

ISLAMIC HOME FINANCING IN NIGERIA

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Abstract

There is urgent need to finance affordable housing, especially in Nigeria. As of 2015, the number of Muslims stands over 80 million. This emphasises the need for Shari'ah compliant home financing to suit the demands of their faith. The immutable principles of Islamic commercial transaction that prohibit riba and gharar has drawn up a sharp distinction between the concepts of Islamic and conventional home financing. Nonetheless, despite the establishment of Islamic banking in Nigeria and the willingness of Muslims to embrace it, home financing in Nigeria remains largely conventional. Drawing on a review of literature on Islamic finance in Nigeria, this paper examines factors that may hinder the implementation of Islamic home financing in Nigeria. The study revealed that low level of awareness, lack of long-term financing, religious and cultural disparity, and an unfavourable framework are main factors hindering the adoption of Islamic home financing in Nigeria.

1. Introduction

The Shari'ah law of commercial transaction is firmly established on the prohibition of usury (riba) and uncertainty (gharar). Islam encourages trade and business but strongly prohibits usury or riba' as stated in the Qur'an: "And Allah permits trade but prohibits riba" (Qur'an, 2:275). Profit from trade is lawful while any additional return from loans is unlawful (riba). This has made a clear distinction between concepts in Islamic financing from that of conventional financing. Loan is one method of conventional financing while the Shari'ah forbids financial activities containing interest and/or which has no real connection to trade. The Shari'ah does not recognise any types of loan other than Qard al-hasan (Loan without interest). However, Qard al-hasan is not suitable for home financing because houses require huge capital and long-term

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financing. Nonetheless, there are other financing products such as Murabaha, Ijarah and Musharakah in Islamic financing apart from Qard al-hasan which have been adopted in some countries for home financing.

Housing is maslaha (welfare) and a basic human need. Despite the importance of housing, the problem of affordable housing is among the most pressing issues facing Nigerians. Many find it difficult to secure a house due to its high cost. In fact, there are many people, particularly in rural areas, living in temporary shelters or crowded into sub-standard and sometimes unsafe housing. In addition, there are more people living on the streets in cities like Lagos and Abuja because they cannot afford to rent a room let alone buy a house. It is difficult to save in order to own a house for the low and medium income earners in Nigeria. As a result, they need finance in order to fulfil their goal to own a house. However, financing is not viable in Nigeria and this has made it difficult to mobilise finance and credit for housing. Islamic finance could, in principle and in practice, correct these defects if Nigeria can emulate the system of countries like Malaysia.

In Nigeria, house loans are based on riba. Although Islamic finance is practiced in Nigeria, it is still in its infancy stage with little public awareness. Many Muslims have no knowledge of Islamic finance (Vincent and Uloma 2013). Therefore, more research is needed in this area to study the perception of people toward Islamic home financing with regard to the level of awareness. Furthermore, recently, there have been many refinements in the housing sector, yet many Nigerians who have assessed one conventional mortgage financing are not satisfied. Therefore, this paper studies the perceived problems of the current home financing structure to identify factors apart from awareness that may hinder the acceptance of Islamic home financing.

There is urgent need to finance affordable housing as it helps secure the health, personal well-being and quality of life of all Nigerians. The objective of this research is to examine the factors that hinder the willingness of people to accept Islamic home financing in Nigeria in the hopes that financial institutions will consider them when designing products and policies. The information in this research will also help the regulators to devise effective policy actions towards affordable housing.

1.1 Muslim Population in Nigeria

In sub-Saharan Africa, West Africa has the highest Muslim population with the least Muslim population in southern parts of Africa. The population of Muslims in West Africa is projected to grow by more than 60% in the next 20 years, from roughly

160 million in 2010 to about 257 million in 2030 (News from Africa 2011). Nigeria, the most populous country in West Africa, has the largest Muslim population among all sub-Saharan Africa. There are different figures by various surveys for the size of religious groups in Nigeria, which according to the CIA World Book appears to have roughly 50% Muslims, 40% Christians and 10% Indigenous. **Nigeria is expected to have a slight Muslim majority (51.1%) by 2030. According to the survey, the Muslim population is projected to increase by more than 41.1 million from 2010 to 2030**, increasing from 75.7 million in 2010 to 116.8 million in 2030. It is seen as the largest projected growth in sub-Sahara Africa (News from Africa, 2011).

