06.30.2025 JOURNAL OF

Env. Management & Construction Res. (JEMCR) Vol. 8 No. 4

CHALLENGES ASSOCIATED WITH OFF-PLAN REAL ESTATE INVESTMENT IN NIGERIA: A CASE STUDY OF LEKKI-AJAH AXIS OF LAGOS STATE

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DOI Link: https://doi.org/10.70382/bejemcr.v8i4.028

ABSTRACT

This paper aims to investigate those factors influencing off-plan real estate investment strategy with a view to proffering solutions to the hindrances of the strategy. Hence, this paper explores the factors driving and hindering off-plan real estate investment in Lagos, focusing on the Lekki-Ajah axis of the state, with a view to proffering solutions to the identified factors hindering off-plan real estate investment in the study area. To achieve this purpose, the study ascertained the prevalence of off-plan sales in the study area; assessed the factors influencing off-plan real estate investment in the study area and examined the factors hindering off-plan real estate investment in the study area. The results were expected to provide valuable insights to investors, developers, policymakers and other stakeholders in the real estate industry, which is to help them make informed

Introduction

The urban population in Lagos State, Africa's second most populous metropolis, has been growing exponentially. The continuous increase in population demands a corresponding increase in housing to serve the population. The government's failure to sufficiently address this demand has resulted in housing shortfalls of approximately 2.5 million in the state. (Oyalowo, et al 2023) These shortfalls can be taken care of though, necessitates a collaborative endeavour to do so, between the government and private developers. No doubt, the contributions of real estate

investment decisions, devise effective strategies, and create an environment conducive to sustainable and responsible off-plan real estate investment. Data was collected from Estate Surveyors and Valuers within Lagos who are involved in real estate investment. Information was also sought from private real estate developers and stakeholders in real estate development industry. Personal visit and interview was also conducted on most of these developers and stakeholders so as to gather relevant information. However, secondary data was also collected from textbooks, past theses, past journal papers and other academic work.

Keywords: Development, Investment, Off Plan, Real Estate, Sales, Private Developers, Returns.

developers in providing housing in the states are significant. In the same accord, Enisan and Ogundiran (2013) and Ogunbayo, et al (2016) highlighted that private developers are responsible for 65 to 90 percent of housing units in Nigeria's urban areas. However, the substantial financial resources required to solve the problem of the housing shortfalls have resulted in developers exploring the option of obtaining development funds through various sources. These sources include joint ventures, equity and debt financing, off-plan sales or leases, advance payment of key money (off-plan) and sale of securities (Ezimuo, Onyejiaka & Emoh, 2014).

Comparatively, off-plan real estate arrangements are cheaper, making them viable sources of liquidity for property developers. This conclusion aligns with Kimaru's (2018) position that off-plan sales have been proven to be an effective method of financing real estate. The benefits derived from off plan arrangements constitute a significant drive for investors' adoption. Moreover, Cytonn (2022) posited that purchasing a house off-plan is an ideal way to acquire a property at a lower price than its actual market value, making it a great investment option. Other benefits of this arrangement include payment flexibility, design modification and high capital appreciation (Cytonn, 2022). Off-plan real estate investment in Lagos is a high-risk but high-return venture where investors buy into projects before completion, hoping to benefit from lower prices and potential long-term appreciation after completion. (Cytonn, 2022)

However, numerous challenges plague this market, including project delays and cancellations, unclear regulatory frameworks, market volatility, lack of transparency and trust, difficulty accessing finance, high upfront costs, risk of project abandonment, collapse, and limited investor protection. These challenges resulted in reduced investor confidence, decreased demand for off-plan projects, stalled developments, economic losses for investors and developers and missed opportunities for housing and economic growth (Kimaru, 2018; Katwa & Obala, 2023). Two (2) examples of off-plan projects in Lagos state with some of the identified issues are the collapsed 21-storey high-rise luxury residential building and the Lekki Garden Estate Phase 2. On 1st November 2021, a 21-storey high-rise luxury residential building in Lagos collapsed, marking a significant event in the state's real estate market. The project was already 65 percent sold out at the time of the collapse, with apartment prices ranging from 1.2 million USD to 5 million USD per unit. It was reported that the collapse was due to an increase in the number of floors against the government-approved number, the implication being a loss of investment to subscribers (Vanguard News, 2021). Furthermore, it was reported that residents of Lekki Gardens Estate Phase 2, Ajah protested, calling on the project developer to rectify the estate infrastructure as residents battle with flooding and surface seepage of faeces. This is a case of poor construction quality and incomplete infrastructure provision. Lekki Garden Phase 2 is also a product of the off plan strategy. These merits and demerits of the off-plan approach form the basis of investment decisions.

