

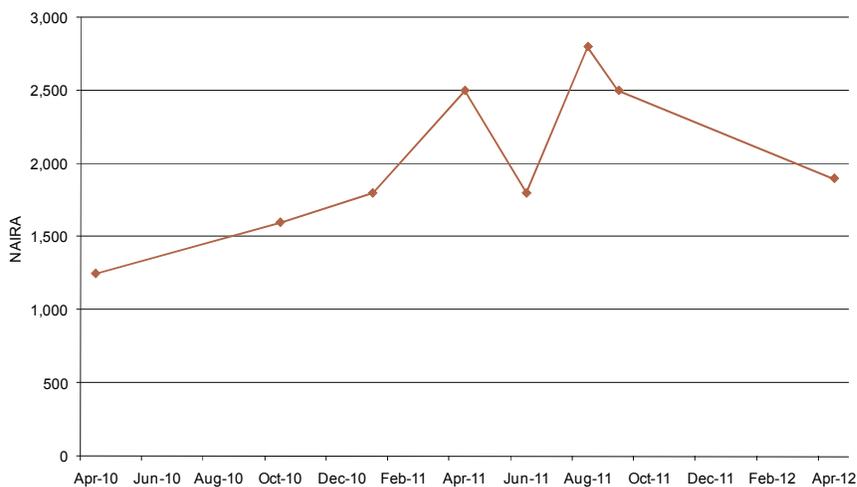
Review

We are pleased to bring you the second edition of our report which takes a detailed look at the housing development market in the Lagos metropolis. Our first report which was published just a little over two years ago, focused on the emergence of new locations for housing developments as a key factor to mitigate risk in the wake of the crisis in the financial sector. The report also highlighted the short-fall in supply of new housing stock against the state government's planned target, and the type of units delivered into the market as developers became more innovative in attracting buyers. In this issue of the report, we will continue to look at the delivery of new housing units into the market, but we will expand our scope by also focusing on those factors that affect the supply of new housing stock in Lagos. There are two factors in particular that have had significant impact on the housing development market since our last report; the rising costs of building components and real estate development finance. In this issue of the report we will also introduce the concept of Planned Construction Starts.

Rising Cost of Components

Cement is the major component in building construction. In the last two years, the price of this component has spiked well above the level of inflation prompting fears of further price increases by real estate developers. In April 2010, the price of a 50kg bag of cement which sold at N1,250 (US\$8.33) rose by 100% to N2,500 (US\$16.67) in the same period twelve months on. This spontaneous price increase took effect as the general elections were approaching in the country. Nonetheless, the price hike had a significant impact on current and planned housing projects as house builders (developers) had to review their prices and re-evaluate proposed developments due to escalating construction costs. We will see more evidence of this in another section of the report.

Figure 1 Cement Price



Source: RAC Research

After the elections, a presidential directive was given ordering all cement producers to immediately reverse the price increase of the commodity to pre-election levels and further urged to find a lasting

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solution to make the commodity more affordable to consumers. This directive was heeded upon as prices dropped briefly only for prices to peak at almost N3,000 (US\$20) in Q3 2011. According to a market survey we carried out, the price of cement currently stands at N1,950 (US\$13) as of April 2012 representing a 24% price drop from the same period a year ago but over a 50% price rise from the same period 24 months ago. Despite the best efforts of local producers to increase their production output of the component with a view to reducing importation which would ordinarily culminate in the reduction of prices on the open market, the removal of the fuel subsidy earlier in the year has cast doubts on the possibility of further price drops.