Table 1: The 10 Largest Muslim Populations in the World in 2010 and Projected Population in 2030.

10 Countries with the Largest Number of Muslims in 2010		10 Countries with the Largest Projected Number of Muslims in 2030	
Country	ESTIMATED MUSLIM POPULATION	Country	ESTIMATED MUSLIM POPULATION
Indonesia	204,847,000	Pakistan	256,117,000
Pakistan	178,097,000	Indonesia	238,833,000
India	000 ,177,286	India	236,182,000
Bangladesh	000 ,148,607	Bangladesh	189,506,000
Egypt	000 ,80,024	Nigeria	116,832,000
Nigeria	000 ,75,728	Egypt	105,065,000
Iran	000 ,74,819	Iran	89,626,000
Turkey	000 ,74,660	Turkey	89,127,000
Algeria	000 ,34,780	Afghanistan	50,527,000
Morocco	000 ,32,381	Iraq	48,350,000

Population estimates are rounded to thousands

Adopted from: Pew Research Centre’s Forum on Religion & Public Life. The Future of the Global Muslim Population. January 2011.

1.2 Islamic Finance in Nigeria

Nigeria’s Islamic finance industry has existed for more than 30 years. Islamic banking in Nigeria began in 1982 by Habib Bank PLC which opened a non-interest banking window offering a small numbers of Shari’ah compliant products. However, as at that time, there was no framework for the operation of Islamic banking in Nigeria resulting in poor growth. Another institution was founded by the name Jaiz International PLC.

This bank was incorporated on the 1st April 2003 as a public limited company with the main objective of being an investment holding company in order to form non-interest institutions like Islamic banks and Islamic insurance (Takaful) etc. It applied for a license in 2004 and was granted approval in principle, AIP to that effect. Unfortunately, it could not meet the new capital requirement.

The legality of non-interest banking in Nigeria began in 1991 with the amendment of the Banks and other Financial Institutions Act (BOFIA). It recognised specialised banks which include non-interest banks/profit and loss sharing banks, microfinance banks, development banks, mortgage banks and such other banks as may be designated from time to time by the Central Bank of Nigeria (CBN). It states in (section 61) of the Act, “Profit and Loss Sharing Banks” means a bank which transacts investment or commercial banking business and maintains profit and loss sharing account. However, it outlaws the incorporation or registration of any bank with a name that includes words like, Islamic, Christian, Qur’anic, Biblical and so on (section 39 (1)). The Central Bank Governor rightly exercised his powers by making regulations to promote and establish microfinance banks, mortgage banks, developmental banks and Islamic banks (or non-interest financial institutions as the case may be). Jaiz International was given license by the Central Bank of Nigeria, the national banking operator to operate as a full-fledged Islamic bank on 11 November 2011. The institution commenced business operations as Jaiz Bank PLC on 6 January 2012 in offices and branches in cities like Abuja, Kaduna, and Kano.

According to the plans for a well-established Islamic finance culture in Nigeria, the CBN rolled out its guidelines on Shari’ah governance for Islamic finance in 2011. It was stipulated in (section 1) of the guidelines, that compliance with Shari’ah principles is a critical element of non-interest banking and finance. In order to ensure that Non Interest Financial Institutions (NIFIs) are carrying out their operational activities and transactions in accordance with the Shari’ah principles, it was mandated under (section 4) of the guideline that all licensed (NIFIs) should establish a body known as the “Shari’ah Advisory Committee” (SAC) as part of their governance structure. This committee will be responsible and accountable for all Shari’ah matters in the institution. In addition, there are other rules that forbid taking and receiving interest payment.

To get rid of riba, Islamic banks are using Murabaha for trade financing. A Murabaha is a sale on a cost plus basis where payment (of the original price and the mark up) is deferred to a later date. Another one is Musharakah, which is obtained for financing

capital project. Musharakah is funding by two or more parties for project development. In this case, losses will be shared based on the contributing capitals and profits may be shared according to the pre-agreed ratio by the partners. For home financing, Ijarah wa Iqtina is used in which the bank will become a lessor and the customer the lessee, and after the full payment of the rent as agreed, the property will be fully transferred to the customer.

