Real Estate Listings in Kenya, & Cytonn Weekly #32

Cytonn Weekly

Executive Summary

- Fixed Income: Yields on Treasury bills were on an upward trend with the 91, 182 and 364-day papers coming in at 8.5%, 10.8% and 11.7% from 8.3%, 10.7% and 11.4%, respectively. The Central Bank of Kenya (CBK) this week developed a draft guidance note on the Internal Capital Adequacy Assessment Process (ICAAP) that seeks to enable institutions (banks and mortgage finance institutions) in determining the level of capital adequacy cover;
- Equities: During the week, the Kenyan equities market closed on a downward trend with NASI, NSE 25 and NSE 20 declining by 0.1%, 0.5% and 0.9%, respectively. National Bank of Kenya, HF Group and CfC Stanbic Holdings released their H1?2016 results;
- Private Equity: ICT infrastructure investments continue to attract private equity capital in the Sub-Saharan Africa region, as Emerging Africa Infrastructure Fund loans USD 20 mn to Helios Towers Africa as part of a USD 105 mn syndicated loan;
- Real Estate: The establishment of the Leather Industrial Park (?LIP?) in Kinanie, Machakos County, reached a major milestone, with the establishment of Phase 1 of the 500-acre development. The development will create jobs for 35,000 people.

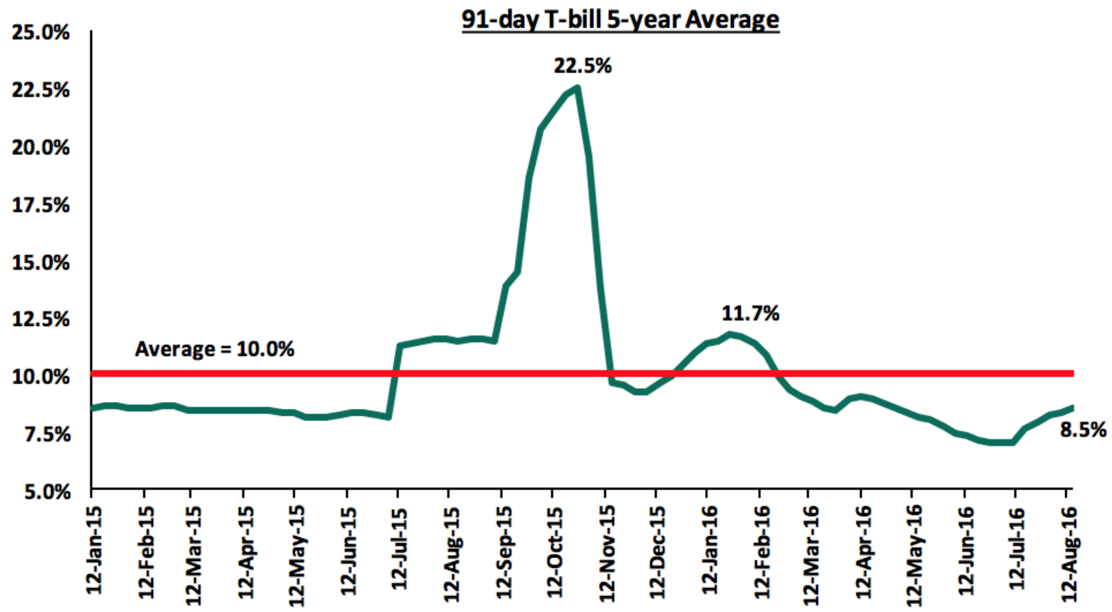
Company Updates

- Cytonn Investments Management Limited, our Group Holding Company, together with Cytonn Cash Management Solutions LLP, our private wealth affiliate, will be holding their Annual General Meeting on Thursday, August 25th at 7:30 am
- Cytonn Investment Co-operative membership recruitment drive is still on. For more information, please see the link: Cytonn Cooperative. The Cytonn Co-operative is registered under The Co-operative Societies Act of Kenya, 2004. The co-operative allows members to access above average market returns that have previously been accessible only to our private wealth investors. To join, please contact us at coop@cytonn.com or download the forms from the website on this link: Cytonn co-operative forms
- To invest in any of our current or upcoming real estate projects, please visit Cytonn Real Estate. We continue to see very strong interest in our products, particularly The Alma, which is now 50% sold and has delivered an annualized return for 55% p.a. for investors who bought off-plan. We have 12 investment ready projects, offering attractive development returns and buyer's returns of a minimum of 25% p.a. See further details here: Summary of investment ready projects
- Given the rapid growth of Cytonn Investments that we have seen over the last 2 years, we are recruiting a Chief Operating Officer to oversee ongoing business operations within the company, and develop a strategic support services function. We also continue to beef up the team with several ongoing hires: Careers at Cytonn.