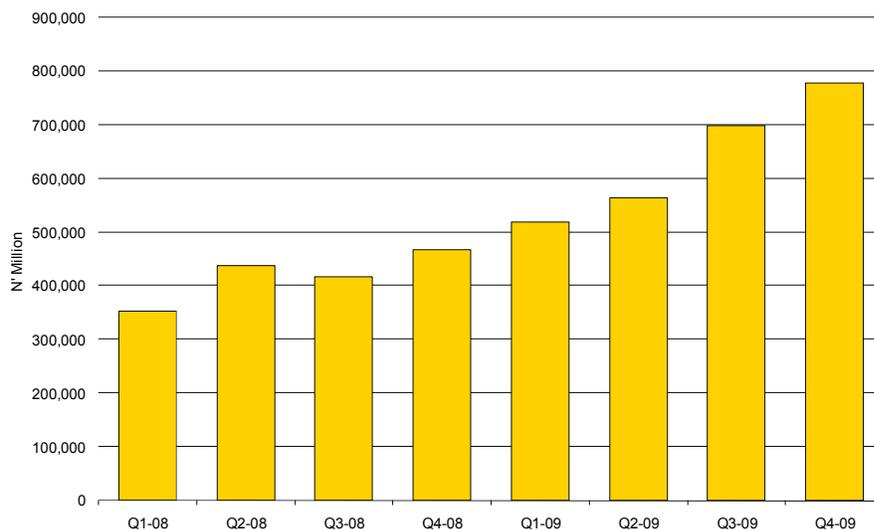
Real Estate Development Finance

Accessing development finance from financial institutions for real estate developments particularly on housing developments has now become one of the most difficult challenges facing house builders. Less than a third of new housing developments are currently being funded by banks in Lagos. Prior to the crisis in the banking industry, financial institutions were eager to fund housing developments as long as developers could provide land which would be regarded as equity.

To illustrate the robustness of the real estate and construction industry, commercial loans to the industry at the height of the construction boom in 2009 was estimated to be N2.55 trillion (US\$17 billion) according to data obtained from the Central Bank of Nigeria (CBN), this is a staggering 53% increase from the N1.67 trillion (US\$11.13 billion) recorded in the previous year.

We are unable to show the proportion of loans for housing developments particularly in Lagos due to unavailability of such data.

Figure 2 Commercial Loans



Source: RAC Research, CBN Statistical Digest

Due to the reforms in the banking sector which resulted in the credit freeze by financial institutions and in a desperate attempt to reduce exposure to development risks, lenders have now become more cautious

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in funding housing developments. There are now more stringent measures which house builders have to adhere to, if they are going to access finance from local banks to fund their developments. One of such measures is the issue of off-plan sales.

Off-plan sale is the selling of units in a housing development before construction begins on the project and such units are usually sold at a discount to attract buyers. It has now become a mandatory requirement by lenders that house builders have to achieve at least between 20%-30% off-plan sales on their proposed developments before receiving any form of finance, and also some additional capital would be required aside from the land as equity. These conditions have posed problems for house builders, particularly the small and medium firms that require funding in order to undertake new projects and are severely constrained by the strict conditions placed by the local banks. This has started to affect the number of new housing developments in the Lagos housing market as we will show below.

