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Challenges of International Real Estate Investment in an Emerging Economy: The Nigerian Experience

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Abstract
Many real estate investors are increasingly looking to invest internationally for reasons of portfolio diversification and the search for higher risk adjusted returns than can be achieved in their domestic markets and in doing that, the emerging economies provide them with great opportunities. These opportunities are seldomly out- weighed by numerous challenges. This paper therefore evaluates the challenges of international real estate investment in an emerging economies, especially NigeriaWith the great improvement in the political situation of Nigeria, coupled with the large size of the country and thus economies, which resulted to sustained Foreign Direct ~~I~~nvestment (FDI) and Gross Domestic Product (GDP) growth, and performance of other economic indicators, Nigeria is in right direction towards realizing the dream of being one of the major emerging market. These attracted international investors as stated by the foreign direct of investment (FDI) of $723.49 Million in 2015. Despite this strong economic growth and potential opportunities even within the real estate markets, international real estate investors faces such challenges like: property market transparency risk, political risk, structural risk, banking risk, currency risk, ownership structure risk.
Keywords: Challenges; International real estate; Investors; Real estate investment; Real estate market; Emerging economies

1.0 Introduction

Countries of the world may be classified into developed or under developed; and in contemporary times they may be categorized as emerging, developed or developing economies. In the opinion of Crosby and walkins (2001), in the 1970's, "less developed countries was the common term for markets that were less "developed" by objective or subjective measurement than the developed countries such as the United States, Western Europe and Japan. These markets were supposed to provide greater potential for profit and more risk from various factors. The term was felt by some people as not positive enough so the "emerging market" label was born and refers to these regions of the world that are experiencing rapid in formalization under conditions of limited or partial industrialization; although in emerging markets such as Nigeria come with much challenges. The aim of this paper is to examine the~~se~~ challenges facing international real estate investment in Nigeria with a view to proffering veritable solution to mitigate them.

1.1 Emerging market.

The term Emerging market, coined by a World Bank economist, Antoine van Agtmael in the 1980's, refers to the market activity in countries that are considered to be transiting from developing to developed nations (Gangster, 2007). Emerging market are countries that are working to restructure their economies to interface with market oriented globalization, providing opportunities for trade, technology transfers, and foreign direct investment through open door policies. These countries basically have a large population and resource base, and are abandoning traditional state interventionist policies to seek sustainable economic growth. They are the globe's fastest growing economies and play a part in contributing to the world's explosive trade growth; in time they are projected to become more significant buyers of goods and services than their industrial counterparts.
In recent times a number of institutions are recognized for trading this phenomenon of emerging market using a number of metrics. These include the Morgan Stanley Capital International (MSCI) index, the Economist, and it's ISI Emerging markets?

The MSCI index includes the following twenty five (25) markets they consider emerging: Argentina, Brazil, Chile, China, Colombia, Czech Republic, Egypt, Hungary, India, Indonesia, Israel, Jordan, Korea, Mexico, Morocco, Pakistan, Peru, Philippines, Poland, Russia, South Africa, Taiwan, Thailand and Turkey. In addition, other small markets including Estonia, Latvia, Lithuania, Romania, Slovakia, Costa Rica, Panama, Uruguay, Venezuela, Kazakhstan, Vietnam and Nigeria are also considered to be emerging markets.

Also the Global Economics papers, prepared by the firms Global Economics Group (GSGEG), on commentaries on the state of the world's economies current trends and future projections, in their 2003 paper "Dreaming with BRICS: The path to 2050".

The Group introduced Brazil, Russia, India and China as the BRIC countries forecasted to be four of the most dominant economies by the year 2050, (Odusote, 2008). This forecast was presented as a "dream", signifying, the significant hurdles these economies needed to scale to bring them to pass. Today the BRIC "dream has begun to manifest in reality as the economies of these regions continue to show rapid growth and development, attracting ever increasing amounts of Foreign Direct Investment (FDI).

