Appraisal of Financing Strategies in Housing Development in Nigeria

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Abstract

Interest in financing strategies is of importance in dwindling and recessive economies like Nigeria. There is need to understand the degree of risk associated with different financing strategies to be able to choose one whose risks can be more easily transferred or mitigated. This study aimed at appraising existing financing strategies in housing development in Nigeria. The objectives of the study were to identify preferred financing strategies for housing development, determine the relationship of preferred strategies with degree of risk associated with them and determine effect of financing strategies on housing development. A survey research design was adopted with questionnaires administered in Abuja and Kaduna to construction professionals. Data were ranked using mean scores and analyzed using regression and ANOVA. The findings showed the most preferred financing strategy in facilitating housing development is the public private partnership. The findings also show a strong association (R value of 0.651) between the degree of preference and degree of associated risks. Furthermore the findings established that financing strategies have significant effect on housing development in Nigeria. The study concludes that some innovative forms of the public private partnership and their application in housing development are yet to be understood. The study recommends that in order to enhance sustainability in housing development, Nigerian construction professionals should promote strategies that are inclusive in terms of value addition to housing development, and those strategies that help in repositioning and re-strengthening of financial institutions as well as strategies that offer investment incentives.

Keywords: *Financing strategies, Housing development, Preference, Risks, Sustainability.*

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Background to the Study

Housing development generally refers to the satisfaction of the basic human need for shelter. Due to the huge capital outlay involved, government alone cannot provide adequate housing for its citizens thus both governments and the private sector are looking for easily accessible capital that would satisfy both the long and short term housing development goals. Though the private sector has taken the gauntlet of complementing government's effort in housing development, it is also faced with financial limitations. Innovative financing strategies are therefore emerging and need to be understood to become relevant in our society. One of these strategies is project financing which has been defined as a specialized funding structure that relies on the future cash flow of a project as primary source of repayment, and holds the project's assets, rights and interests as collateral security (Switala, 2005). It has been noted that the creation of appropriate avenues for access to adequate housing (good quality housing) is a social service for which all tiers of government are constitutionally responsible and accountable (Ugonabo and Emoh, 2013). According to Ugonabo and Emoh (2013), the scale, types, and quality of houses built by the public and private developers reflect the level to which fairness and equity is attained in wealth redistribution and resources utilization. In the same vein, Burnett (2006) pointed out that access to credit has been restricted because of stringent lending conditions, payment of high interest rates or difficult collateral securities. In addition, the mortgage institutions insist on some form of savings referred to as credit or bonds, on medium or long term to worthy customers. Most financial institutions believe that it is both risky and administratively expensive to lend to construction firms, including real estate developers (Waziri & Roosli, 2013). It has been noted that a housing developer as an entrepreneur ought to be committed to assuming the risks of mass housing production in advance of sale (Mabogunje, 2007). It is in this light that this paper seeks to find strategies that can help the Nigerian society and the construction industry in particular to meet up with the housing development target through identifying alternative financing sources and strategies that can boost the housing supply.

Objectives of the Study

The aim of the study was to appraise the financing strategies in housing development in Nigeria.

The objectives of the study were:

i. To identify the preferred financing strategies facilitating housing development.
ii. To determine the relationship between degree of preference of financing strategies and the degree of associated risks.
iii. To determine the effect of financing strategies on housing development.

Hypothesis

Ho: There is no significant relationship between preference for financing strategies for housing development and their associated risks.

Ho: Financing strategies have no significant effect on housing development in Nigeria.

Statement of the Problem

Housing inadequacy has been a source of concern to the general population. It is reported that nearly half of Nigeria's population live in cities, with 80% living in slums (Daniel, Wapwera, Akande, Musa & Aliyu, 2015). This has created a dare need for private investors to be encouraged to augment government developmental efforts especially for middle and low income earners. Furthermore, the dearth of housing has been attributed majorly to lack or limited access to finance and high cost of land registration and titling (Mabogunje, 2007). The dismal performance of Nigerian mortgage industry in particular and other financial institutions have contributed to the non effectiveness in addressing the challenge of housing finance. The mortgage sector's aggregate loans total assets falls far below the best practices standard of at least 70% as stipulated by the Central Bank of Nigeria (Jiboye, 2011 & Adetiloye 2013). The situation has left developers to seek for interventions in the housing sector from diverse sources.

The housing backlog in Nigeria is estimated at 14 million units requiring about N49 trillion ($326 billion) to bridge the housing deficit (Efin A and Fin Mark Trust, 2010). Due to the complex nature of construction processes, the financing housing project is perceived by lenders to have greater risk than other forms of lending. Housing development requires large funding right from its inception or conceptualization stage up to the commissioning stage, though at varying degrees. Thus the ability of a financier to evaluate a project as viable does not depend only on the availability of funds, but is function of time, interest rate and risk. The search for innovative financing strategies for has become imperative in the struggle to meet the housing demand. It is to this end that the study seeks to appraise financing strategies in housing development with the view to ensure both financial and housing sustainability in Nigeria.