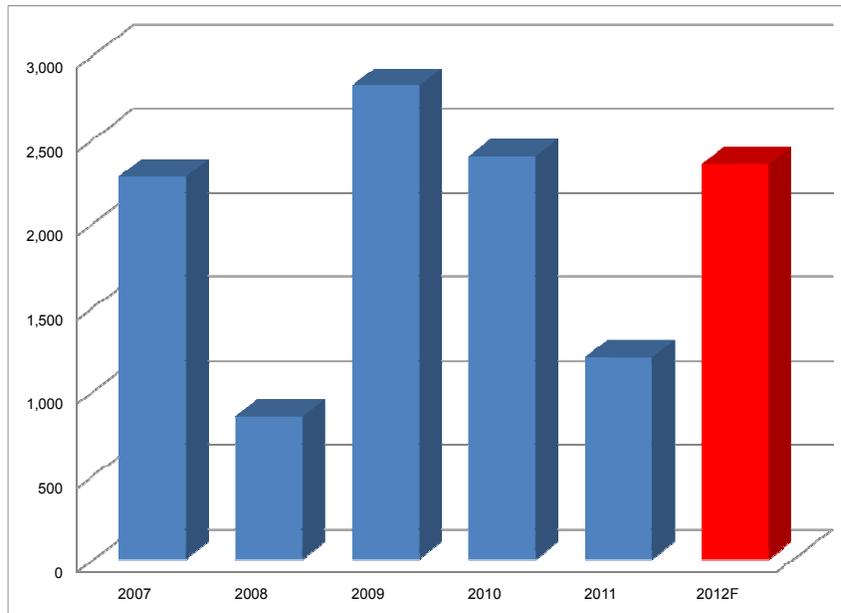
Planned Construction Starts

In this section of the report, we will be taking a close look at the number of planned new housing units to be developed on a build-to-sell basis by house builders in a particular period for the City of Lagos. This is what we refer to as "Construction Starts". We are able to provide data on planned construction starts because we regularly track new housing developments for the Lagos market. On a cautionary note, we have to emphasize that our data is strictly based on estimates of planned housing developments that feature 10 units or more as proposed by the developer. During the course of our research we have found that due to fund raising issues or lack of due diligence, on average, less than 40% of planned new units become actualized.

In 2009, there were over 2,800 planned new housing units to be located across 30 sites in various parts of Lagos ranging from the low-income areas such as Epe and Ebutte-Metta to the high-income locations such as Lekki and Ikoyi, according to our data. Some of the planned developments for this period include; Lekki - Adiva Plainfields (960 units), Epe - Sir Michael Otedola Housing Estate (362 units) and Lekki - Beach Resort Estate (227 units). This leap in the number of planned new stock follows on the heels of the low construction starts recorded in the previous year as the number of new stock dropped to under 1,000 units. This can be attributed to the stock market crash which took place over that period. In the last five years, there have been over 9,500 planned new housing units across the Lagos metropolis.

There was a slow-down in construction starts last year as the number of planned new housing stock fell to just 1,200 units in fewer than 15 residential developments in the state. This is a direct result of the factors discussed earlier, such as the rising cost of cement and access to real estate development finance. Some of the planned developments for this period include the proposed Modo Heights (450 units of flats) at Ketu and The Belvedere (375 units of terrace houses) at Lekki Phase 2.

Figure 3 Number of Planned New Units



Source: RAC Research

This year we forecast that the number of planned new housing stock will be just short of 2,500 units and be almost at par with 2010 levels even as cement prices remain high. One of the factors for the surge in planned new stock is the Lagos State Government (LASG), which has approved plans for the development of over 70 housing projects across the state with contracts already awarded to some construction firms late last year. The housing developments will be located in different parts of the city, such as Ikorodu, Surulere, Ogba, Ibeju-Lekki, Ikeja and Igando to name but a few. Whilst this is a good initiative on the part of the government, the number of planned units will not make any significant impact to the number of delivered stock that is required on annual basis in Lagos as will be presented below.

Supply of New Housing Stock

Despite efforts by the LASG to boost the housing stock in the state, the delivery of new housing stock into the market still falls short of target. In 2009, the LASG entered into an agreement with several private house builders under the Public Private Partnership (PPP) initiative to deliver 15,000 new housing units in the state over the next five years. The terms of the agreement stated that the state government would provide land and an enabling environment for house builders whose responsibility would be to provide the financial resources to undertake developments.