Fixed Income

During the week, T-bills were oversubscribed with a subscription rate of 183.5%, compared to 219.6% recorded the previous week. There is still a lot of interest on the short-term bills with the subscription rate for the 91-day, 182-day and 364-day papers at 350.4%, 179.3% and 76.5%, down from 379.4%, 210.9% and 87.5%, respectively, the previous week. The oversubscription for the 91-day and 182-day papers indicate that investors are focusing more on the short-term papers as they anticipate rates to rise in the short-term. Yields increased across all tenors with the 91, 182 and 364-day papers increasing to 8.5%, 10.8% and 11.7% from 8.3%, 10.7% and 11.4%, respectively.

The 91-day T-bill is currently trading below its 5-year average of 10.0%, having witnessed a downward trend in the previous three months towards the close of the last fiscal year. The downward trend for the 91-day paper has since reversed and we have seen a 146.2 bps increase over the last one month. The upward pressure on rates is as a result of Government borrowing given the new fiscal year.



In line with the Securities Issuance Calender released last week, the government will be issuing a 10-year fixed coupon bond to raise Kshs. 25.0 bn for budgetary support. We shall be giving our recommendation on the bond in our Cytonn Weekly #33.

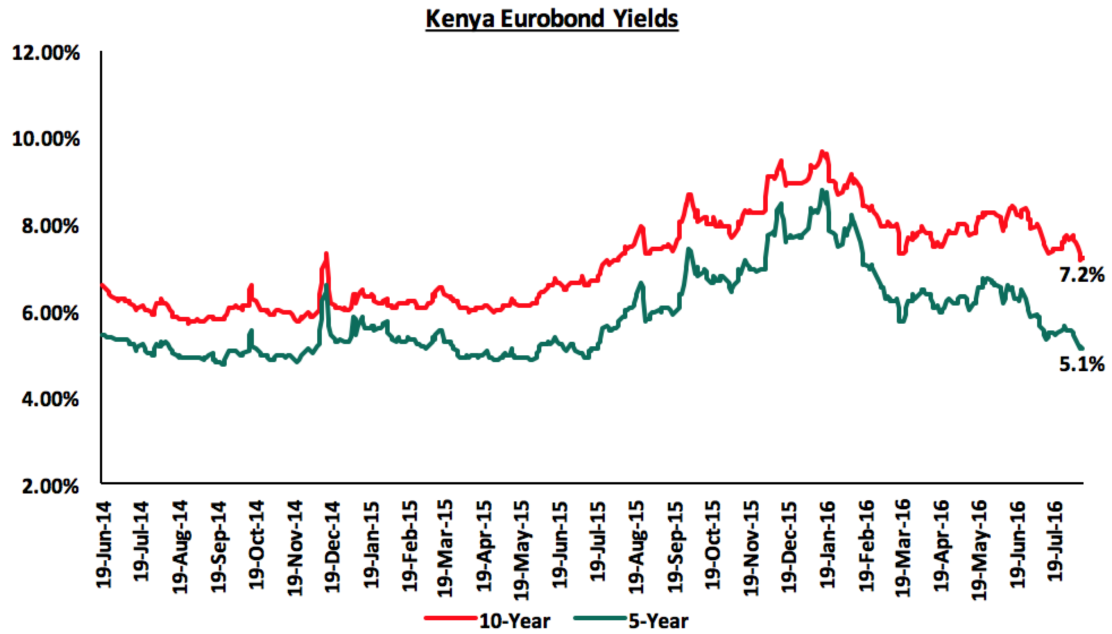
The Central Bank Weekly report revealed that the interbank rate decreased by 60 bps to 5.4%, from 6.0% the previous week, despite a net liquidity reduction of Kshs 30.4 bn. The liquidity reduction was as a result of Term Auction Deposits and payment of taxes by Banks of Kshs 28.1 bn and Kshs. 19.2 bn, respectively. As highlighted in our Cytonn Weekly Report #28 the interbank rate is often determined by the liquidity distributions within the banking sector as opposed to the net liquidity position in the interbank market.

