A rare case of good socialism

Creating a broad-based mortgage system

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Key Recommendations

- Government policy should increase the incentive for more Nigerians to contribute to the National Housing Fund (NHF) by raising the interest rate from 6% to 12%, thus generating more funds to finance more mortgages.
- There is need to transform the National Housing Fund (NHF) into a fund for repurchasing mortgage loans from banks.
- Policy should target 16% mortgage rate by making only mortgages at this rate eligible for repurchase by the NHF; NHF funds should subsidize the 4% difference.
- Contribution to the NHF should be made a pre-condition for accessing rent-subsidized public housing developed through NHF-financed slum redevelopment schemes. This should encourage lower-income Nigerians to contribute.

In April 2019, President Muhammadu Buhari refused assent to the National Housing Fund (Establishment) Act of 2018 ("the new NHF Act"). The private sector decried what it described as yet another attempt to cripple the free market with a socialist intervention. While the proposed legislation is indeed inadequate, the reaction to it also leaves much to be desired. The Act fails to recognise that government interventions are critical in developing a housing (supply) system that meets demand while encouraging economic development. Useful discussions and efficient housing policy solutions depend on a conceptual separation of two distinct elements in the debate. The first element involves government interventions to assist the private financial and housing markets to deliver homes. The second element encompasses another set of interventions to ease the housing conditions low-income Nigerians face. The lack of distinction between these two objectives and the tools required to meet them has made interventions in housing, including the NHF Act, wasteful and ineffective.

Houses: a befuddling asset class

Nigeria has a 17 million "housing gap", according to a 2012 assessment. This paper attempts a rough illustration of the housing needs of different classes of Nigerians as a basis to critique extant policies aimed at addressing these needs. In addition, it sets out recommendations on addressing Nigeria's housing gap. In Lagos it is possible to find couples with steady incomes paying about N1 million in rent whilst saving N15 to N40 million to buy a house that costs between N35 and N90 million. The couple may have a "driver" who lives in a single bedroom with a wife and three children in a slum with poor sanitation. The driver's parents could be living in a village in a "house" built of mud that lacks any modern amenities such as electricity or water. In many Western and developing markets government interventions have sought to address the housing needs of equivalent classes of citizens since the early 1900s.

These types of housing needs are correlated, as solving one helps to alleviate another category. Yet policy solutions must target specific problems and particular objectives. Professionals and members of the middle class hoping to buy homes that cost N20 million upwards do not need "low-cost" housing. The solution to the housing problems of villagers living in mud houses or migrants sleeping in the open in cities such as Lagos or Kaduna lies in jobs that generate economic development, rather than in a plan to build 750 000 houses across Nigeria, as announced in 2017 by the former Minister of Power, Works and Housing. On the other hand, urban dwellers, from low-income workers to young professionals and civil servants who earn N30 000-N250 000 per month, face severe housing problems that are amenable to direct state policy interventions. Houses are a complex asset class; a home is the most expensive item that 99% of people will ever purchase. Yet, governments everywhere readily accept an obligation to help keep rents low, even for the middle classes, and get people on "the property ladder". For example, America's Department of Housing and Urban Development's (HUD)

Federal Rental Assistance schemes offering grants, tax credits, or reduced-interest loans to build or rehabilitate rental housing. Also, the Help to Buy scheme in the UK which offers first-time home buyers discounts on property taxes, mortgage interest and insurance. The critical question is which housing policies should assist low-income earners and which should support private markets to better deliver houses to those Nigerians who can afford them. The appropriate subsidy levels required to meet each policy objective, the incentives they provide to businesses and individuals, and the social and economic pay-offs are important considerations. Government interventions in the housing sector have been devoid of these calculations.

Serving the privileged in the name of the poor

The housing problem first got the government's attention when the investment of massive oil receipts triggered migration to Nigeria's urban centres and slums proliferated. According to the Third National

Development Plan, “There is no area of social service where the urban worker in Nigeria now needs relief more desperately than in housing.” It is unclear to what extent the 1975 document influenced housing policies, but it did reflect a deeply ingrained tendency to treat housing policy as an aid to the poor rather than a market-enabling intervention. This thinking has persisted despite its glaring failures. Nigeria's housing policy interventions are briefly described below, along with explanations on why they have failed.

Low-cost housing: Housing authorities were set up at the federal and state level to build “low-cost” housing for poor Nigerians, identified in policy documents as suffering under the country's housing shortage. They were to buy these houses unaided by mortgages. The federal and state government subsidised inputs, hence the cost of these houses was below market price. But these governments had limited funds to build low-cost housing, hence no more than 2% of Nigerians ever benefitted. Wealthier Nigerians often acquired the houses through bribes or influence. The poorest Nigerians lacked the means to acquire “low-cost” even if such houses were available.