AIM OF THE STUDY

The aim of this study is to examine the challenges associated with off-plan real estate investment as well as its benefits to the buyers or investors such that off-plan investment can serve as "anticipatory hedging" to the buyers which means that the buyer can take advantage of the present price against any anticipated price appreciation of properties in the future, especially when a booming market is expected.

SCOPE

This paper focuses on off-plan real estate investment as it is applicable in Nigeria with specific reference to Lekki-Ajah Axis of Lagos State.

LITERATURE REVIEW

Off-plan, a common approach in property development, varies in name depending on the region. In Nigeria, it is called off-plan (Olayiwole, 2023); in Australia, it is off-the-plan. (Reid et al, 2020) Moreover, Taiwan refers to it as presale housing (Juan, Chien & Li, 2010) while in Malaysia, it is sell-then-build (Fauzi, Yusof & Osmadi, 2011). Mwaita and Rambo (2020) defined off-plan sales as a developer selling a residential unit before completion or sometimes before construction begins. Mwaita and Rambo (2020) also note that buyers can make decisions based on plans, maps, computer-generated images, or virtual reality tools. According to Ogunbayo, et al (2016), the off-plan strategy began in 1954 due to rising real estate demand and limited land, which pushed developers to build high-rises and large housing estates. This requires significant upfront capital, making off-plan sales attractive for securing funds. Ogunbayo, et al (2016) attribute the market's long-term strength to strong institutional guarantees for builders and buyers. Hayes, (2022) observed that condominium developers often sell properties off-plan in the United States and they need to sell up to 40% before lenders finance construction. Buyers can secure an unfinished property with a 5% deposit, paying the balance upon project completion or according to the development schedule payment method. This practice is also found in Canada and Australia, where Australia requires a 10% deposit. In China, the timing of capital for developers differentiates the off-plan sale mechanism from other markets. The presale approach requires customers to pay 100% upfront before project completion (Hayes, 2022)

According to Hayes, (2022), payment can be made in cash or with a down payment of at least 30% plus mortgage funds, exposing customers to significant risk. If presales underperform, failing to cover financing costs, the project will likely default, resulting in buyers losing their invested money. Even with a partly mortgaged payment, buyers still bear all risks, as they remain liable for the mortgage if the developer abandons the project. However, there are benefits of off-plan real estate sales to both developers and buyers. This study focuses on the benefits to the buyers or investors. Hayes, (2022) define this benefit for homebuyers and property investors as "anticipatory hedging," which means that the buyer can take advantage of the present price against any anticipated price appreciation of properties in the future, especially when a booming market is expected. Furthermore, because they are typically low deposits used to ensure future ownership of housing units, off-plan selling payment arrangements assist buyers in overcoming initial payment constraints. Off plan properties can also provide more options for home buyers and investors looking for their ideal dwellings/investments regarding location and features that may be in limited supply in the spot market. Furthermore, buyers can contribute to the design depending on the purchase time. This is backed by Reid et al, (2020) who argue that because developers sell units before they are built, it provides an excellent chance to redesign the home to meet the needs of the individual before construction. The authors advocate for a customer focused concept, which implies that customers have evolved from passive value acceptors to active value co-creators. Another benefit, though discouraged in some markets due to the impact on genuine house buyers, is the advantage of short-term speculation. Speculators typically use presale payment arrangements to construct highly geared options or forward contracts with the expectation of profitably reselling the properties before completion. (Reid et al, 2020)

According to Reid et al, (2020) trading such contracts before completion is feasible because buyers are typically regarded as equitable owners in the title, allowing the forward contract to trade easily in the market. Moreover, as seen in markets like Taiwan, the off-plan sale is more appealing to speculators because there is no liability for transaction tax, i.e., capital gains tax, before the property is completed. After all, the property has not yet been listed on the official property registration. (Reid et al, 2020) All these benefits of off-plan sales make it appealing to real estate buyers or investors to adopt the investment strategy. However, barriers have been identified to the adoption of the strategy. Even though developers increasingly embrace off-plan real estate as a financing strategy, several barriers hinder its adoption, particularly in emerging and less-regulated markets. Legal and institutional frameworks to protect buyers and ensure project completion heighten investor risk and limit market confidence (Katwa & Obala, 2023). Uncertainty about market behaviour, changes in property values and tenant risks, underdeveloped credit systems, and weak regulatory oversight further discourage investment. In developing economies, these issues are compounded by informal market dynamics and a lack of transparency, creating an uneven playing field for investors, which inflates perceived risks. Investment decisions are analogous to a game in which the players are placed in a rule-governed situation with defined outcomes, characterised by strategic interdependence between the game players. (Katwa & Obala, 2023)