Existing Strategies of Financing for Housing Development

The common sources of housing finance in our Nigeria are:

National Housing Fund (NHF): Due to the large quantities of housing need, coupled with the huge amount of funds required to meet such need, the government mobilized for a special fund to exclusively tackle the housing problem through a form of savings required by law. Thus the National Housing Fund (NHF) was envisaged to mobilize resources (mandatory savings) from the worker, private and public employers of labour, statutory allocation by the Federal Government and building societies under a broad policy formulated and regulated by government to provide shelter for Nigeria workers (Ibimulua & Ibitoye, 2015). The NHF was expected to add stability to the housing finance system by reducing reliance on government interventions (Adedokun, Akinradewo, Adegoke, &. Abiola-Falemu, 2011). It requires that the three tiers of government (Federal, State and Local Governments) contribute at least 2.5% of their annual revenues into the NHF as the policy works mainly by pooling resources from both the public and private sectors. The Law provides for 4% interest on workers contribution to the Fund. This low interest rate has been attributed as one of the reasons why other financial institutions are reluctant to invest in the fund since it makes it competitively less profitable. So far, the NHF in Nigeria has been assessed to have performed unsatisfactorily in the provision of housing (Adedokun, Akinradewo, Adegoke & Abiola-Falemu, 2012 & Adetiloye, 2013).

Formal Financial Institutions: These include mortgage financing, loans from commercial banks, merchant banks, thrift and credit societies and insurance firms. Mortgage lending is primarily used to finance private ownership of residential and commercial property, while loans from other financial institutions like commercial and merchant banks are usually preferred for other forms of new construction projects. The traditional source of obtaining finance housing development has been though bank loans which can be on l o n g t e r m , medium term or short term or even as overdrafts. However, many persons, e s p e c i a l l y corporate real estate developers have been confronted with challenges in efficient and sustainable credit delivery to the housing development from these financial institutions (Waziri & Roosli, 2013). These challenges include the demand to meet strict loan requirements and collaterals which often most firms are unable to meet. The inability to provide these collaterals thus becomes an impediment to financial assistance. In addition, the firms are expected to pay interest on loans at very high rates since most banks consider it administratively expensive and risky to lend to construction firms and estate developers (Nedwick & Burnett, 2015). These stringent lending conditions are felt more by new firms with no established track records and thus suffer more setbacks in seeking external financing. The banks in turn face higher risk of lending to small borrowers and makes lend at higher costs or in small amounts. Eventually, this causes the banks to lose edge in an increasingly competitive market filling up with other non-bank lenders (Kolawole, 2014).

Equity Capital: Equity can come from the developer equity, outside equity or a combination of both. That is it may be raised from an individual's personal savings or released from joint ventures, consortiums, corporate organizations, mezzanine fund partners, and some other form of passive partners such as business angels. Generally, it is funding which is sourced from savings of private or public individuals, profits of enterprises and mezzanine debt, or other lower-risk equity investment such as pre-sale arrangements. Financing of construction development always involves at least two equity parties: the developer, who is also the active partner, and the equity investor or mezzanine lender. The equity parties provide 20% to 35% equity requirement sought by most construction lenders financing residential and commercial development projects (Wikipedia, 2017). The use of Mezzanine capital is relatively new in Nigeria. They have higher risks but pay higher yields and are usually used in project finance to provide credit enhancement for more senior debt issues. Mezzanine lending is said to acts as equity or debt depending on the capital structure of the deal and the needs of the developer for the particular project and helps to bridge the gap between the mortgage and outside equity (Kane, 2001). Mezzanine lenders will also often charge an arrangement fee, payable upfront at the closing of the transaction. These arrangement fees contribute the least return, and their purposes are primarily to cover administrative costs or as an incentive to complete the transaction (Kane, 2004).

Public Private Partnerships (PPP): Private agencies have been involved in delivering housing units in Nigeria such as the Abuja Property and Development Company (APDC), the Lagos State Property Development company (LSPDC) and several other development and investment companies in the states of the federation. Another example is the Nigeria Mortgage Refinance Company (NMRC) initiated by the Federal Ministry of Finance in collaboration with the Central Bank of Nigeria (CBN), Federal Ministry of Lands, Housing & Urban Development (FMLHUD) and the World Bank/IFC as a PPP arrangement to augment the housing production (Aluko, 2009). The PPP strategy is adopted when project sponsors want to minimize financing costs and make their tenders more competitive. It involves selection of appropriate mix of equity and debt financing, and the identification of appropriate finance sources (Liu, Love, Smith, Mathew & Sing 2016).