GSGEG (2005), put forth another paper "How solid are the BRICS." and in it, they highlighted their forecast of the Next Eleven (N-11) emerging market of the world, slated to be among the world's top 20 Economies by the year 2050 in different capacities. The countries includes, in no particular order; Mexico, Turkey, Bangladesh, Indonesia, South Korea, Philippines, Egypt, Iran, Vietnam and Nigeria.

1.2 Distinction between an emerging economies and developing nation

What differentiate an Emerging market from a developing, or what may be considered as a "third world" Nation is primarily the Nations' ability to have sustainable, market oriented growth, foreign "investment" replaces foreign assistance."

Government of developing countries rely heavily on borrowing from institutions like the IMF and World Bank, resulting in a debt overload and severe economic imbalance. When traditional government borrowing fails to fuel the development process, countries seek equity investment from investors as a means of financing economic growth. In order to attract this foreign investment, the foundation of a market economy must be established to create a business climate that satisfies the expectations of foreign investors.

India, a country that maintained strict government control over foreign trade and investment until 1991, provides an example of a country that has opened its markets to foreign capital and trade, and consequently experienced tremendous growth as an emerging world economy.

Further along the development process, many emerging markets have evolved to be considered "developed" or "first world" nations. According to the MSCI country index, the change in the classification from an emerging to a developed market index is based on the country's relatively high level of economic and equity market development. Greece is an example of a nation that was recently upgraded to a "developed" status. Greece exceeds the GNP per capita threshold used by the world Bank to characterize high- income countries, and moreover has enacted sound economic, fiscal and monetary polices to qualify for admission to the European Economic and Monetary Union (EEMU). This has created a solid basis for increased economic and financial stability, including reduced currency risk and a lower cost of capital.

1.3 Emerging Market in Real Estate

According to Jones Lang LaSalle (JLL, 2006), cross border transactions represented 42% of total real estate investment volume, an 8% increase from the previous year. This clearly signifies the rapid globalization of real estate as an asset class much of which can be attributed to the growth in the emerging market economies. As a result of rapid GDP growth the emerging markets are expected to experience a disproportionate expansion in the real estate sector to accommodate a growing industrialized work force and the increasing demand for large quantity of assets. In 2006 alone, Russia's real estate market expanded 700%, and JLL reported strong deal flow in china, turkey Mexico and Brazil (JLL, 2007).

The word's dominant commercial real estate markets are in better shape than at any time since global financial crisis of 2008-2009. Levels of real estate investment activity are returning to pre-crisis levels and investors are moving up the risk curve into new geographies and property types. Meanwhile, corporate bodies are now executing long-term portfolio strategies and selectively extending their foot prints into market

As momentum builds across the global real estate markets, investors, developers and corporate occupiers are demanding (and expecting) ever greater levels of real estate transparency. At the same time, there is a growing recognition by governments, particularly in emerging economies, that poor real estate transparency not only hinders inward investment but also has deep impacts on the quality of life of its citizens.

There are factors that contribute to the growth in investment in real estate in emerging markets.

These are:

1.3.1 Accessibility.

The enormous real estate investment opportunity outside the USA is not a new phenomenon, as USA investors have long had a presence in Western Europe and Japan. What has changed is the increasing accessibility to emerging markets throughout the world. As the emerging economies are rapidly industrializing, they are developing strong sectors and infrastructure necessary to facilitate international investment. Currently, emerging market account for over half of world's output; and by 2050, they will account for almost 78% (Ganster, 2007). The economic growth in these markets has not only fueled the development of infrastructure needed for investment but also created investment vehicles that did not exist in the past to allow investment in these market more freely. In the late 1990s for instance, foreign investors could not invest directly in South Korea, but a change in the legal structure has significantly increased foreign capital inflows into the market (Philip & Youguo, 2006).

1.3.2 Perception

The perceived risk of a country has a strong effect on investor sentiment for that market. Investing in the emerging markets is no longer associated with the traditional notion of providing development assistance to poorer nations. As emerging market increasingly sign trade agreements to enter the global economy, capital flows are directed more toward new market opportunities and less by political consideration, reflecting the transition from dependency to global interdependency in addition an evolution of investor attitudes is also shaping the real estate investment landscape, putting emerging market in the radar of many opportunities investors.