Below is a summary of the money market activity during the week:

all values in Kshs bn, unless stated otherwise			
Weekly Liquidity Position ? Kenya			
Liquidity Injection		Liquidity Reduction	
Term Auction Deposit Maturities	0.0	T-bond sales	0.0
Government Payments	12.9	Transfer from Banks ? Taxes	19.2
T-bond Redemptions	0.0	T-bill (Primary issues)	28.1
T-bill Redemption	0.0	Term Auction Deposit	0.0
T-bill/T-bond Rediscounting	0.0	Reverse Repo Maturities	0.0
T-bond Interest	0.0	Repos	0.0

Reverse Repo Purchases	0.0		
Repos Maturities	4.0		
Total Liquidity Injection	16.9	Total Liquidity Withdrawal	47.3
		Net Liquidity Injection	(30.4)

According to Bloomberg, yields on the 5-year and 10-year Eurobonds issued in 2014 declined week on week by 0.3% and 0.4% to 5.1% and 7.2%, respectively, from 5.4% and 7.6% last week, respectively. Since the mid ? January 2016 peak, yields on Kenyan Eurobond have declined by 3.7% and 2.5% on account of improving macroeconomic conditions. This is an indication that Kenya remains an attractive investment destination.



The Kenya Shilling depreciated against the dollar by 0.2% this week to 101.6, on account of dollar demand from players in the energy sector. On a year to date, the shilling has appreciated by 1.0%. We expect the shilling to remain relatively stable for the remainder of the year supported by (i) the high levels of foreign exchange reserves equivalent to 5.1 months of import cover, and (ii) improved diaspora remittances, with cumulative 12 months? diaspora inflows to June 2016 increasing by 11.0% to USD 1.7 bn from USD 1.5 bn in the year to June 2015.

During the week, Members of Parliament rejected a proposal by Kenya Bankers Association on behalf of the commercial banks to counter the passage of the interest rate cap bill, the proposal would have put in place the following measures in a bid to stop the capping of interest rates:

1. Collectively pool funds equal to Kshs 30.0 bn that will go towards lending to Small and Medium Enterprises (SMEs) at 14.5% or lower;
2. Contribute Kshs 100.0 mn towards helping SME?s obtain financing by giving them technical assistance;
3. Pledge to cut lending rates by 1.0% or slightly more with immediate effect in line with the Kenya Banks? Reference Rate (KBRR) that was reduced to 8.9% from 9.9%. The first commercial banks to announce their intention to comply were I&M Bank, Standard Chartered Bank Commercial Bank of Africa and;
4. Cancel bank closure charges for customers to enable them move across banks easily.

The banks planned to contribute to the funds continually in proportions based on their SME lending, as explained in a Memo to the governor of the Central Bank of Kenya (CBK). This comes in a week after a bill was passed by the Members of Parliament to amend the Banking Act by placing restrictions on the rate at which banks offer loans and pay for deposits. The amendment was to put (i) a cap on lending rates at 4.0% above the Central Bank Rate (CBR) and (ii) a floor on the deposit rates at 70.0% of the CBR. We did a note on the same: The Impact of Capping Interest Rates on the Kenyan Economy. The move to cap interest rates would (i) put a strain on smaller banks, (ii) lead to the emergence of shadow banking systems and (iii) control the spread that banks can earn on lending; all of which bankers are trying to evade. The proposition by the banks however failed to address the fact that the high lending rates are mainly brought about by the continuous high domestic borrowing by the government which offers a higher return and is considered a non-defaulter hence posing no risk to the banks. Instead, the proposition sought to provide short term solutions to a long term problem which was not enough to deter the decision by the Members of Parliament.

