent prices for landlords and similar investors, the Nigerian property market also provides attractive returns on investment that cannot be ignored by investors seeking to purchase property in a nation where an investment in real estate can bring returns of 30-35%. The high-end Lagos market, for example, illustrates the potential for profitable investments with properties selling for $1.37 million. However, from the perspective of a UK investor considering the Nigerian real estate market, certain prospects abound as follows:

- **Great Demand for Real Estate**

Odusote (2008) in a study on Stimulating Nigerian emerging Real Estate Markets Investment Opportunities through the Public Sector put total rooms in 4 or 5-star hotels in Lagos at 1200 rooms to service Lagos state population of over 14 million people. The study shows quality of service at 85% to 90% and daily average rates of about $300 per night. This yields revenue per available room (REVPAR) of about $270 as compared to $220 in New York, $240 in Paris and $250 in London. Similarly, in the aviation sector, Nigeria has only one airport in Lagos, Abuja and Port Harcourt. The airports are always congested as the facilities are inadequate. Now this is a far cry of 3 in Moscow, 5 in London and 3 in Berlin. This implies indeed that Nigeria is in dire need of real estate investment in all the economic sectors.

“According to the World Bank, Nigeria has annual estimated average urbanisation rate of 3.75 per cent per year for the period 2010–2015, with a total of 47 per cent of the country’s population currently living in urban areas. Driven by demographic trends and urbanisation, Nigeria’s population is rising rapidly at a time when population growth is slowing in other global regions. Nigeria is projected to be 440 million by 2050, hence the recent burgeoning middle-class urban populations will need far more housing and the influx of migrants into Nigeria will drive house appreciation.” This will certainly drive the demand for real estate. Unprecedented shifts in population will drive changes in demand for real estate which constitutes 54 per cent of the world’s wealth.

- **Currency Exchange Rate**

Currency exchange rates affect how much one pays for goods whether locally (especially for imported goods) or internationally. In this era of globalization, from a Nigerian perspective; imported goods are as commonplace, or sometimes even more commonplace, than those produced domestically. A weaker domestic currency means that the price one pays for foreign goods will generally rise significantly. As a corollary, a stronger domestic currency may reduce the prices of foreign goods to some extent. The latter represents the plight of any UK investor considering a portfolio of real estate assets in Nigeria. Convivially, purchasing a portfolio of real estate assets in Nigeria today with pounds or dollars is tantamount to Black Friday shopping.

- **Favourable Real Estate Taxes**

A country’s tax regime is always a key factor for any investor considering moving into new markets (Sackin, 2013). A survey by Kirkuk (2013) shows that Britons pay the heaviest property taxes in the world with property taxes a significant 4.1% of the British GDP. A comparative review of the tax system in the UK and Nigeria is presented in table 1:

Table 1: Comparative Review of Taxes in UK and Nigeria

UK Tax System	Nigeria Tax System
Capital Gains Tax = 10% - 40%	Capital Gains Tax = 10%
VAT = 17.5%	VAT = 5%
Inheritance Tax = 40%; except by spouse	Inheritance Tax = 10%
Stamp Duties = 3% of purchase price	Stamp Duties = 2%
Withholding Tax = 20%	Withholding Tax = 5% - 10%

Source: PKF Worldwide Tax Guide (2013). www.pkf.com

Table 1 shows that investors stand to pay far lesser tax in Nigeria than in the UK. Therefore, considering the tax differences between the two countries, a UK investor will surely pay lesser tax on his real estate portfolio than in the UK.

PROBLEM FACED BY A UK INVESTOR IN THE ACQUISITION OF A PORTFOLIO OF REAL ESTATE INVESTMENTS IN NIGERIA

In some ways, Nigeria looks like a real-estate investor's dream. Africa's largest economy has an emerging middle class eager to shop in modern stores and is attracting many of the world's largest companies, which need offices. The country has a shortage of all types of modern space, raising the likelihood that the market will favor landlords for years to come. However, there also are drawbacks to investing in Nigerian property. For starters, the country ranked 96 out of 97—one above Sudan—in the Jones Lang LaSalle (2012) global real-estate transparency index, which tracks the ease and confidence investors have in buying commercial real estate in a given country. The result is a market that is seeing an increase in deals with high price tags from opportunistic funds willing to take a chance on Nigeria's potential but the world's largest and most established investors continue to steer clear of the country.