1.3.3 Globalization Of Real Estate Providers

most of the worlds "Global" real estate brands, including Hines, Jones Lang LaSalle, CBRE and fish man speyer, in addition to the banks and funds who are financing them, have set up shop in many of the emerging market. With an increase in cross-border development and investment, and mergers of commercial real estate brokers, data reporting and order process has become more standardized, making investment more plausible for many foreign firms.

1.3.4 Technological Advances And Increase Market Transparency

The global information exchange is integrating emerging markets into the global market at a faster peace, most notably through the aid of the internet. This has a number of implications on investment from a real estate perspective. As research and brokerage firms expanded their horizons, information on practically any market can be available within minutes. Advances in space imagery from stallites and aerial photography will provide additional research analysis tools. This has resulted in improving transparency across the globe. According to Jll's 2006 global Transparency index, there have been steady improvements in transparency each year. Generally speaking, the greater a country's transparency, the easier it is to do business in the real estate sector, leading to increased real estate capital flows.

1.3.5 Trade and Globalization

The establishment of global trading blocs in North America, Europe, Pacific Rim, Asia and the Regional Trade Agreement in Eastern, West and South Africa are having a significant impact on the development of emerging countries. Trade agreement not only open up emerging economies to global capital movements, but also increasing ~~also~~ set standards for labour, environmental and fiscal policies. This contributes to the standardization of investment criteria and creates a more open market for real estate investment.

2.0 Nigeria

2.1 Country overview

Nigeria is in the Western part of Africa, in the gulf of guinea and occupies a total land area of about 923,773 sq. km, with estimated population of 158.3million people according to world gazette (2010). It is the 8th largest country in terms of population and the 32nd largest country in the world in land mass (World Bank, 2010). It shares borders with Benin Republic in the West, Niger and Chad on the north and Cameroon on the East, on the South is approximately 85km of coastline to the Atlantic Ocean. On this coast line is the Niger Delta basin of the south which has the largest River deltas in the world and is the convergence of the two major rivers in the country: the River Niger, which runs from the West, and the River Benue which runs from the East.

There are roughly three climatic regimes in the country: the tropical rainforest of the far south, the desert like climate of the far north and the savannah which accounts for everywhere else. The majority of the country falls in the last region: with a long wet season in the south, particularly the south-east, and a shorter wet season in the north (Economic intelligence unity, 2012).

The country has English language as an official language and about 250 ethnic groups with more than 500 indigenous languages making it one of the most ethnically diverse Nations in the world. Three main ethnicities dominate: the Fulani/Hausas of the North (speak~~s~~ Hausa language); the Igbos of the South East (speak~~s~~ Igbo language); and the Yorubas of the South-West (speak~~s~~ Yoruba) and they together account for about 70% of the population and these are official recognized indigenous languages. Other ethnic groups include the Ijaw, Edo, Kanuri, Ibibio, Ebira, Nupe, Urhobo, Tiv etc which collectively make up the remaining 30% of the populace. Religion in the country is primarily Christianity and Islam with a small minority of a variety of traditional deity worshipers. In particular, the Hausa/Fulani tribe of the North are Muslims, the Ibo tribe of the South-East and other minority tribes of the South-South are Christians, and the Yoruba tribe of the South-West are a mixture of Christians and Muslims The country has been under democratic dispensation since 1999, with

President Muhammadu Buhari as the president and commander-in chief of armed forces, since 29th May 2015 till date. The country runs a presidential system adopted from he United States of America. It has a bicameral legislative arms-of senate (the upper chamber) and the House of Representatives (the lower clamber). The country in made of 36 states and the federal capital territory

2.2 . Emerging Nigeria

With a total market of 17.9 million people and a GDP of 569.1 billion following the re-basing of the economy (USAID bank; 2015)-more than 60% of West Africa's GDP-Nigeria is the core of economic activity in west Africa and an important component of the economic development of the continent as a whole. It is a member of economic community of West Africans states (ECOWAS) which was formed in 1975 to promote economic integration in the region.