Nigeria currently has one full-fledged Islamic bank which is Jaiz bank PLC. and three windows of conventional banks like Keystone bank, Stanbic IBTC, and Sterling bank. For insurance and capital market sectors, there are Lotus Capital (a full-fledged Islamic fund management company) and Takaful windows in African Alliance PLC., and Cornerstone Insurance PLC. Despite all these achievements, Islamic financing has not fully developed, especially in the area of financing products. Therefore, this research focuses on home financing for the benefit of homebuyers, especially Muslims. Apart from one's own personal equity, Islamic home financing can serve as an alternative to conventional financing so that Muslims will be freed from riba based financing. For now, Nigeria has only one Islamic home financing product which is based on Ijarah wa Iqtina offered by Jaiz Bank.

With the gradual increase of Islamic finance products in Nigeria spurred by the initial licenses issued to some banks by the CBN to operate Shari'ah –compliant banking, and the high number of Muslim population in the country, this has motivated the researcher to know what may cause delay in the adoption of Islamic forms of home financing in Nigeria. This is necessary because Nigeria is still in its infancy stage, especially in the area of Islamic home financing. Presently, only conventional financing is used in Nigeria for home financing. With the high and unstable interest rate of conventional financing, Islamic home finance will serve as a better alternative due to its predetermined price at the contracting period. In addition, it will help the homebuyer to have a good financial planning because the financing amount will be shared evenly and be paid through instalments.

1.3 Home Financing in Nigeria

Financing is the deliverance, provision, raising, or acquisition of funds in order to undertake or facilitate an economic activity (of e.g. consumption, production, trading, services, education, health, construction etc.) that cannot be realised otherwise (Irfan, 2008). As there is the innate desire of every man to own a decent house, it is the single non-commercial investment for most consumers (Ogedengbe and Adesopo, 2003).

Asset acquisition, such as a house, takes a large bulk of peoples' income. For the house owner, the house stands as a life-long investment and a store of value. Despite its importance, most homebuyers lack the cash to purchase their residence. They have to look for their best choice of financing. As a result, home financing or mortgage is a major aspect of housing decision.

Finance constitutes a fundamental centrepiece in any project. The ability of a homebuyer to get enough funds for the house acquisition determines the success of the acquisition (Ogedengbe and Adesopo, 2003). Finance is an all-important factor, a sine qua non and crucial ingredient for house acquisition. Home financing can be viewed as the borrowing of money to buy or acquire a house. Moreover, the provision of housing services depends upon a well-functioning home financing system, while the performance of any home financing system will depend primarily on the volume and nature of funds within the economy and the proportion of it that can be spread, mobilised, or dedicated for housing.

In Nigeria home financing is the same as mortgage. The word mortgage is mainly linked with the loan secured on real estate. Mortgage is the common method individuals use to purchase real estate without paying the full value of the property at a single time from their personal resources. The Housing Handbook of 1991 defines mortgage as an instrument recognised by law through which property is given up as security without necessarily giving up possession of it for repayment of a debt or obligation. It can be said that when you create a loan that is used to finance the purchase, construction, completion, or improvement/renovation of a house, the house is in turn held as security (or collateral) for the loan. A mortgage is therefore an agreement between the homebuyer and the financial institutions to allow the homebuyer to finance the purchase of a home. The mortgage terms agreements make clear the condition of transfer of title from the financial institution to the homebuyer, through the payment of instalments over time by the purchaser. The financial institution makes its profit by charging interest which is added to the principal base of the transaction.

There are different types of mortgage institutions in Nigeria providing mortgage services to homebuyers. These institutions have their own requirements and eligibility guidelines which differ from one another. The mortgage instruments are provided by the Federal Mortgage Bank of Nigeria and the National Housing Fund which are federal programmes meant to give Nigerians access to cheap long-term funds for the purpose of buying or developing a property. There are also Primary Mortgage Institutions (PMI's), banks, and other financial institutions offering home loan or

mortgage products which can be accessed to purchase a property. These loans are available to qualifying low and medium income homebuyers.