The Central Bank of Kenya (CBK) has developed draft guidelines on Internal Capital Adequacy Assessment Process (ICAAP) that seeks to enable institutions (banks and mortgage finance institutions) in determining the level of capital adequate to cover for their respective risks. Under the guideline all institutions (banks and mortgage finance institutions) are required to formulate their own ICAAP that ensures that overall internal capital levels are adequate and consistent with their strategies, business plans, risk profiles and operating environments on a going concern basis. Though the CBK acknowledges that there is no single correct approach to conduct the ICAAP, their focus on guidance will lead to better supervision of the financial system as they have to review and evaluate the soundness of an institutions ICAAP. Under the CBK guidelines, an effective ICAAP should comprise of (i) Corporate Governance oversight, (ii) Sound capital planning, (iii) comprehensive identification and assessment of risk, (iv) stress testing, (v) monitoring and reporting, and (vi) internal control review. We believe this move by the Central Bank will lead to improved supervision and ease with which the CBK conducts its supervisory role as they involve the financial institutions in this process and they don?t have to handle it on their own. Subsequently, this will also lead to banks being required to have a capital base depending on the amount of risk appetite they possess. This move is commendable as each bank is unique and will be able to manage based on their peculiar business strategy.

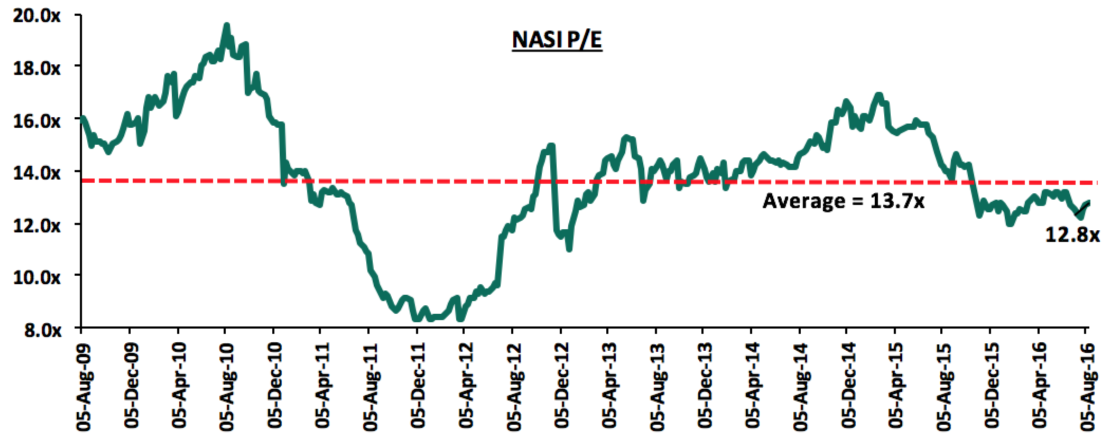
The government is ahead of its domestic borrowing for this fiscal year having borrowed Kshs 26.9 bn for the current fiscal year against a target of Kshs 26.4 bn (assuming a pro-rated borrowing throughout the financial year of Kshs 229.6 bn budgeted for the full financial year). Interest rates have bottomed out and we are currently witnessing upward pressure on interest rates given government borrowing for the new fiscal year. It is due to this that we advise investors to be biased towards short to medium-term papers.