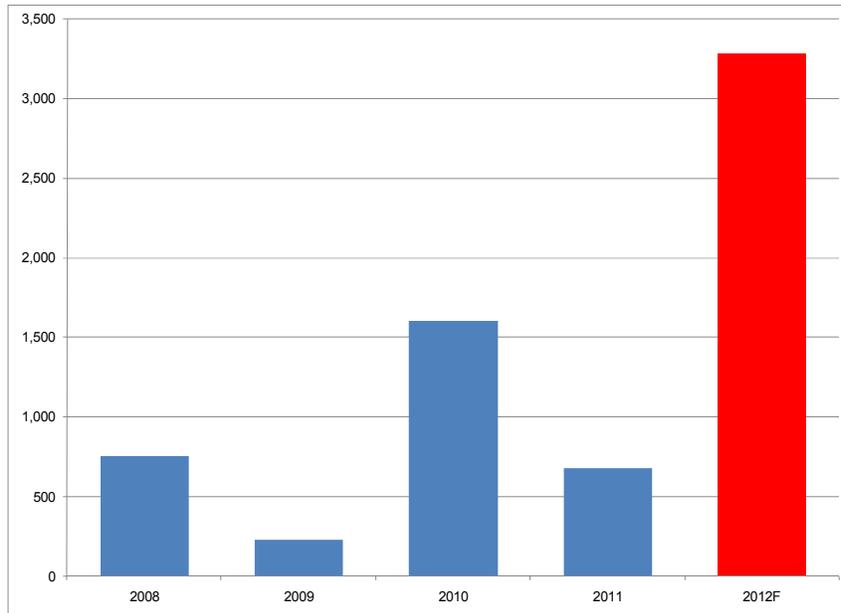
Based on our data, less than 3,000 new housing stock has been delivered into the market in the last 3 years. That is an average of 830 units per year. One of the reasons for the persistent low supply of housing stock is that quite a number house builders have difficulty in accessing finance from financial institutions and with very limited cash flow are unable to embark on new developments. Several on-going developments have either been suspended halfway through construction or cancelled due to the depletion of funds. According to our data, between 2010 and 2011, the LASG delivered 814 housing units through the Lagos State Ministry of Housing and its property division LSDPC. Some of the developments that

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were delivered include the Lekki Peninsula Residential Scheme II Ogombo (90 units), Igbogbo Housing Scheme, Ikorodu (256 units) and Sir Michael Otedola Housing Estate, Epe (362 units).

Figure 4 Number of Delivered Units



Source: RAC Research

Approximately 1,600 units were delivered into the market in 2010 as several large scale private housing projects that had been in the pipeline for the past 2 - 3 years finally got completed. Among such housing developments that were delivered are Friends Colony Lekki (230 units), County City Estate Agege (174 units) and King's Court Shasa (200 units). Of the 1,600 units that were delivered in this period, 76% of the units were multi-family units i.e. apartments while the remaining 24% were single-family units i.e. detached, semi-detached and terrace houses. We expect to see a large number of developments that have been in the pipeline to finally reach completion in 2012. Hence we estimate that slightly under 3,300 units will be delivered into the Lagos housing market for this year.

In our last report we stated that the Lagos housing market required an annual supply of 224,000 new units to meet its housing needs. Achieving this figure would be a herculean task as the annual supply of new stock is considerably low as shown above in Figure 4. Based on our analysis on the future supply of new housing stock, we reached the conclusion that on an annual basis, Lagos would require 25,000 planned new units to deliver 10,000 units annually to the market in order to ease the acute housing deficit in the state which is estimated at 5 million units.

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Important Note

Finally, in accordance with our normal practice, we would state that this report is for general informative purposes only and does not constitute a formal valuation, appraisal or recommendation. It may not be published, reproduced or quoted in part or in whole, nor may it be used as a basis for any contract, prospectus, agreement or other document without prior consent, which will not be unreasonably withheld.

Our findings are based on the assumptions given. As is customary with market studies, our findings should be regarded as valid for a limited period of time and should be subject to examination at regular intervals.

Whilst every effort has been made to ensure that the data contained in it is correct, no responsibility can be taken for omissions or erroneous data provided by a third party or due to information being unavailable or inaccessible during the research period. The estimates and conclusions contained in this report have been conscientiously prepared in the light of our experience in the property market and information that we were able to collect, but their accuracy is in no way guaranteed.