The economic organs of the country can be traced back to the British colonialists who used the colony as a source of raw materials, minerals and food stuffs to be exported to the Western World, first through the Royal Niger Company and eventually as an official protectorate of British Empire (wikipedia, 2013). The exports of natural resources remain today a large source of the country's revenue albeit dominated by petroleum and its derivatives. As a nation it was one of the founding members of the Organization of Petroleum Exporting Countries (OPEC), having the 11th largest proven oil reserves in the world, with a production quote of 2.53 million barrels per day. With demand for petroleum products in the world (developed and emerging markets) declining amidst limited supply this revenue generator has continue to attract the country's economic development negatively?

However, in addition to petroleum and there are other mineral resources, more than four hundred scattered all over the country (including significant amount of tin, columbite, iron ore, coal, limestone, Leal, gold, zinc, tin etc), the countries favorable climate and terrain also affords it a vast amount of arable land suitable for the cultivation of variety of produce-cocoa, palm oil, yams, cassava, sorghum, millet, corn, rice, livestock, groundnuts, cotton. If these mineral resources are properly harnessed, the countries economic condition would be positively enhanced

However, despite these vast resources and the potential for economic buoyancy, the country's historical mismanagement and political unrest has seen it fall below its potentials, leading to economic depression. This has resulted to the classification of the country by the World Bank, first as low income country in 1989 and declared poor enough to be eligible for concessional aid from the international Development Authority, and this condition persisted all the way into the 90's.

However, the Nigeria fortunes changed in recent times due to several factors, most as a result of the current democratic dispensation which has brought a fair measure of stability to the country. The new democratic governments, now committed to the country's economic development in the aftermath of decades of under-development, have affected a number of policies that have seen the country's economy grow significantly in the last 5 years with projections of continued growth.

One of these policy changes was in the area of government spending. Since 2004 the government introduced a system of basing the budget on a conservative oil price reference and by so doing detached government spending from changes in oil price. The Excess in revenue from this new system are then saved in a special account. This practice has increased the country's foreign reserves from &7.5 billion in 2003 to & 43 billion in 2012 and now 31.43 billion (CBN, 2015). It has also helped to reduced inflation to about 9.2% per annum compared to the 40% average in 1990's.

There have also been structural reforms including the privatization of 116 government enterprises between 1999 to 2014. The government owned and operated power Holding company of Nigeria, which in the past was the sole provider of power to the country was unbundled into 18 different companies of power generation, transmission and distribution. There were also massive deregulations in downstream oil sector and telecommunication sector which have all had positive results, especially the telecommunication sector. Public procurement reforms were also introduced and are estimated to have saved more than $1.5 billion since 2001 (World Bank, 2007).

Again, there have been reforms in the area of combating corruption in the country. In 2003, Nigeria was one of the first countries that adopt the Extractive Industries Transparency Initiative (EITI) to help improve the governance of the oil and gas sector. Government also instituted two bodies, the Economic and Financial Crimes Commission (EFCC) and the Independent Corrupts Practices Commission (ICPC) to battle corruptions. These have since been responsible for a number of high profile convictions of corrupt officials and the seizing, confiscation and refunding of several billion worth of assets to the federal and state governments, though they are been accused of being selective in the persecution. Nevertheless, these developments have consequently resulted in improvements in the perception of corruption in the country as measured by the World Bank Institute (WBI) index.

The effect of all these reforms has resulted in one of fastest growing economics in the world.

The Foreign Direct Investment (FDI) of $513 billion in 2010, GDP of $569.1 billion in 2014 and the sustained FDI, and GDP growth projected over the next few years, and the performance of other economic indicators, are a step in the right direction toward realizing the "Dream" of the N-11: a truly emerging market (see Table I and II) below.).

