

Beyond Stocks and Bonds: Striking Gold with Alternative Investments in Nigeria

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Introduction

Wealth management is a key component of financial planning aimed at holistically managing the wealth of individuals or families. With the constantly evolving economic landscape in Nigeria, effective wealth management is critical to preserving and enhancing wealth over the long term and achieving both financial and personal goals.

This article explores the concept of alternative investments within Nigeria, highlighting the role of diversification in wealth management. It discusses how alternative investments can mitigate the risks associated with traditional markets such as stocks and bonds; and provides practicable advice on incorporating these investments into a broader wealth management strategy.

The Concept of Wealth Management and Importance of Diversification

In Nigeria, wealth management is essential due to the nation's unique economic and regulatory environments. The importance of diversification is particularly clear in an economy heavily reliant on a single sector, such as oil. Nigeria's dependency on oil makes it vulnerable to global price shocks and downturns. By diversifying investments across sectors such as agriculture, technology, and manufacturing, economic risks can be spread and thereby mitigated. This approach reduces the risks associated with concentrating wealth in limited assets or sectors—a common practice among Nigerian investors.¹

Challenges of Traditional Investments and the Appeal of Alternatives in Nigeria

Traditional investments, such as stocks and bonds, face limitations within Nigeria's volatile market environment. Their performance is often impacted by interest rate fluctuations and general market instability.²

In contrast, alternative investments, including real estate, commodities, private equity, and infrastructural developments, offer a viable solution to counteract market instability and

¹ Nigeria Economic Update: Resilience through Reforms

<<https://www.worldbank.org/en/country/nigeria/publication/nigeria-economic-update-resilience-through-reforms> > accessed 6th June 2024

² Omorose A. Ogiemudia, Osagie Osifo and Igbinovia L. Eghosa “ Market Risk Factors and Stock Returns in the Nigerian Bourse” CBN Journal of Applied Statistics Vol. 13 No. 2 (December 2022) <

https://www.cbn.gov.ng/Out/2023/STD/A469_for_publication.pdf > accessed 28th May 2024

economic downturns. These alternatives could help diversify risks and have the potential to yield higher returns by tapping into emerging and less saturated markets. This strategic diversification is key for investors aiming to enhance the stability and profitability of their portfolios in such an unpredictable environment.

Overview of Alternative Investments

Alternative investments represent a distinct category separate from the traditionally publicly traded assets like stocks, bonds, and cash.³ This category also includes non-traditional investment strategies utilized within specific vehicles like private equity funds and hedge funds. These investments are often more complex and trade less frequently than their conventional counterparts, offering diverse sources of potential returns.

The definition of alternative investments can vary depending on the context. For example, the Chartered Alternative Investment Analyst Association (CAIA), a global association, categorizes them into several classes, including private equity, real estate, private debt, hedge funds, and various structured products. This classification provides a framework for understanding the expansive and dynamic nature of alternative investments, which is crucial in both legal and financial advisory contexts.⁴

Types of Alternative Investments in Nigeria

- a. **Real Estate⁵:** Real estate is a staple in the Nigerian investment scene, offering direct acquisitions such as property purchases or indirect investments through real estate funds.
 - **Direct Real Estate Investments:** Investors benefit from rental income, property appreciation, and potential business profits. For example, properties in prime areas like Ikoyi, Lagos, have appreciated by about 113% between 2021 and 2023 due to high demand for luxury spaces.⁶

³ CFA Institute, 'Introduction to Alternative Investments' (2023) CFA Institute
<<https://www.cfainstitute.org/en/membership/professional-development/refresher-readings/introduction-alternative-investments/>> accessed 29th May 2024

⁴ Donald Chambers, Mark Anson, Keith Black, Hossein Kazemi. Alternative Investments- CAIA Level 1. J. Wiley & Sons (2020)

⁵ Olanrele, O. O., Said, R., and Daud, N. 'An evaluation of the performance and acceptability of REIT in Nigeria.' (15th African Real Estate Society (AFRES) Annual Conference, Golden Tulip, Kumasi, Ghana, 31st August – 3rd September 2015) pp. 269-286.

⁶ <<https://www.thisdaylive.com/index.php/2023/11/20/report-ikoyi-recorded-113-rise-in-value-of-land-in-two-years/>> accessed 22nd June 2024.