The importance of information available to the players in a game makes a big difference in the outcome. If the information is biased toward some players, then the game would be unfair to those who do not possess the information. Generally, information is not symmetrically accessible and available to all actors in a market and most of the time, the sellers or producers have far more information about what they are selling than the buyers (Hayes, 2022). Information asymmetry characterises all real estate markets, but the nature of the off-plan process exacerbates it. Developers, by definition, have more excellent knowledge about the property, its quality, and its likelihood of completion than potential house buyers. The developer does not share this knowledge about the project's financial stability and construction with prospective buyers. This information asymmetry can lead to market inefficiencies via what is known as adverse selection, putting the buyer at a disadvantage due to a lack of information. This disadvantage mostly manifests in supplying lemons to the buyer. This means the buyers are offered faulty, defective properties, or poor-quality construction when completed. However, Katwa & Obala (2023) posit that as the project progresses, information asymmetry are reduced as the physical construction of the building reduces the developer's default risk. Given this, the principal-agent relationship created during the execution of an off-plan sale contract is unique. One has an inherent asymmetric information problem as the agent knows more about the situation than the principal. The buyer of the uncompleted property relies on the developer to finish the construction work. This lack of knowledge and technical expertise in the construction work, therefore, makes the principal unsure of whether his agent serves his best interest in terms of the quality of the work and the timely completion of construction after the agent has collected the money. (Kimaru, 2018)

According to Kimaru, (2018), this is typically a moral hazard problem. A moral hazard is said to arise when the actions of one party (the agent) are not observable but are pertinent to the other. As (Kimaru's 2018) pointed out, the actions taken by agents are not directly observable, and therefore complete monitoring is not generally possible. It is, therefore, not uncommon that problems such as the inaccurate size of the properties and mismatch of fittings and finishes were found when presale buyers collected their properties upon completion. Aside from the risks imposed on buyers due to asymmetric information, a study by Kimaru, (2018) further revealed that developers had imposed extra profit on off plan property prices in the off-plan market. Oyalowo (2025) supported this moral hazard problem with a model of effort disutility, which deduced that building defects are accentuated by marketing property projects before the completion of construction. Ogunbayo, et al (2016) further proposed a game-theoretic model, which shows that even defect warranties are of limited use to tackle moral hazard. The heterogeneous and latent features of housing are factors in the moral hazard that hinder the standardisation of real estate and make it prohibitively costly to specify the required quality in a forward contract completely. This difficulty of being standardised makes them more susceptible to moral hazard. Also, going by the models of Ogunbayo et al (2016), if the quality of pre-sale units is necessarily poorer than expected by buyers, then buyers would adjust their expectations (and thus the price) downward and so would developers lower the housing quality further. The process repeats and all pre-sale units eventually reach the minimal quality level (e.g., the minimum requirements imposed by the legislation or the maximum protection provided by warranties), giving rise to the adverse selection problem analysed (Olayiwole, 2023). This suggests that forward contracts hardly exist in real estate; however, the prevalence of the off-plan system in major markets globally suggests otherwise. The continued sustenance of the off-plan system is due to certain forces counteracting the moral hazard problem. Olayiwole, (2023) posited that the goodwill of a developer is valuable and thus counteracts moral hazard intents. In conclusion, by weighing the benefits gained and corresponding risks borne, it is apparent that an off-plan property contract has put developers in a more advantageous situation than the buyers. It enables them to transfer part of their project risks to other parties without incurring any loss, and can provide an opportunity to help them earn an abnormal return. On the other hand, off-plan property buyers must weigh the benefits against the additional risks incurred before deciding. (Katwa & Obala, 2023)

RESEARCH METHODOLOGY

This study investigates the challenges associated with off-plan real estate investment in the Lekki-Ajah axis of Lagos State. Data was collected from Estate Surveyors and Valuers within Lagos who are involved in real estate investment. Information was also sought from private real estate developers and stakeholders in real estate development industry. Personal visit was made to the study area and interview conducted on some of the occupiers of the off plan estates so as to gather relevant information. However, secondary data was also collected from textbooks, past theses, past journal papers and other academic work.

RESULTS AND FINDINGS

Findings show that most of the buyers or occupants of the case study area had previously brokered an off-plan real estate transaction. This was discovered from the information gathered and personal interview conducted on the occupiers of the study area.

It was also found out that buyers or occupants of the study area had brokered an off-plan transaction involving the sale of different types of buildings such as bungalows, apartments/flats, terraced houses, detached houses and semi-detached houses. The findings revealed that most buyers had brokered off-plan transactions involving various properties, with terraced houses being the most common.