Table I: GDP growth rate comparism: Nigeria, BRIC and USA

COUNTRY	2007	2008	2009	2010	2011	2012
NIGERIA	6.2	6.8	6.6	6.3	6.2	6.2
BRAZIL	5.4	4.6	3.6	4.2	4.1	4.3
RUSSIA	8.1	7.2	6.4	6.0	5.3	3.0
INDIA	9.0	7.7	7.1	7.5	7.6	8.1
CHINA	11.9	9.8	9.0	9.2	9.0	8.6
USA	2.2	0.8	1.1	2.5	2.6	2.5

Source: Economist intelligence unit country data (2007)

Table II: Economic indicators of Nigeria: Current and future projections.

Key indicators	2012	2013	2014	2015	2016	2017
Real GDP growth (%)	6.2	6.5	7.2	6.9	7.3	7.1
Consumer price inflation (AV. %)	12.2	10.9	9.6	9.9	10.2	10.8
Budg of balance (%of GDP)	-3.0	-2.3	-2.0	-2.3	-2.0	-1.8
Current account balance (%of GDP)	2.3	0.5	0.1	0.6	1.5	1.8
commercial bank Prime rate (AV. %)	16.0	14.5	13.0	13.5	13.8	13.8
Exchange rate N:USS$(AV.)	15.7	162	168	171	173	174

Source: Economist intelligence unit country Data (2012)

3.0 Challenges of international real estate investment in Nigeria

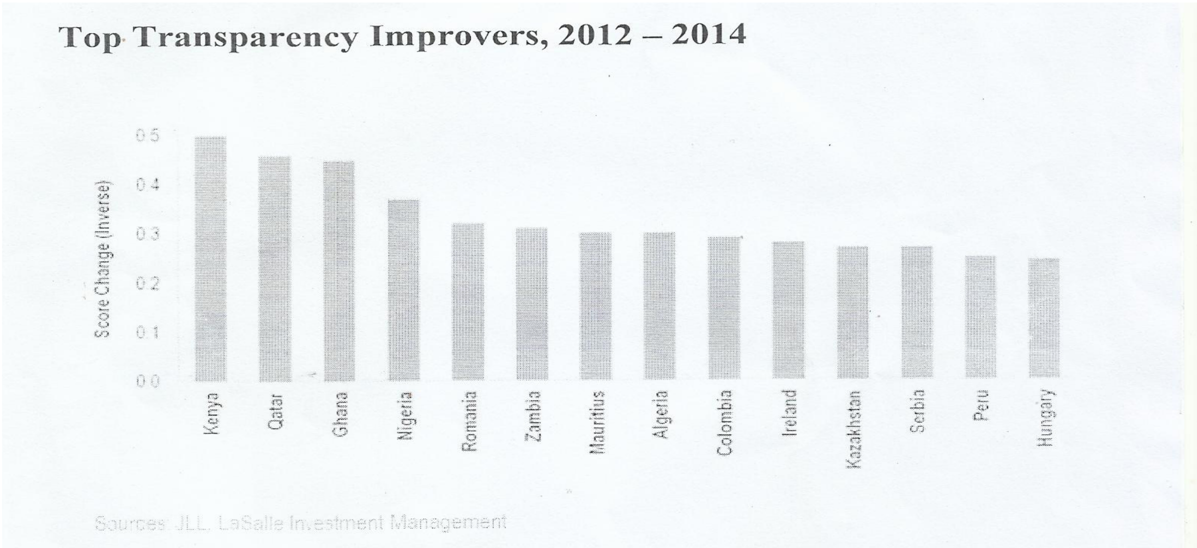
Despite the strong economic growth and potential opportunities within the real estate market in Nigeria, there are numerous challenges to international investors, just like most of emerging markets. Generally speaking, the more uncertain the returns are in a market, the higher the risk associated with the investment. While this is true in any real estate investment, the factors of this risk are escalated in foreign market when political, legal and currency factors come into play. The following challenges are faced by foreign investors in Nigeria