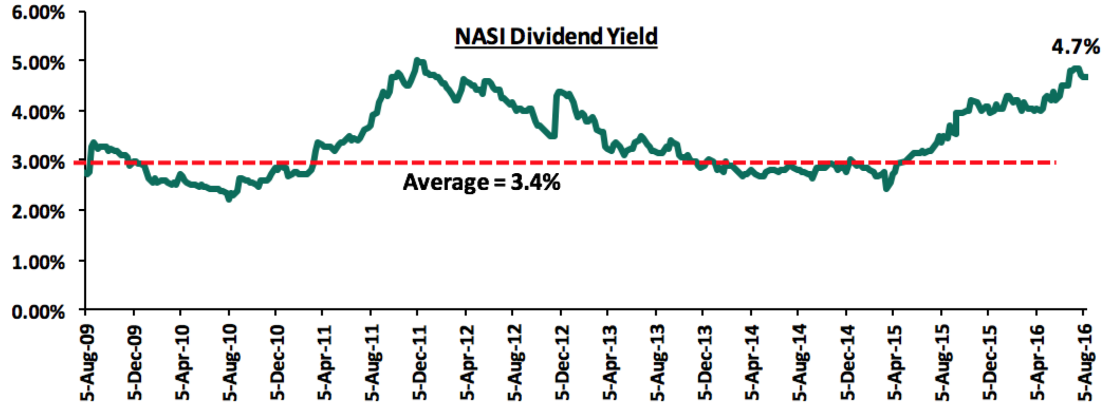
Equities

During the week, the Kenyan equities market closed on a downward trend with NASI, NSE 25 and NSE 20 declining by 0.1%, 0.5% and 0.9%, respectively, with the YTD performance coming in at (1.3%), (6.4%) and (14.6%). The week?s performance was as a result of large cap stocks such as Diamond Trust Bank, EABL and Standard Chartered Bank losing 1.8%, 1.1% and 0.5%, respectively. Since the February 2015 peak, the market has lost 37.3% and 19.0% for NSE 20 and NASI, respectively.

Equities turnover declined by 53.9% to Kshs 1.8 bn from Kshs 3.9 bn the previous week as the foreign investor participation declined to 55.9% from 68.4%. Foreign investors were net buyers with net inflows of USD 4.5 mn, compared to a net inflow of USD 8.5 mn recorded the previous week. Safaricom was the top mover during the week accounting for 27.2% of the market activity and gaining 1.0%. With Q3?2016 in its second month, companies have started releasing their half-year results with WPP Scangroup, BAT Kenya, CIC Group, KCB Group, KenolKobil Group, HF Group, National bank and CfC Stanbic Holdings having already released their results. We maintain our expectation of stronger earnings in 2016 compared to 2015, with an estimated growth of 12.5%, supported by a favorable macroeconomic environment. Given the low valuations, long-term investors should gradually be taking positions in the market.

The market is currently trading at a price to earnings ratio of 12.8x, versus a historical average of 13.7x, with a dividend yield of 4.7% versus a historical average of 3.4%. The charts below indicate the historical PE and dividend yields of the market.





Housing Finance Group released H1?2016 results:

HF Group released their H1?2016 results recording core earnings per share (EPS) growth of 26.3% to Kshs 1.8 from Kshs 1.4 in H1?2015, against our projection of Kshs 1.5. The growth in EPS was driven by a 23.9% growth in operating revenue which outpaced an 18.6% growth in total expenses.

Key highlights include:

- Total operating revenue grew by 23.9% to Kshs 2.5 bn from Kshs 2.0 bn in H1?2015 driven by net interest income growth of 21.8% to Kshs 2.1 bn from Kshs 1.7 bn in H1?2015, supported by a 21.5% growth in interest income. Interest expense grew by 21.5% to Kshs 2.4 bn from Kshs 2.0 bn in H1?2015 driven mainly by the spillover effects of the high interest rates environment witnessed in Q3? 2015. Net interest Margin stood at 3.5% from 2.9% in H1?2015
- Non-interest income grew by 35.8% to Kshs. 416.9 mn, from Kshs 306.9 mn in H1?2015, supported by the continued sale of HF Development and Investment (HFDI) real estate inventory, which continues to supplement the core mortgage and banking business of HF Group. The current revenue mix stands at 83.3% Funded to 16.7% Non-Funded Income, respectively
- Total operating expenses grew by 18.6% to Kshs 1.6 bn from Kshs 1.4 bn on account of a surge in amortization costs associated with the new core banking system and a 235.7% rise in rental expenses associated with the 6 new branches HF Group opened within H1'2016
- Loan loss provisions grew by 7.6% to Kshs 305.0 mn from Kshs 283.4 mn despite non-performing loans increasing by 29.0% to Kshs 5.4 bn from Kshs 4.2 bn. Cost to income ratio improved to 64.4% from 67.4% in H1?2015
- PAT growth came in at 26.3% to Kshs 612.6 mn from Kshs 485.1 mn in H1?2015.