1.4 Home Financing Problem in Nigeria

Housing problems in Nigeria result from connections among social, political, and economic policies. The housing deficit reportedly stands at 14 to 17 million; up from the 8 million identified in the 1980s and 13.64 million estimated by Ajakaiye and Fatokun (2000) for the 2000 – 2005 period. According to Omirin and Nubi (2007), over 72 million Nigerians are either homeless or live in rented sub-standard homes in areas best described as slums. The identified factors militating against housing provision in Nigeria include inadequacy home financing, high cost of building materials, problem of land acquisition, unfavourable land policy, lack of infrastructures (physical and financial infrastructures), etc. However, the major obstacle that hinders the access of average Nigerians (the low income) to adequate homes is lack of finance. Olusola et al. (2002) identified lack of soft loans as one of the major obstacles against housing production in Nigeria. House acquisition is bedevilled by inadequate access of funds. Home ownership depends on the personal financial resources because mobilization of finances for house acquisition is difficult.

The problem of home financing has been documented by scholars. The pooled effect of high population upsurge and urbanization rooted on a declining economy of the nation as revealed in Nigerian cities has thrown the country into a serious housing finance debacle (Adediji, 2007). The people most affected by the finance menace are the low-income groups who occupy the largest part of Nigerian society. According to the 2010 Global Monitoring Report of UNESCO, roughly 92% of the population earns less than US \$2 a day, with about 71% surviving on less than US \$1 a day. Lack of financing is due to low earning power, inability to afford down payments, and inability to provide guarantors that are capable to the mortgage institutions (COHRE, 2000). Other mitigating factors that have prevented developing nations like Nigeria to extend credit to potential homebuyers can be linked to the ability of debt repayment by borrowers, and high interest rate extended to potential homebuyers by the banking institutions (Nnana, 2010). Ogedengbe and Adesopo (2003) added that collateral security and certificate of occupancy as demanded by most of these financial institutions are problems for homebuyer in securing finance. One can also cite the high rate of inflation, high cost of building materials, and collapse of the nation's currency as factors responsible for housing finance problems (Ogunsemi and Abiola-Falemu, 2006).

Moreover, houses involve huge capital expenditure and the earning capacity is generally low which makes it difficult for the average Nigerian to save towards owning a house. The cost and availability of home financing can influence its viability. The consideration of acquiring a house is driven by the cost of acquisition, availability of home financing, and various government economic policies that could be fiscal or monetary. Consequently, finance has been identified as pivotal in housing delivery in Nigeria (FGN, 1991), culminating in the promulgation of National Housing Fund (NHF) Decree 1992. Although the Federal Government of Nigeria provides finance schemes for housing to all government and private workers through the NHF, it has been insufficient.

Only a few urban dwellers have been able to benefit from mortgage loans by commercial banks, mortgage institutions, and state housing corporations. Available information discloses that the supply of finance by the federal mortgage bank is not adequate to meet the increasing demand (Sanusi, 2003). The trend of the housing share against the average GDP declined from 3.6% in the 1970s to 1.7% in the 1990s and less than 1% now. This is an indication of decreasing home financing activities. Accordingly, there is a need to propose and develop a strategy to expedite the improvement of home financing market. Persistent increase in Nigeria's population means a thorough approach to solve the surviving housing problems in the country. For that reason, the development of the home financing market may be a major factor for the development of the overall financial market.

Owning a house is the Nigerian dream, however, there is no mechanism for risk sharing in Nigeria. This makes it difficult for banks and other financial institutions to provide financing to low-income groups. This is due to the absence of a credit information database (Akeju, 2007). Nigerian financial institutions prefer to offer financing to the rich. The bank lending practice does not favour low-income households because they cannot simply give loans to applicants whose financial records or credentials indicate that they may have problem repaying their loans. In addition, banks cannot simply give loans to people to buy houses they cannot afford. As such, 93% of loans granted to individual homeowners went to middle and upper income earners (Adeboye, 2009). This means that banks are not assisting low-income groups to buy homes through mortgage financing.

Many Nigerians are homeless due to their fear from entering into debt who consider debt financing is bad. This happened due to the financing requirements by the financial institutions. The problem of financing requirement is one of the major problems facing

most Nigerians, especially from conventional financial institutions such as collateral and high interest rates, down payment charges, guarantors etc. Through home financing in Nigeria, houses are usually purchased under the banks name. The house ownership will be changed if the financing amount and interest on it have been repaid in full. However, if there is default in payment, the bank will foreclose the house and the homebuyer will lose what he has paid for. Interest free financing on the basis of mutual ownership may be one way out of this predicament. This is the purpose of this study to help Nigerian Muslims avoid *riba* as it is against their belief. The researcher views the adoption of Islamic home financing in Nigeria as an advantage to bring about a win-win situation between the financial institutions and the homebuyer.