Federal and state agencies also use the government's power to acquire land and to plan and regulate urban development. This often includes appropriating land for "government-scheme" estates where the rich and influential acquire grossly under-priced plots through "allocation" and later resell at market rates. Professor Paul Collier of Oxford University noted in a 2012 *Business Day* article that individuals rather than the Nigerian government captured the vast capital gains from urban land.

Unfortunately, this grossly inefficient "low-cost" approach has been adapted to the rhetorical transition to the private sector-led development model. State and federal government agencies allocate hectares of land to developers under bizarre public-private partnership (PPP) schemes for nominal sums far below the market value. According to a 2011 study of the PPP model in Abuja, developers mostly sell off the plots at market prices and buyers build palatial duplexes, mansions and bungalows rather than the intended low-cost housing.

Mortgage saving scheme: In 1991 Nigeria created the National Housing Fund (NHF), into which workers were to pay 2.5% of their salaries. Insurance firms had to invest 10% of their non-life and 20% of their life funds in the NHF and banks 10% of their loan books, an obligation that was largely ignored. Many workers, including all civil servants in some states, also do not contribute to the NHF, mainly because they earn less than is required to buy homes and so will never need these loans. The total NHF contribution of workers who do not take out mortgages is paid back at retirement, but only at a 6% interest rate. The NHF is also irrelevant to acquiring homes in Nigeria's main cities, which form the most liquid real estate market in the country. Designed to aid buyers of "low-cost" houses, no more than N5 million could be borrowed from the NHF until 2010, when its threshold was raised to N15 million. Like other interventions, the NHF is irrelevant to most Nigerians planning to buy their own homes. Nigeria's mortgage to gross domestic product (GDP) ratio is a mere 0.2%, compared to 2% in Ghana, 31% in South Africa, 32% in Malaysia and 80% in the United Kingdom.

A comparison of Nigeria's housing policies with those of Singapore highlights the structural deficiency of the former. In Singapore, the Housing Development Board (HBD), the public housing authority, builds homes specifically for the poor. These are modest high-rise buildings with ground-floor toilets that were erected after the demolition of slums. The flats were offered for rent rather than being sold as “low-cost” accommodation to the poor, who lacked the means to purchase them. The Singaporean government also used a Land Acquisition Act to appropriate land for public housing, but it paid near-market rates as compensation. Singapore also established the Central Provident Fund (CPF) into which workers and employers jointly contributed 25% of an employee's salary to fund his/her medical insurance and pension. In 1968, the government allowed Singaporeans to draw from their CPF savings to pay deposits on the HBD flats they lived in, or on new ones. The CPF also supported long-term mortgage lending. The HBD started to develop more expensive houses from the early 1970s. The Singaporean model thus adapted to changing economic conditions. Countries like

Malaysia have successfully copied it. Today, about 85% of Singaporeans live in accommodation developed by the state-owned housing corporation. The CPF is often described as the bedrock of Singapore's “market-based welfare” system.

Recent developments

National Mortgage Refinance Company (NMRC): The NMRC acts as an intermediary between Nigerian mortgage lenders (banks) and capital markets. Promoted by the Ministry of Finance, it was founded in 2013 as a wholly private institution regulated by the Security and Exchange Commission and the Central Bank of Nigeria. The NMRC raises funds on international capital markets with which it buys mortgages from Nigerian banks, thus improving liquidity. It is a significant but modest development that seems to have reduced the mortgage rate by 1-2%. However, it lacks the potential of Nigeria's NHF or Singapore's CPF to mobilise mass savings. Mortgages bought by the NMRC have a tenure of less than five years, which is the limit of the risk appetites among domestic lenders and foreign capital markets.

LagosHoms: This scheme was established in 2012 to aid first-time homebuyers in Lagos State acquire mortgages subsidised by the state government (at 12%). The State Housing Corporation constructs eligible homes. LagosHoms is innovative as it recognises that financing is the major barrier to acquiring homes. It has elements that are very useful in improving on the federal government's NHF, namely a 12% rate (which is closer to the market rate) and the use of public funds to subsidise interest rates. Yet critically, unlike the NMRC, it is a modest intervention. It focuses on using government resources to help the less well-off, if not the poor, rather than developing what is by far Nigeria's largest construction and real estate market, centred in Lagos. A crucial failing is that the eligible houses are built by a government agency. LagosHoms houses are won through balloting, a rationing system imposed by the limited government funds available to build homes or subsidise mortgages. The huge potential of private investment in urban renewal projects, which would improve housing supply and conditions as well as unlock public revenues, has not been explored. The NMRC has survived the change in government at the federal level because it is a government-initiated private sector initiative. In contrast, LagosHoms has been severely hampered by the change in governors, even though Lagos's ruling party has remained effectively the same. The scheme has been poorly funded since former Governor Babatunde Fashola, who had initiated it, left office.

