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Real estate infrastructure financing in Ghana: Sources and constraints

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A R T I C L E I N F O

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A B S T R A C T

Finance represents a major barrier to real estate development in Ghana and constraints responsible remain unknown. In order to gain insight into this important social/economic issue, a positivist tradition of thinking via the survey approach sought to uncover, explain and rank these constraints using the Relative Importance Index. A total of 53 questionnaires were distributed to real estate developers within the Kumasi Metropolis of Ghana. The survey reveals that real estate developers predominantly use debt financing including short-term bank loans, mortgages and hire purchase. Finance is constrained by five main factors: i) legislation; ii) macroeconomic barriers; iii) collateral barriers; iv) inadequate risk assessment and diversification mechanisms; and v) a dearth of financial mobilization mechanisms. This paper provides a practical reference for the targeting of policy interventions to overcome these constraints and to catalyse the development of finance for real estate infrastructure delivery. The work is also useful to the Government, banks and capital market regulators who seek to develop the capital market to provide appropriate financing options. These options may include real estate investment trusts (REITs) and risk reduction/diversification platform via derivatives. Future research is proposed which seeks to explore practical innovations in designing tailor-made real estate financing options that meet the needs of real estate developers.

1. Introduction

As the population continues to grow and urbanization accelerates, incremental housing development has consistently proven to be deficient in meeting Ghana's housing need (Bank of Ghana, 2007; HFC, 2007). By incremental housing, owners become self-developers relying on small crafts and trades to build 'gradually' over 5–15 years using their sweat equity as and when funds become available (Debrah, Ibrahim, & Rufasha, 2002); or otherwise use personal savings accumulated over long periods (Mathema, 1999; Tomlinson, 2007). This has resulted in a substantial housing deficit of about 100,000 units as at 2013 (UN-HABITAT, 2008). According to Sandilands (2002), the real estate sector leads to improved cities and contributes significantly to the gross domestic product (GDP) of nations; for instance, it contributes about 10 percent to Thailand's annual GDP (Chanond, 2009). However, an important feature of the real estate investment market is its comparative large size and long investment horizon, requiring colossal sums of long-term finance. In a study by Attakora-Amaniampong (2006), the main sources of finance to real estate developers were bank loans, equity, retained earnings and deposits by prospective buyers. Real estate is thus characteristically capital intensive, usually requiring a mixture of both equity and debt financing. The ability of real estate developers to borrow and spread repayments over an extended period for housing development is necessary to enhance affordability.

An efficient real estate finance system is nonetheless a *sine qua non* to residential real estate delivery, which in most advanced economies is inseparable from the mortgage market; contributing 77%, 85%, and 85% to GDP in the USA, UK and New Zealand respectively (EFinA and FinMark Trust, 2010)—this compares to 0.5% in Ghana as at 2012 (Centre for Affordable Housing Finance in Africa, 2012). The availability of finance and its cost is a key constraint to real estate firms (Attakora-Amaniampong, 2006; Karley, 2009) and as such a vital resource to Ghanaian

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developers. Finance is opined as essential by Tipple and Korboe (1998) and the mode in which it is accessed represents a critical factor of a healthy housing system (Boamah, 2010; Warnock & Warnock, 2008). The source of housing investment provides a medium by which finance is channelled from surplus units to developers for housing construction; a key issue for sustainable housing delivery in any country (Boamah, 2011). The mere availability of a source of finance for real estate developments inures little benefit in the absence of its efficiency. When combined, availability and efficiency will increase access to, and accelerate the allocation of adequate finance for the purchase and construction of houses sustainably at a competitive cost (Gevorgyan, Stefan, Hirche, & Entwicklungsbank, 2006). The adequacy of finance at a competitive cost is crucial in reaping the full benefits from real estate investments (Boamah, 2011). For instance, the growth in sub-prime mortgage lending in the United States of America increased homeownership (low-income and first time homebuyers) by 12 million between 1993 and 2005 (Bible & Joiner, 2009; Gramlich, 2007).

Despite the importance of real estate finance to developers, particularly in developing countries, the literature (Bank of Ghana, 2007; HFC, 2007) reports upon a clear dearth of housing supply to meet growing demand. In this study therefore, the sources of finance available to private real estate developers in Ghana are first identified and discussed using a synthesis of previous studies (Attakora-Amaniampong, 2006; Awuvagoge, 2013). These aforementioned 'sources' then form the basis of an examination and explanation of any 'constraints' to capital flow. This paper aims to: i) extend the discussion by estimating the relative importance of these finance sources; ii) identify finance constraints within the residential real estate sub-sector; and iii) provide pragmatic guidance for government and, financial and property development sectors of the economy.