Most of the investors who are active in the country are either local players or foreign funds that specialize in Africa. "You're not going to get the European pension money here" soon, says Mark Bradford, chairman of property agent Jones Lang LaSalle in sub-Saharan Africa. "There's not much of a market [for them] here yet, but the potential is huge." One of the many challenges facing foreign real-estate investors is the paucity of market data. Unlike most other markets, investors can have a hard time finding statistics with basic information such as deal prices, supply, leasing activity and property ownership. Some other problems bedeviling the Nigerian real estate industry are:

- **Level of Government Interference**

Since the real estate industry is the live-wire of every economy, prudent government interference is highly welcome. However, government is a system and problems usually arise when individuals step out of the system to impose policies which may be for personal gain. Such is the abuse suffered by Nigeria's main land policy, the Land Use Act (1978) which has been used to encroach on people's land without concrete evidence on its subsequent use for public welfare. This has created a major risk in land ownership in Nigeria, a phenomenon that is also riddled with problems given that ownership of real estate in Nigeria is only subject to a lease of 99 years.

- **Real Estate Financing**

The contribution of mortgage finances to Nigeria's GDP is close to negligible with real estate contributing less than 5% and mortgage loans and advances at 0.5% of GDP (World Bank, 2008). Real estate investment is capital intensive, yet investors in Nigeria are mostly faced with stringent requirements in accessing funds such as hidden charges and this has led to the abandonment of a number of real estate projects before completion.

- **Title**

The investor would find that it is not really easy to obtain title to property in Nigeria. About 90% of properties in Nigeria do not have valid titles due to difficulties in obtaining such (Ewumi, 2014). Note that obtaining a title still does not guarantee land ownership in Nigeria since government lays claim to all land in the territory. Therefore, titles to land only refer right of occupancy and it is pertinent to note that properties without valid title cannot be used to access loan.

- **Corruption**

Normally, to get things done in Nigeria, certain hands must be greased. This is a major problem in Nigeria as personal interests seem to have overtaken patriotic obligations. An investor that is not willing to play ball may be left at the roadside while such illegal payments add to the cost of real estate investment. Also, certain builders may be distracted by quick money and lose focus in what matters, thereby leading to the use of substandard materials which may occasion building collapse as is almost persistently witnessed in Lagos and Onitsha.

- **Infrastructural Decay**

As earlier pointed out in this paper, the real estate investor in Nigeria may end up taking up the roles of government in the provision of basic infrastructure to support his investment. This is not ideal and adds to the cost of investment.

- **Taxation**

While this was bandied around as a prospect in this paper, probity will not be achieved if its constraints are not likewise mentioned. Real estate investors in Nigeria are subjected to multiple taxations such as development levy, income tax, building plan approval levy, property tax, land use tax, and we also have cases whereby real estate investors are expected to pay renovation tax whenever they want to renovate their properties.

BRIEF REVIEW OF FOREIGN REAL ESTATE INVESTMENTS IN NIGERIA

We conclude by conducting a brief review of the performance of foreign real estate investments in Nigeria. The foreign players in the country include Actis LLP, a London-based private-equity firm with $1.7 billion invested in Africa. Its Nigeria projects include the Ikeja City Mall, a 307,000-square-foot mall in Lagos. The development, which cost $100 million, opened in 2011 and currently is occupied with tenants such as Africa's largest food retailer Shoprite Holdings Ltd. and Samsung Electronics Co.

The encouraging performance of the Ikeja City Mall has led to further investment in the sector. Actis also, is spending about $100 million to develop the 194,000 square-foot Heritage Place office building in Lagos. "Nigeria from an international perspective has attracted more interest over the last two or three years," says David Morley, head of real estate at Actis. Another good example of foreign investors real estate investment in Nigeria is the Abuja World Trade Centre, a 37-storey building valued at $1bn currently been built on 6.102 hectares, construction is still on going along Constitution Road, Central Business District. The foreign investor is First Intercontinental Limited, which is a subsidary of Churchgate investment limited.

In conclusion, around 58 million people will move to cities in sub-Saharan Africa in the current decade, according to a UN report. Nigeria is at the heart of this urbanization. The country's economy, powered by a booming oil-and-gas industry, is expected to expand by 6.6% in 2016—significantly above the average for the region. Lagos is predicted to reach a population of 20 million by 2020, up from just under 8 million at the last census in 2006, which would make it one of the world's biggest cities. The paper recommends that the prospects outweigh the problems for any serious and avid investor. Diversification of real estate assets is also recommended as a panacea.

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