3.1 Property Market Transparency

One of the greatest contrasts in developed and emerging markets is the difference in "transparency", which refers to the quality and quantity of the information made available to participants, as well as the consistency of the rules and regulations with respect to property rights in ~~a~~ the market. From an investor's view point, high transparency in the market likes the US and UK not only eases the flow and reliability of information, but also makes it harder to find market inefficiencies that would earn a "risk premium". On the other hand, low transparency imposes additional risks and transaction costs

JLL's latest global real estate transparency index reveals continued progress in transparency over the past two years. Over 80% of markets have registered an improvement since 2012, although typically, increases in most markets have been 'slow but steady'. Out of 102 markets covered by the index, 14 countries including Nigeria saw a significant improvement in their overall score (see attached).

There transparency score reflects the lack of reliable current market statistics (including investment performance indexes and market data), as well as a weak record for property rights. There is also no requirement to report sale or transfers of property, and therefore many real estate transactions are not transparent to the market.



3.2 Political risk

Many foreign investors consider political risk to be one of the most determinants in real estate decision (Ganster, 2007). Country risk analysis involves an examination of the country's economic outlook and stability of its government, as well as factors including corruption and crimes. A major political risk associated with real estate investment in unstable markets is expropriation of the property by military government, or physical damage to real estate from revolution, rebellion, or civil war.

Nigeria has witnessed series of political instability until 1999. Even the present constitutional democracy does not warrant less political risk as there is still large scale corruption in the polity. Nigeria is still regarded at present as one of the most corrupt countries of the world even though President Muhammadu Buhari is currently doing every thing to change the perceptions. There are still cases of unrest and strife, caused by regional dissension, cases of militancy in the Niger Delta region, inter-tribal wars in most part of the country, kidnapping, armed robbery and Boko Haram insurgency in the North East Nigeria, leading to high political risk.
The country's political risk is at present rated as CC, depicting poor stable political environment.

3.3 Structural Real Estate Risk

Structural factor- including the size and state of country's economy have an impact on the economic risk of a real estate market (Chen&Hobbs, 2003). Larger economies are stable and capable of withstanding external economic turmoil. The country's economic stand point and its place in the world economy also have a significant affect on investment risk in that country. Nigeria with an estimated population of 179.1 million people is regarded as one of the emerging economies of the world and in fact the 8th largest country's of the world in terms of population (World Bank, 2014). The country is suppose to be among least risky countries in terms of economic structure, but lack of transparency in doing business in the country, incessant strike actions by labour unions arising from non-payment of workers salary and government policies have posed serious challenges to international real estate investors in the country. Currently, the country is rated by the Economist intelligence unit as (BB) in the Economic structure risk. This means that in spite of the size of the population of the country, it is still not economical very stable, though it got its best rating compare to other challenges or risks.

3.4 Financing Risk (Banking Risk)

Another major challenge of international real estate investment in Nigeria is the banking system. Just like most of other emerging market economies, the country's bank lending is relatively inefficient even though it is the most common source of financing for both domestic and foreign investors.

Nigeria bank lending rate has been fluctuating over the years and hovers between 15-20%, but currently at 11%. This high cost of finance is a serious impediment to international real estate investors. Most banks in Nigeria are not into long terms financing and therefore the non-availability of project real estate financial is a considerable risk. Though Nigeria operate a well-regulated banking system, with central bank of Nigeria as regulatory authority, which serves as "lender of last resort, the banking sector has suffered a series of inconsistency in term of operations. These inconsistencies have ~~has~~ resulted to the series of bank distress in Nigeria.

The inconsistency in terms of operations and regulation in the banking sector has resulted to the consolidation of banks from forty-nine (49) banks to twenty-five (25) banks in 2006 and further down to twenty-one (21) banks presently. The inconsistency in monetary policies and regulations in Nigeria is a threat to the stability of the banking sector and pose a serious challenges to international real estate investors. The country's bank sector risk is therefore rated "C", (country risk summary, 2014).