The new NHF Act: The proposed Act sought to improve on the 1992 National Housing Fund Act, attempting to boost NHF funding by increasing mandatory contributions from banks and insurance companies and demanding a new 2.5% pre-tax profit from cement-producing firms. However, the amended legislation failed to address key weaknesses in the extant NHF that has ensured that an overwhelming majority of Nigerians neither contribute to the fund nor use it for its intended purpose.

The main criticisms of the proposed amendment are:

1. It is a forceful diversion of funds from individuals and companies.
2. The 2.5% NHF contribution from salaries is unfair and regressive; it is 25% of the payroll tax of workers on minimum wage and only 2% for most professionals.
3. It will prevent funds from banking and insurance companies from going to more rewarding investments.
4. The 2.5% profit contribution by cement firms will make houses more expensive, as cement firms will pass this cost on to consumers.
5. The housing sector cannot be developed at the expense of other sectors.

As seen from the Singapore example, "forced saving" is a useful method to pool funds for mortgage lending in a market with low levels of liquidity. According to Ayo Teriba (see article in this volume), deposits in Nigerian banks are 20% of GDP, compared to 40–200% in peer countries, meaning that Nigerian banks have little capital to lend. Critics of the proposed NHF amendment reject this principle rather than its design. It is erroneous to argue, as they do, that fine-tuning the relevant housing sector policies and regulations such as the Land Use Act without making non-market public interventions will spur the market to supply affordable, longer-term mortgages.

A broad-based mortgage system can and should be funded by taxing other sectors because of the powerful impetus it could give to construction, real estate, finance and other sectors. In 2003 Chee Wong and Adriel Yap wrote that Singapore's "public housing has, to a great extent, contributed towards lowering wages, higher productivity, political and social stability, thereby attracting international capital and manufacturing investment". The contribution that a well-designed NHF would make to economic growth would be several times greater than the sums "forcefully diverted" from banks and cement companies.

Conclusion and recommendations

The goal of a housing policy is to help people live in safe, affordable accommodation. A housing policy should help as many people as possible to acquire their own homes, and others to spend as little as possible of their income on paying rent. It should also provide safe shelters for those too poor to pay for any accommodation. The easier it is for more people to buy or build their own homes, the bigger the supply of housing becomes and the more rents will drop. A mortgage system that assists the majority of the population to acquire homes is indispensable to boost the supply of housing. Creating a pool of mortgage funds through a "forced saving" scheme is unavoidable to establish such a broad-based mortgage system.

Recommendations for a more effective NHF:

1. Ensure a genuine focus on the poor: Make the NHF contributions of lower-income and informal sector workers and others who cannot afford to buy homes a condition of rent-subsidised public housing. Such a step should form part of a slum clearance and urban renewal programme. This not only resolves the NHF equity problem but also creates an incentive for broad-based compliance. Furthermore, savings in the NHF should pay out at rate not below the return on market-based pension schemes for people who cannot access a mortgage or seek subsidised public accommodation.

2. **Make it affordable to make it mass:** A choice has to be made between helping a few thousand Nigerians obtain 30-year mortgages at a 6% interest rate and helping millions of Nigerians obtain 15-year mortgages at 12%. The latter is more affordable for the government and will attract more investments in a reformed NHF (either as savers or buyers of government housing bonds).

3. **Merge the NMRC and the Federal Mortgage Bank of Nigeria**: The NHF contribution should be used to buy off mortgage loans from banks; a role the NMRC currently plays with a smaller but more expensive pool of capital. This will combine the advantages of mobilising funds through public policy with the private sector's allocative efficiency. Banks should be left to assess who needs a mortgage and the risk involved.

4. **Make it as easy as walking in**: Banks are in the best position to determine who needs and can finance a mortgage. They should be allowed to open "NHF accounts" and keep deposits in these for three months before transferring them to the NHF. Banks should routinely offer 12% mortgages to their customers over 15-year terms because they have information about their intention to buy houses and a bigger pool of funds to repurchase the mortgage loans

5. **Interest rate subsidy:** High interest rates reflect the shallow nature of Nigeria's financial markets, as well as of inflation. Mobilising funds into the NHF will reduce the cost of long-term mortgages by deepening the market. Yet, for the first four to five years of the operations of the reformed NHF, it may be necessary to subsidise interest rates, e.g. the 4% difference between the 16% market rate and the target 12% NHF rate. (This signals 16% to the banks as the mortgage-lending rate eligible for repurchase by the NHF.) Some NHF funds would be set aside for subsidising interest rates, to be complemented by government grants as in the LagosHoms scheme.

6. **Urban Planning & Infrastructure Fund:** High rents and cost of land, as well as various accommodation problems, are tied to the lack of transport infrastructure and not to the inadequacy (the number) of houses per se. So, just building more houses can never be an adequate solution. Connectivity is just as important. A portion of NHF funds should be set aside for eradicating slums and improving transport connectivity. This will have the effect of smoothening house prices (between well-planned and unplanned urban areas) and generating considerable taxes through urban renewal projects.