ALITHEIA CAPITAL

Market Update

Monday, February 16, 2009

THE FINANCIAL CRISIS - Birthing New Solutions In The Real Estate Landscape

The global financial crisis is no longer headline news, neither is the impact of the crisis on the Nigerian economy. But, how do all of these impact on real estate related industries and property products? Falling capital values, scarcity of debt financing, and risk to rental income from companies cutting back on budgets are some of the emerging industry trends that are directly attributable to the financial crisis. When the dust finally settles, we can expect that the Nigerian Real Estate Sector will have experienced significant and largely permanent changes. This edition of the market update presents our predictions of the industry post the meltdown, specifically as it relates to sector participants and property products.

DEVELOPERS AND CONSTRUCTION COMPANIES – Building Survival Strategies

With a shrinking credit market, cautious equity investors, fewer buyers and growing construction costs, we expect that Developers will look more inward at opportunities to maximize their current holding, create liquidity and cash realization deals, and limiting expansion strategies except to acquire distressed assets at depressed prices.

Developers will also work closely with their design teams seeking better design efficiencies and standardisation of components with a view to reducing construction costs and managing timelines more tightly. We also expect more aggressive marketing strategies (including mock-up/sample units) in a bid to attract buyers for more competitively priced products. We anticipate that there will be a number of interesting joint ventures between Developers (such as Union Homes, UPDC et al on 1004 Estates), with the possibility of smaller Developers forming strategic alliances and mergers.

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While data on annual construction output in the country is not readily available, we expect a significant decline in new construction activity, particularly from the private sector. Construction Companies which have traditionally serviced the private sector may expand their market reach to compete for public projects. With fewer projects and fiercer competition, construction companies will consider a cut in profit to keep workforce and equipment working.

We anticipate many more construction companies will engage in development activity as co-promoters, willing to share development risk in exchange for exclusive rights to construct. Contractors will follow through more prudently, contract issues related to variations and claims and will seek adjudication more readily and may take more direct responsibility through the supply chain.

SERVICE PROVIDERS – Tough Times Don't Last, Tough People Do

Building Consultants: We anticipate that by mid-year, many leading Building Consultancy firms will have taken significant steps to manage/reduce costs as it becomes obvious that several projects will not be realized. Clients will review project delivery strategies with an emphasis on design efficient solutions. Consultants will be required to provide more "outside the box" solutions. The drive for "value for money" will lead to the prominence of development/project management expertise.

Estate Valuers: As the gap between valuations and sale/lease price widens and properties are forced to sell/let at more than 15%-20% below their supposed market value, Clients will require a greater degree of professional skill and judgment from Valuers. This will hopefully lead to the need for organised disclosures, driven by the Agents/Valuers themselves.

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Property/Facilities Managers: Attracting and retaining the "best" tenants (particularly in the "luxury" residential subsector for which there is already sufficient data to support market softening) will become increasingly important and the role of property/facilities management will come to the fore. It is expected that Investors/Promoters will recognize the need to involve companies which offer property and/or facilities management in the conception and design of their projects.

PRODUCT TYPES

Supply is inadequate and largely inappropriate across all product types. This is particularly so in the low/middle income residential subsector (across the country) and commercial offices/industrial (in major cities). It is this shortage that will fortunately, prevent a significant price meltdown.

As sale and purchase activity continues to fall in the "luxury" residential market, a price correction may see the average purchase price drop by 15%-20% specifically in areas considered prime in the major cities of Lagos and Abuja. Rental values will also fall in the face of increasing stock, coupled with fewer tenants willing to pay current top rents, in Victoria Island and Ikoyi (we do not expect the percentage fall to be as substantial as sale values) and for the first time in a while, tenants will be in a stronger position, negotiating leases in their favour. By contrast, rental and sale values will continue to rise slowly in the suburbs of major cities as more people seek rental and ownership opportunities in these locations.

In a market where most corporate organisations build and own their offices, we anticipate additional pressure on demand for office accommodation, as Companies have/will make decisions to shelve building projects. This will cause significant rental increases particularly on "Grade A and B" properties.

Curtailed individual and business spending, has left many retailers experiencing a sharp drop in revenue. We expect to see significant tenant turnover, and vacancies particularly in the upscale malls. However, we anticipate that the demand for standard "lock up stalls" (such as Ikota Shopping Centre) will continue to rise, even as the Lagos State Government rids the city of illegal/informal retail areas.

There has been very little activity in industrial real estate. Manufacturing and logistics companies typically build for own use. Manufacturing is under tremendous strain and several owner-occupiers are looking at spatial utilisation with a view to creating industrial stock for the market. It is expected that there will be a slight increase in the supply of Industrial properties within existing industrial estates.

With speculative land purchases on the decline, and several parcels on the market "for quick sales", we expect a fairly significant price correction of land values particularly in prime locations, and far less so in the suburbs, which may even witness a steady price appreciation.

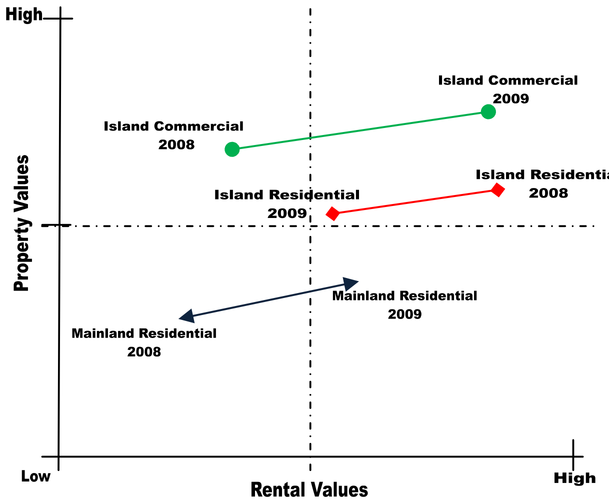

Figure 1Property Products: Projected Pricing

CONCLUSION
Overall, in the course of the year and well into 2010, we expect that real estate opportunities will indeed represent real value for investors. Professional service providers will be held more accountable for their services and the formal disclosure of real estate transactions may be one of the most useful outcomes of these times, if it indeed comes to light. Collaborations to overcome project resourcing challenges will present new opportunities and solutions.

These are interesting times!

NEWS FLASH

LAGOS STATE INITIATES PRIVATE PUBLIC PARTNERSHIP SCHEMES WITH DEVELOPERS FOR AFFORDABLE HOUSING

The Lagos State Government has announced that15,000 housing units will be constructed over the next 24 months at a total cost of US$70million in various parts of Lagos mainland (such as Yaba and Gbagada) and suburbs such as Ikota and Abijo. These projects will be executed through several partnership arrangements with Developers in which the Government's contribution are the sites and an enabling environment. Developers will raise the financing and provide all technical/management resources.

We expect that the Developers will seek appropriate construction technologies which will enable the rapid deployment of the houses and at the same time address some of the quality issues the construction industry faces. The use of technology should drive the need for standardisation of building components, encouraging the establishment of small "specialist" suppliers and service providers.