3.5 Currency Risk

The risk of currency devaluation is a threat to the stability of dollar denominated returns. Many Latin America markets have had a history of volatile currency fluctuation, and consequently devaluation remains a real risk, mostly recently seen in Argentina in 2002. Currency risk is readily applicable to Nigeria since 1986, when the government of President, Babangida devalued naira the country's local currency. The exchange rate of naira stood at #199 to $1 (Key indicators, 2015), and it is expected to worsen over the years.

Additionally, Nigeria has a legal restrictions on the transfer abroad of funds associated with capital employed in an investment and this perhaps is one of the greatest risks mitigating investment in Nigeria. The country's currency risk is consequently rated (B) and that pose a challenge to international real estate investors.

3.6 Ownership Structure Risk

The right to own or use land is a prevalent issue in many emerging markets economies. National and local governments still own a vast majority of land in many emerging markets, requiring investors to structure long term leases, a risk that some institutional investors have trouble accepting.

In Nigeria, the current law guiding the use and ownership of real estate is the Land Use Act of 1978 (Cap 202 of law of federal of Nigeria, 1990).The Act vested all land in the territory of each state in Nigeria in the Governor of that State who holds it in trust and administered for the use and common benefit of all Nigerians. The Act also stipulates that all land in the urban areas shall be under the control and management of the Governor while order land shall be under the control and management of the local government of which the land is situated. The implications of this is that individual has only possessory rights, thus individual are only entitle to right to occupancy covered by statutory or customary certificate of occupancy issued by Governor of a state or a local government chairman for land in urban area or land in rural areas respectively. These statutory or customary rights of occupancy are not easy to get, hence most properties do not have perfect titles. Generally speaking, acquisition of property and perfection of the title documents are tedious, cumbersome and costly in the country.

Another challenge is the power vested by the Act to the government to revoke right of occupancy for overriding public interest. The Act stipulated that the holders or owners of the right of occupancy will only be entitled to compensation for economic crops, trees and other unexhausted improvements (section 29(1) and there is no compensation for land. Yet another challenge arising from this is the issue of consent. For real estate development transactions, banks ~~looks~~ at the subject land as collateral, but the transaction is put at risk because of the myriad of problems under the Act. The banks are required to obtain a consent which they do at very heavy costs. The original title documents which the banks place safely in their vaults may turn out to be worthless, if the Federal Capital Territory minister's announcement to withdraw such certificate of occupancy is carried out. We witnessed such rascality from the former Federal Capital Territory minister-Mallam El- Rufai and immediate past minister- Mallam Balla Mohammed recently, with cancellation of Certificates of Occupancy and demolition of several buildings and Estates in the capital territory. Thus, many investors consider Nigeria property rights to be at considerable risk for real estate investment.

3.7 Transparency of Regulatory System

In an effort to encourage FDI, Nigeria introduced the Nigeria Investment Promotion Commission Decree No.15 of 1995.This Decree makes it possible for foreign investors to invest in any part of the Nigerian economy with or without Nigerian partners. This attracted a foreign direct investment (FDI) of $723.49 million to the country in 2015. However despite the current administration's effort to make government more transparent, corruption in Nigeria seems to have not been reduced. For real estate developers, the corruption often translate into inconsistencies in the building codes, building approvals and documentations, increasing the uncertainty and risk associated with the investment.

In a nutshell, international real estate investors is faced with challenges arising from weak property rights, regulatory inconsistencies, low transparency, currency risk, political policy inconsistencies and unstable banking system.

Conclusion

This paper has revealed that despite the strong economic growth and potential opportunities within the real estate market in Nigeria, international real estate investors still ~~faces~~ numerous challenges. The challenges are political risk, banking risk, structural risk, property market transparency risk, currency risk, ownership structure risk, legal risk and the country risk generally.

The challenges would be surmounted only with the government's ability to show a political will and be transparent in the conduct of business activities.

They should ensure the stability of the political climate and the economy through the stabilization of exchange rate, interest rate and check on inflation.

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