It was also discovered that option to spread payment, buying at a lower price than the price of finished properties and the advantage of selling at a higher price on delivery (speculation) were common drivers of off-plan investment in the study area.

Furthermore, it was also discovered that the opportunity to select a unit before or during construction was available to buyers.

It was also discovered that, though the buyers had the opportunity to select a unit before or during construction, they did not have the opportunity to contribute to design and monitor the project from start to finish.

It was revealed that delay in delivery and loss of invested funds due to unscrupulous acts of the developer (e.g., paper allocation without subsequent physical allocation of units, overselling of the project, etc.) were barriers to off-plan real estate investment.

Loss of rent in the event of delayed delivery, loss of capital growth in the event of a refund, loss of investment in the event of construction collapse and abandonment of the project by the developers are also part of the challenges of off-plan real estate investment.

It was also found out that reduction in building specification (e.g., lesser living room size than advertised) and low construction quality/building defect were part of the challenges.

The use of substandard building materials, mismatches of fixtures and fittings, reduced number of facilities and change of investor's preferred unit by the developer were considered to also be a problem.

A change of preferred project location due to unforeseen construction challenges was also discovered as a problem of off-plan real estate investment.

Findings also revealed that there are initiatives such as developers dividing their projects into proportions and only selling off-plan after completing the preceding proportion (e.g., dividing a 100-unit project into 30-30-40, the second 30 units can only be sold on the completion of the first) which poses problems to off-plan sales and investment initiative.

It was also discovered that the defect liability period for off-plan projects is less than one year there is no concrete legislative framework to assure its implementation.

The problems of middlemen such as bankers, lawyers and agent holding funds paid by home buyers and releasing them to developers as development progresses was also discovered.

CONCLUSION

Based on the findings, the study concludes that there are significant and insignificant drivers and hindrances to adopting off-plan real estate investments. The findings show that the option to spread payment, buying at a lower price than finished properties, the advantage of selling at a higher price on delivery (speculation) and the opportunity to select a unit before or during construction are the highest drivers of off-plan. However, it is agreed that investors emphasise contribution, but it has little influence in the Lekki-Ajah real estate market of Lagos State. Moreover, it was observed that low construction quality and building defects are the main barriers to adopting the off-plan strategy. This study also found out that in the Lekki-Ajah market, investors in the off-plan market are more concerned with the danger of losing their capital than with building specific risks (expected reduction in building standard, mismatch of fixtures and fittings, lower number of amenities, etc.). Risks of significant importance to the Lekki-Ajah investors include delays in delivery, loss of invested funds due to unscrupulous acts of the developer (e.g., paper allocation without a subsequent physical allocation of units, overselling of the project, etc.), loss of capital growth in the event of a refund, abandonment of the project by the developer and loss of investment in the event of construction collapse. In the context of this study, investors prioritise financial risks (security of investment) more than construction quality.

To ensure the sustenance of the strategy as a property development and investment strategy, maximum attention must be paid to these drivers and the barriers actively eliminated. The developers may increase subscriptions by adopting marketing strategies that illustrate the benefits of off-plan investments. In addition, developers need to engage in comprehensive feasibility and viability appraisal of the project before venturing into them to identify the likely risk factors that may affect the delivery of the project. This will help avert delay in delivery, abandonment of the project and their resultant effects.

RECOMMENDATIONS

To increase the adoption, acceptability and effectiveness of off-plan real estate investments, the followings are recommended.

1. Developers are advised to always divide their projects into proportions and only sell off-plan after completing the preceding proportion as this is a strong driver to off plan investment.
2. The use of independent project manager who represents, monitors and reports to investors directly are strongly advised.

3. There should be a law regulating off plan sales and investment in the country especially in the study area and strict adherence and compliance be followed.
4. There should also be heavy sanction and penalty or huge fine on defaulters of any proposed law.
5. A provision of 'loss of deposit' insurance cover to off-plan investors is recommended to ensure that buyers' deposits are fully refunded in the case of the developer insolvency or negligence.
6. The defect liability period for off-plan projects should also be extended to minimum of one year or maximum two and a legislative framework to assure its implementation should be put in place.
7. The idea of middlemen holding funds paid by home buyers and releasing them to developers as development progresses should be discouraged as this will hinder the developers to plan.
8. The buyers should also be given the opportunity to contribute to design or monitor the project from time to time so as to be sure that the developers follow the design agreed upon at the initial stage.
9. Finally, Estate Surveyors and Valuers should be engaged to help carry out feasibility and viability appraisal of the project before venturing it.

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