Project Financing Strategy: This is a financing strategy that is especially attractive to the private sector since firms can fund major projects off the balance sheet. It is a loan structure that relies primarily on the project's cash flow for repayment, with the project's assets, rights and interests held as secondary security or collateral. Basically, it is the financing of long-term infrastructure development based on a non-recourse or limited recourse financial structure, in which debt and equity used to finance the project are paid back from the cash flow generated by the project (Investopedia, 2016). The lenders' recourse is limited primarily or entirely to the project's assets, including completion and performance guarantees and bonds, in case the project company defaults.

Methodology

The survey research design was adopted for the study. Data were gathered by means of semi-structured interviews and structured questionnaires in Kaduna and Abuja being among the fastest developing capitals in Nigeria, and where activities of the estate developers are significantly noticeable. Seventy (70) questionnaires were administered to the respondents in the study area. Forty (40) were administered in Abuja while thirty (30) questionnaires were administered in Kaduna and a total 64 questionnaires were retrieved, representing a response rate of 91%. Purposive sampling was used to select construction professionals in tertiary institutions, organizations and private firms who were deemed to be knowledgeable in housing finance. Data were analysed using mean scores, regression analysis and ANOVA. Findings were presented in charts and Tables and the results were discussed.

Result of the Study

This study was aimed at appraisal of the project finance strategies in housing development in Nigeria, using a case study of Abuja and Kaduna cities. Figure 1 shows the percentage of the different professions that took part in the study.

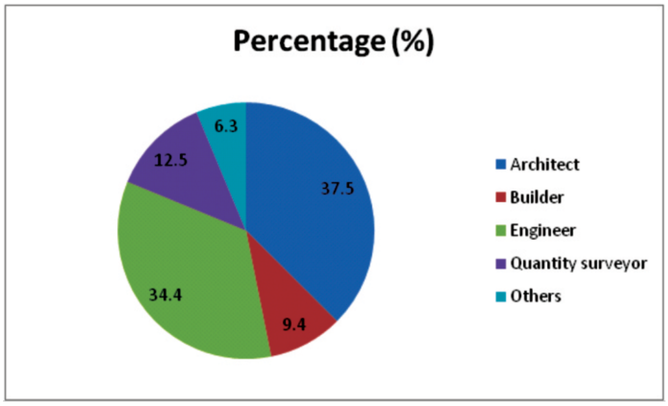

Figure 1 Profession of Respondents

When the respondents were asked to rank existing strategies of housing finance in order of preference in facilitating housing development, the findings obtained is presented in Table 1. Table 1 shows the frequencies of degree of preference by respondents. The mean scores were computes and the items were ranked in accordance with the mean scores. The item with the highest mean score was the first in the rank order. The Public Private Partnership (PPP) financing strategy was ranked by over 59% of the respondents as the most preferred financing strategy in enhancing housing development in Nigeria, with an overall mean of 4.50.

Table 1: Ranking of Preference of Finance Strategies in Housing Development

S/N	Financing Strategy	Degree of Preference					
		5	4	3	2	1	Rank order
1	Public Private partnership	38	20	6	0	0	1st
Ii	Equity Release Schemes	32	28	4	0	0	2nd
Iii	Syndication of Resources	10	28	13	7	6	8th
Iv	Foreign Loans	8	20	18	12	6	12th
V	Foreign Direct Investment	12	10	16	20	8	13th
Vi	Project Finance	12	16	9	20	7	9th
Vii	Joint Ventures	20	32	6	2	4	6th
Viii	Mortgage Loans	12	32	13	5	2	4th
Ix	Loan from commercial banks	22	31	8	3	0	3rd
X	Merchant banks	2	23	27	7	5	11th
Xi	Trust schemes	18	24	8	2	12	7th
Xii	Loans from thrift and credit society	14	26	12	12	0	5th
Xiii	National Housing Fund	4	18	10	22	10	15th
Xiv	Loan from Pension Trust funds	2	10	19	21	12	18th
Xv	Loans from insurance firms	6	18	9	12	17	16th
xvi	Government bonds	20	21	11	8	4	5th
Xvii	Grants (Individuals & multilateral development banks)	14	19	9	15	7	6th
Xviii	Site and Services Schemes	4	17	12	23	8	14th
Xix	Supplier Credit / business angels	14	11	18	17	4	10th
Xx	Mezzanine capital	6	18	22	12	6	17th