2. Problems that may hinder the adoption of Islamic home Financing

While the academic literature on Islamic home financing has explained the interrelationships between Islamic and conventional home financing and the customer perception on Islamic home financing, few researches have explicitly addressed Islamic financing in the context of Nigeria and only one was found in home financing. A few pioneering efforts focus on customer perceptions on Islamic banking, examining the intentions of the customer regarding Islamic financing; the collective findings are varied. Ibrahim and Mustafa (2011) examined the perceptions of Nigerian Muslim youths in Malaysia based on the establishment and operation of Islamic banks in Nigeria. The finding shows that the perception of youths on Islamic banks in Nigeria is significant to its establishment and operation. Furthermore, the perceived problems and challenges on Islamic banks are of significance to its establishment and operation in Nigeria.

However, despite the willingness to have the Islamic banks there are still many challenges. Abdullahi (2013) explored the possibilities of introducing Islamic banking in West Africa and sought to determine the challenges that come with the introduction of the system. The findings show that Islamic banking is yet to be fully taken up as there are still many domestic challenges to the operation of the system. Sanusi (2011) examined the issues and challenges of Islamic finance. He stated the challenges facing Islamic banks included limited knowledge, skills, and technical capacity, lack of Shari'ah compliant liquidity management instruments, absence of *Takaful*, lack of Islamic accounting/auditing knowledge, lack of a robust and comprehensive legal framework, lack of knowledgeable Shari'ah scholars, double taxation, misperception of Islamic bank in Nigeria, etc. This study reviews previous literature on Islamic finance in Nigeria to determine the problems that may hinder the adoption of Islamic home financing in Nigeria.

- 1. Lack of Awareness:** Public awareness is very important in selling any product. In order for people to go for a product, they must have knowledge of it. In Nigeria, there is little awareness of Islamic banking products which may hinder their adoption. The research by Vincent and Uloma (2013) on how knowledgeable Nigerian elites were about Islamic banking found that many Nigerians did not understand the operations of Islamic banks neither were they aware of its existence. There is a need to conduct campaigns for creating mass awareness on the practices of Islamic banking and finance (Yatoo and Muthu, 2013). For home financing in Nigeria, lack of awareness might be due to the product being new in the market and it is only offered by one bank with limited branches. Since people are only aware of mortgages as it is the common type of financing, there is a need to create awareness of Islamic home financing products.
- 2. Unfavourable Regulatory Framework:** The regulatory framework for home financing favours conventional banks because the framework is structured in accordance with the conventional financial system. From this framework, the CBN is allowed to give banks loans with interest which is not in accordance with Shari'ah. This means that Islamic banks cannot access the loan. From the legal view, Aminat (2011) compared the Islamic and conventional legal framework on mortgage financing schemes in Nigeria. She found that there is similarity in terms of permissibility. In terms of Islamic mortgage financing operation, there is the constitutional permission (Sections 260 – 264; 275 – 279 and 237 (2) (b), CFRN, 1999 (as amended 2011)). However, there is difference in term of grants based on *riba*. Under CBN Act Section 29, based on this provision, the CBN is empowered to provide loans with a fixed interest rate to be calculated on the amount at the end of the agreement for banks. From this provision, the loan pertains to conventional banking operation only because Islamic bank do not operate based on interest. They operate pure Islamic transactions and forbid any transactions that contain the element of *gharar*. In conclusion, from the CBN Act, it is noticeable that the provision contained therein recognises only conventional economic activities, and there is no recon for Islamic economics. This has shown the clear difference in the legal framework that caters for Islamic and conventional home financing. There is need to modify the existing framework by making provisions for Islamic banks where they will be given interest free loans to benefit the community. In addition, the National Housing Fund, which is a federal government programme, is based only on the conventional system where the housing loan

is given with interest. CBN should give Islamic banks access to this NHF to be based on non-interest.