- **Indirect Real Estate Investments:** Real Estate Investment Trusts (REITs) allow participation in the real estate market without direct property management. REITs pool funds to purchase, manage, and operate properties, providing dividend-based income and portfolio diversification.
- **Innovative Real Estate Opportunities:** The sector is also evolving with innovative housing solutions and smart buildings, poised for growth.

Both direct ownership and REITs in the Nigerian real estate market present significant opportunities for asset appreciation and income generation, essential for a diversified investment portfolio.

- Private Equity:** Private equity in Nigeria involves investing in private enterprises, ranging from emerging startups to well-established firms seeking expansion capital. With the Nigerian government prioritizing infrastructure development, significant investment opportunities are emerging in sectors such as transportation, haulage, utilities, and telecommunications. These opportunities provide private equity investors with a potential for substantial returns.
- Hedge Funds:** Hedge funds are investment funds that use a variety of strategies to earn higher returns for their investors. These strategies can include using financial tools like derivatives, borrowing money to invest (leverage), and betting against stocks (short selling). In Nigeria, hedge funds are smaller and less developed compared to global markets, but they offer growing opportunities, especially by focusing on local market conditions. They are usually designed for sophisticated investors, such as wealthy individuals and large institutions, who are comfortable with higher risks and longer investment timelines.
- Commodities:** This type of investment covers physical goods such as agricultural products or oil. In Nigeria, commodities include local resources like crude oil and agricultural products⁷ including cocoa and palm oil. These investments can act as inflation hedges and provide additional diversification within an investment portfolio.
- Sustainable and Green Investments:** There is a growing interest in renewable energy, sustainable agriculture, and green real estate projects in response to global climate

⁷ <<https://businessday.ng/agriculture/article/boosting-cocoa-oil-palm-production-to-drive-nigerias-economic-growth/>> accessed 30th May 2024

concerns. Nigeria, with its vast natural resources and need for sustainable development, offers fertile ground for these investments.

- f. **Cultural and Creative Sectors:** The Nigerian film and music industries, part of the broader creative sector, present unique investment opportunities. As cultural exports continue to grow in popularity worldwide, investments in these areas are not only profitable but also promote Nigerian culture globally.

Advantages of Including Alternative Investments in a Portfolio

Incorporating alternative investments into a portfolio provides multiple benefits that enhance individual financial security and contribute to the broader growth of the Nigerian economy:

- a. **Enhanced Returns:** Alternative investments often present opportunities for higher returns compared to traditional investments. For example, private equity investments in emerging sectors like Nigerian tech startups have shown significant potential for growth.
- b. **Inflation Hedge:** Real assets, such as real estate and commodities, generally track inflation closely, helping to preserve purchasing power. In an economy like Nigeria's, where inflation is a concern, these assets offer a crucial safeguard.
- c. **Economic Growth:** Investing in sectors like real estate, infrastructure, and startups drives economic development. Funding new infrastructure projects can enhance efficiency and productivity, while investments in startups promote innovation and generate employment opportunities.
- d. **Portfolio Stability:** Including assets that typically perform well during economic downturns, such as gold or real estate, can help reduce the overall volatility of a portfolio. This diversification provides greater stability during uncertain times, safeguarding investors' capital.

Practical Strategies for Diversifying Portfolios with Alternative Investments

Here are some effective strategies to consider:

1. **Diverse Asset Allocation:** Spread investments across different asset types such as real estate, private equity, hedge funds, commodities, and collectibles to reduce overall risk.
2. **Geographic and Sector Diversification:** Invest in different geographic regions and sectors to capitalize on varying economic dynamics and growth opportunities. In

Nigeria, sectors like technology, healthcare, and renewable energy present significant growth prospects.

3. **Hedging:** Use financial instruments like derivatives to protect against significant losses in unstable markets. Hedging strategies can help stabilize a portfolio by offsetting losses in one investment with gains in another.
4. **Set and Monitor Risk Limits:** Establish clear risk parameters that align with investment objectives and tolerance levels. Regular monitoring and adjustment of these limits are crucial to ensuring that the portfolio remains aligned with changes in market conditions or the investment landscape.

Navigating the Future of Alternative Investments

As Nigeria's economy evolves, alternative investments bring promising opportunities. Key trends highlight significant growth in technology-driven investments, sustainable projects, and expansions in private equity and real estate. These opportunities are fueled by both local and international interest in diverse and resilient investment options.

For more information about the legal implications of diversifying your investment portfolio or exploring new alternative investment avenues, reach out to: info@scp-law.com or visit our website at www.scp-law.com.