This shows that the role of PPP's in housing development has within a relatively short time been recognized and accepted as very suitable for facilitating housing development. The release of equity by investors or release of personal savings was ranked second most important source of financing for housing development with a mean score of 4.44. Equity release depends on investors' profit or individuals' effort in savings which depends on the standard of living of citizenry. The trouble however, is how much personal savings can be made available to facilitate adequate housing development? Reliance on this financing strategy necessitates significant economic improvement in the environment of corporate investors and individuals. The third most important ranked financing strategy was found to be the use of loans from commercial banks which had a mean score of 4.13. Loans from mortgage institutions was ranked 4th with a mean score of 3.73. While loans from thrift and credit societies and the use of government bonds were both ranked 5th with means scores of 3.70. It is surprising that in spite of the upsurge of innovating financing strategies such as project financing, the traditional methods of financing housing development through financial institutions were still being given a high priority by the respondents. However, it must be borne in mind that dependence on financial institutions and the use of government bonds may not offer sustainable financing because it makes housing development to be vulnerable to swings in monetary policy or inflation. Ebimobowei & Wisdom (2012) are of the same view and have opined that the use of bonds is appropriation of future income to solve a current need. Project financing was ranked 9th by respondents with a mean score of 3.23. The low ranking of this strategy might be due to lack understanding of the strategy, which is another form of public private partnership, where return on investment is determined by the project's success. The least preferred financing strategies by respondents were the use of insurance loans, use of forward sale arrangements and the use of loans from the pension's trust fund which had the means scores of 2.66, 2.41 and 1.94 respectively. The low ranking may likely have been due to the fact that the respondents are not very conversant with them or that respondents might have found them to be ineffective in housing development due to some constraints or high risk content.

The study also determined the relationship between the degree of preference of the financing strategies and the degree of risk associated with the strategies as ranked by respondents using regression analysis and the summary regression model result is presented on Table 2. The R-value = 0.651 and R^2 = 0.424. The R value indicates that there is a positive linear relationship between degree of preference for financing strategies and their degree of associated risks in housing development in Nigeria. The value of R^2 indicates that the explanatory power of the independent sub-variable is 0.424, meaning that 42.4% of the variation in preference for financing strategies is explained by the model. The value of the R^2 indicates that there is significant relationship between preference for financial strategies and their associated risks in housing development.

Table 2: Model of Relationship between the degree of Preference of Financing Strategies and their degree of Associated Risks in Housing Development

Model Summary				
Model	**R**	**R^2**	**Adjusted R^2**	**Std Error of the Estimate**
1	0.651[a]	0.424	0.357	4.74577

To determine the effect of financing strategies on housing development, the analysis of variance (ANOVA) was computed and presented on Table 3.

Table 3: ANOVA[b]

Model	Sum of Squares	Df	Mean Square	F	Sig.
Regression	282.120	2	141.060	6.263	0.009[b]
Residual	382.880	17	22.522		
Total	**665.000**	**19**			

a. Predictors: (Constant), financing strategies
b. Dependent Variable: Housing Development in Nigeria

Table 3 shows the result of ANOVA test which revealed that *financing* strategies have significant effect on housing development in Nigeria. Since the P- value actual is 0.009 is less than 5% level of significance. This implies that the model was significant. The coefficients of the model are shown on Table 4.

Table 4: Coefficients[a]

Model	Coefficients		Standardized Coefficients	t	Sig
	B	Std Error	Beta		
1. (Constant)	21.313	7.163		2.976	0.008
Risks	1.685	1.106	0.281	1.524	0.005
Strategies	-5.325	1.649	-0.595	-3.230	0.046

a. Dependent Variable: Housing Development in Nigeria

The coefficients on Table show the result of effect of financing strategies on the housing development in Nigeria. The result indicates that *financing strategies* have significant effect on housing development in Nigeria

Conclusion

There is a slight shift in the preference of financing strategies for housing development from the complete reliance on loans from financial institutions to public private partnership financing. However, there are more forms of innovative financing strategies not yet understood and adopted for housing development in Nigeria. These include the use of strategies such as project financing and the use of mezzanine capital to provide alternative financing based on risk sharing amongst project partners with abilities to manage and control risks.

The relationship between degree of preference for financing strategies and the associated risks reveals risks considerations are strong influences in accessing finance for housing development. Therefore, imbibing risk management culture is pertinent to successful housing development in Nigeria. The varying financial risks in the financing strategies include credit risk, reliability, transparency, information timing, economic risks, currency trends, profit, competition risk and any legal risk in the lending transaction.

To sustainable housing development is dependent on the use of sustainable financing strategies. However, no single financing strategy is best for all circumstance of housing development. Thus it becomes paramount that stakeholders in housing development are able to recognize and rightly appreciate the degree of risk associated with the different financing strategies to be able to adopt those strategies that help appropriate or mitigate risk and at same time facilitate efficient housing development.

Recommendation

The study recommends that to achieve sustainability in housing development, there is need for strategies that are inclusive in terms of value addition to housing development, re-positioning and re-strengthening of financial institutions by all tiers of government and strategies that offer incentives for elected officials to invest in housing development.

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