- 3. Lack of Long-Term Financing:** Long-term financing is a major problem in the Nigerian housing market. Long-term financing is a form of financing provided for more than 15 years. Islamic banks are operating with a limited set of short-term traditional instruments, and there is a shortage of products for medium-to long-term maturities (Iqbal, 2007). If Islamic banks could not provide long-term financing, people may not opt for their product. This is because home financing requires huge capital. Therefore, long-term financing is very important in order to spread the payment burden over the financing period. As a kind of innovation, Islamic banks should provide home financing that is not less than 15 years.
- 4. Religion and Cultural Disparity:** Nigeria is a multicultural country with at least three recognised religions. Culture describes the beliefs and practices of another society. If there is disparity, people would have different perceptions of Islamic home financing product and this may lead to misperceptions by non-Muslims. It could even lead to public rejection of products. Misinterpretation of the concept might jeopardise its success (Sanusi, 2011). Therefore, there is need for greater awareness in this area by the Islamic banks, religions leaders, village heads and the CBN. They should let people know the objectives and advantages of Islamic home financing product so that they would not attach it to one religion or culture. Thus, irrespective of religious belief, people would still go for Islamic products because of its risk sharing mechanism. A survey was conducted by Imam et al. (2015) examining the willingness of people to invest in Islamic fund in Borno state. They found that Borno people are willing to invest their money in Islamic funds regardless of their religious beliefs. However, this might not be applicable in other regions because Borno people are mostly Muslims so they might have basic knowledge of Islamic finance.
- 5. Competition:** Islamic banks are relatively new in Nigeria and are facing strong competition from conventional banks. In the area of home financing, conventional mortgage has existed for years and has gained popularity. There should be strong competition with conventional banks if Islamic banks want people to accept their products for home financing. They can only achieve this through innovativeness by creating new Shari'ah compliant home financing products. The development of new products and processes is increasingly a

focal point of competition (Al-Salem, 2009). Gumel and Mohd Azmi (2013) investigated the relationship between consumer innovativeness and customers' intention to adopt Islamic banking in Northern Nigeria and find that consumer innovativeness as a personality trait and a key to new product success to influence customer attitude, social influence, and perceived behavioural control. Therefore, Islamic banks must develop Shariah compliant products that meet the economic needs of society.

6. **Networking:** Nigerians have long been eager to have Islamic banks. Their willingness has made it a necessity for the introduction of Islamic finance in Nigeria. Research has shown their interest in its establishment and willingness to adopt their product. Due to its status as a new bank, Islamic banks in Nigeria have limited branches centred only in the Northern part of the country. While networking is one of the important variables in determining the adoption criteria of Islamic banks (Tara et al., 2014), this may hinder the adoption of their products because it is not accessible. The only solution to this problem is to establish branches in all the regions in Nigeria so that those interested in their products will have access.

3. Conclusion

This study has discussed home financing in Nigeria and problems associated with it. Mortgage financing is the main mode of home financing in Nigeria. People perceived financing requirements by the financial institutions as the major problem for accessing home financing which according to the previous study, have made it almost impossible for low income families to buy a house. There is lack of risk sharing mechanisms in home financing in Nigeria. In addition, Nigerian Muslims comprise 50% of the total population, which shows the potential of Islamic finance. Therefore, Islamic home financing is suitable in Nigeria and appropriate for both Muslims and Non-Muslims because it is based on a profit and loss sharing system.

The challenges that may hinder the adoption of Islamic home financing products include low level of awareness and knowledge on Islamic home financing. Moreover, the legal framework is not in favour of Islamic finance in Nigeria. The CBN provides loans for conventional banks with a fixed interest rate which is not Shari'ah compliant. In addition, competition from conventional banks and networking problem can hinder the adoption of Islamic home financing. The Islamic banks should try to increase their network and create awareness of their products so that people will know what they are offering.

Apart from Ijarah wa Iqtina, more Islamic home financing products that are in line with Shari'ah regulations could be offered to the public, especially the Muslims community in Nigeria. Nigerians will definitely go for the product that is Islamic if the Islamic banks can provide proper solutions to the above challenges because of the high number of Muslim population and because it is aligned with their religious ethics. It is high time that Nigerian Islamic banks introduce a new product towards for efficient home financing in the country.

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