HF Group performance was above expectations, with a strong top line growth. HFC, the banking arm, continues to dominate overall contribution, at 99.6% of the group?s PAT. However, HF Group registered slower balance sheet growth, with 6.2% deposit growth and 7.0% loan growth, resulting into a loan to deposit ratio of 134.5%, raising concerns on its ability to gather deposit. Through HFDI, HF Group is sufficiently diversifying its income streams as seen by the 35.8% growth in NFI. Going forward, we expect HF Group to leverage on the new banking system, to support the growth of the core business, HFC. However, diversification through HF Development and Investment and HF Insurance Agency will continue to support long term growth.

For a more comprehensive analysis, see our HF Group H1?2016 Earnings Note.

National Bank of Kenya released H1?2016 results:

NBK released their H1?2016 results, and recorded a core earnings per share (EPS) decline of 70.0% to Kshs 1.0 from Kshs 3.4 in H1?2015 (stripping the one-off gain of Kshs. 0.7 bn through the sale of buildings) against our projection of Kshs 1.9. The decline in EPS was driven by a 46.1% growth in operating expenses that was faster than the growth in operating income of 12.6%.

Key highlights include:

- Total operating revenue grew by 6.3% to Kshs 5.8 bn in H1?2016 from Kshs 5.5 bn in H1?2015 (stripping the one off gain from sale of buildings), driven by a 16.9% growth in net interest income. This was supported by (i) an 8.7% growth in interest income to Kshs 7.0 bn from Kshs. 6.4 bn in H1?2015, and (ii) a 3.2% decline in interest expense to Kshs. 2.5 bn from Kshs 2.6 bn in H1?2015. Net interest margin decreased to 7.2% in H1?2016 from 7.9% in H1?2015
- Non-Funded Income recorded a decrease of 17.8% (stripping the one-off gain from sale of buildings) to Kshs 1.4 bn from Kshs 1.7 bn in H1?2015. This decline was as a result of poor performance of Non Funded Income items such as fees and commissions on loans, other fees and commissions, and forex income, which declined by 65.7%, 7.9%, and 22.0%, respectively. The current revenue mix stands at 76:24 Funded to Non-Funded Income
- Total operating expenses grew by 46.1% to Kshs 5.4 bn in H1?2016 from Kshs 3.7 bn in H1?2015 driven by a 385.9% rise in loan loss provision despite the decline in staff costs by 2.5%. The high growth in expenses resulted in a significant increase in cost to income ratio to 92.4% from 59.7% in H1?2015
- Reported PAT declined by 82.0% to Kshs 311.3 mn from Kshs 1.7 bn in H1?2015 compared to our expectations of a 66.5% decline.

We are of the opinion that NBK?s growth going forward will be propelled by (i) their ability to raise funds to shore up their capital requirements which are below Central Bank?s minimum statutory requirements in order to meet the required threshold and be able to grow the loan book, (ii) their management of expenses which will enable the bank to control the run-away cost to income, which currently stands at 92.4%, the highest in the industry, (iii) removing the overhand associated with the conversion of the preferred shares as investors need clarity around the conversion terms, and (iv) improving sentiment towards the bank by clearing out on issues of corporate governance that had resulted in ballooning of Non-performing loans within the lender.

For a more comprehensive analysis, see our National Bank H1?2016 Earnings Note.

CFC Stanbic Holdings released H1?2016 results:

CfC Stanbic Holdings released their H1?2016 results recording core earnings per share (EPS) growth of 22.2% to Kshs 6.1 from Kshs 5.0 in H1?2015 against our projection of Kshs 6.9. The growth was driven by a 22.0% growth in total operating income to Kshs 9.4 bn from Kshs 7.7 bn, outpacing an 18.7% rise in operating expenses.