2. Historical account of real estate financing in ghana: 1939–2013

Real estate financing is inextricably linked with the state's role in housing policy formulation and the need to provide residential developments, across a range of price levels (Anim-Odame, Key, & Stevenson, 2010; Karley, 2009). However, the provision of subsidized housing first emerged from two catastrophic events in 1939, namely: i) the outbreak of world war two and the need to house veterans; and ii) *force majeure* emanating from a cataclysmic earthquake which left thousands of citizens homeless (Arku, 2009; Tipple & Korboe, 1999). Between the late 1950s to the early 1980s, the Ghanaian government directly financed and developed housing infrastructure (Arku, 2009). As a leading provider of housing, the state built a large number of dwelling units to replace the predominantly informal settlements that manifested from a population boom and acceleration of urbanization (Owusu, 2012; UN-HABITAT, 2011). As instruments to engender accelerated housing development, the government set about establishing state-owned enterprises and quasi-state institutions including the State Housing Construction (SHC), Tema Development Corporation (TDC) and the Ghana National Housing Corporation (GNHC) (Owusu, 2012). To act as a platform for these enterprises, a Development Plan was implemented from 1959 to 1964 and 6,700 housing units were proposed for construction. This plan then evolved into a formal housing policy and from 1964 to 1970, 60,000 new dwellings were to be constructed throughout the country (Owusu, 2012). To finance these plans and policies, the First Ghana Building Society (FGBS) was established in 1956 under the Building Society Ordinance, 1955 (Act 30) to provide credit facilities to home builders and buyers (Boamah, 2011). The state's role as the major provider of housing shrunk during the 1970s because of the global economic recession (Boamah, 2010) and it adopted an 'enabling role' to empower people to finance and develop themselves (Arku, 2009). To realise this objective and improve housing affordability, the monetary strategy adopted established financial institutions to provide credit facilities to homebuyers. For instance, the Bank for Housing and Construction (BHC) was established in 1973, whilst the Public Servants Housing Loans Scheme, the Armed Forces Mortgage Loans Scheme and the Low Cost Housing Programme were implemented to build more housing units and estates in three urban centres around Accra, Tema and Kumasi. This era also saw the promulgation of the (NRCD 96) to provide concessionary construction finance and credit to home buyers.

The implementation of World Bank/IMF supported Structural Adjustment Programmes (SAPs) as a panacea to heightened macroeconomic problems in the 1980s significantly shifted the role of government as a direct provider towards a neo-liberal route (Konadu Agyemang, 2000; Yeboah, 2003). This competitive driven approach sought to enable private sector participation in housing delivery and improve housing finance efficiency commensurate to increasing housing supply through commercial development (Arku, 2009). In turn, this saw the establishment of the Ghana Real Estate Developers Association (GREDA), 2007 to act on the behalf of private ventures and preserve professionalism throughout the sector. Intensification of neo-liberal tenets (in the post-SAP era) has seen the state facilitating and enabling the private sector to achieve sustainable urban planning (UN-HABITAT, 2011). This role is evident in the provision of conducive environments for the efficient operations, which is integrated within Ghana's Growth and Poverty Reduction Strategy (GPRS 2). For instance, financial and/or tax incentives were implemented to attract potential investors into housing development, these include: the reduction of corporate tax from 55% to 45%; declaration of a 5-year tax holiday for new real estate developers; and exemption of house purchases (from real estate developers) from Stamp Duty (Arku, 2009).

As part of the World Bank Urban II project, the World Bank and the state (through the Social Security and National Insurance Trust - SSNIT) contributed US$8 million and US$16 million respectively to set up the Home Finance Company in 1990, now the HFC Bank. The bank was to operate as a secondary lender (refinancing mechanism) but now acts as a primary lender (i.e. originating, underwriting, funding and servicing mortgages) and subsequently, monopolized the mortgage market over a decade (Asare & Whitehead, 2006). In response to this monopoly, some financial institutions (such as the Ghana Home Loans, Fidelity Bank, Ecobank and Cal Bank) sought to provide alternative mortgage and construction finance (Attakora-Amaniampong, 2006). Amidst this emergent competitive background, basic core points such as land acquisition and finance necessitated the preparation of the five-year Comprehensive National Shelter Strategy Programme (1993–1997). Unfortunately, this programme failed to achieve its objectives (PPEU, 1991: Abusah, 2004).

In 2009, the Government demonstrated an intent to provide 'affordable housing' for Ghanaians through a Private Public Partnership (PPP) arrangement. By this approach, the Government was responsible for providing Sovereign Guarantees and other forms of support to enable the private sector to raise substantial funding for the construction of 300,000 'affordable housing' units; this initiative was otherwise known as STX Housing Project and was estimated to cost USD 10 billion. However, this ambitious arrangement never materialized and since then, there has been no substantive housing policy. More recently, there has been the injection of significant financial resources into the housing sector; for instance, about 81 real estate and allied projects valuing about $105 billion were recorded between 1995 and 2005 (Arku, 2009). Some studies