Key highlights include:

- Total operating income grew by 22.0% to Kshs 9.4 bn from Kshs 7.7 bn in H1?2015 driven by a 24.4% growth in net interest income to Kshs 5.5 bn from Kshs 4.4 bn in H1?2015. The rise in net interest income was as a result of a 24.7% rise in interest income from loans and advances to Kshs 6.1 bn from Kshs 4.9 bn in H1?2015, recorded by CfC Stanbic Bank. Net Interest Margin came in at 5.6% compared to 5.3% in H1?2015
- Non-funded income (NFI) recorded an 18.8% rise to Kshs 4.0 bn from Kshs 3.3 bn in H1?2015 against our expectation of a 12.6% growth driven by a 17.1% increase in foreign exchange trading income to Kshs 1.5 bn from Kshs 1.3 bn in H1? 2015 recorded by CfC Stanbic Bank. Revenue mix stood at 57.9% Funded and 42.1% Non-Funded Income
- Total operating expenses grew by 18.7% to Kshs 5.8 bn from Kshs 4.9 bn in H1?2015 on account of 246.1% rise in loan loss provision to Kshs 0.8 bn from Kshs 0.2 bn in H1?2015. Cost to Income ratio came in at 61.7% from 57.1% in H1?2015
- PAT grew by 22.2% to Kshs 2.4 bn from Kshs 2.0 bn in H1?2015.

CfC Stanbic Holdings earnings were driven by a strong core performance with both Funded and Non-Funded Income recording growths of 24.7% and 18.8%, respectively. However, the bank is still highly dependent on the Non-Funded Income accounting for 42.1% of the operating revenue. Of this, 37.8% is from forex income from their South Sudan business, which has been volatile in the past years. South Sudan now contributes 10.0% of the group?s revenue, a strong improvement from the 4.0% in H1?2015 despite the political instability in the country. In order for CfC Stanbic Holdings to record stable earnings, we believe they should firm up their core banking business and fully adopt alternative channels of distribution such as agency and mobile banking.

For a more comprehensive analysis, see our CfC Stanbic Holdings H1?2016 Earnings Note.

Below is a list of the listed banks that have released H1?2016 results with the recorded Core EPS growth for H1?2016 in comparison to H1?2015;

Banks H1'2016 EPS Growth		
Bank	H1'2015	H1'2016
KCB Group	13.1%	13.6%
HF Group	2.3%	26.3%
National Bank of Kenya	123.1%	(70.0%)
CfC Stanbic Holdings	(41.6%)	22.2%
Average*	2.1%	14.7%
**-Market Cap Weighted*		

Britam Holdings has bought out Kenya Farmers Association?s (KFA) 1.0% stake in Real Insurance Company at Kshs 14.6 mn, to become the sole owner. Real Insurance will now be incorporated into Britam?s existing business. In August 2014, Britam acquired 99.0% of Real Insurance Company (K) Limited funded through a cash payment of Kshs 825.0 mn and shares worth Kshs 550.0 mn. In September 2015, Real Insurance Company shareholders approved a name change to Britam Insurance Company Limited to ride on Britam?s strong brand and regional presence. Britam has presence in Kenya, Malawi, Mozambique Rwanda, South Sudan, Tanzania and Uganda and the 100% ownership is in line with its regional expansion strategy as the company looks to broaden its reach in these countries. Real Insurance Company (K) owns a 65.0% stake in Real Insurance Company of Malawi that is listed on the Malawi Stock Exchange, a stake which Britam will now own, enabling expansion in Malawi. Britam already has a footing in Malawi, dealing in general insurance business with three main products. Real Insurance Company of Malawi also offers general insurance products but has a stronger foothold in Malawi, having existed in the country since 1959 as Royal Insurance Company of Malawi. This move is strategic for Britam to hasten its expansion in Malawi and strengthen its holding in the country.

The UK Government development fund, CDC Group, will acquire a 10.68% stake in I&M Holdings as approved by the Competition Authority of Kenya (CAK) during the week, joining the top four largest shareholders list. CDC Group will purchase 6.25% and 4.43% from DEG ? a German investment and development company - and PROPARCO ? a Paris-based development financial institution, respectively as detailed in our Cytonn Weekly Report #16. CDC?s financial sector experience and expertise could play a role in improving I&M Holding?s strategy.

Below is our equities recommendation table. Key changes from our previous recommendation are:

- Liberty has moved from an ?Accumulate? recommendation, with an upside of 19.0% to a ?Buy? recommendation with an upside of 26.0%, following a 5.5% w/w price decline
- I&M Holdings has moved from a ?Lighten? recommendation, with an upside of 4.1% to an ?Accumulate? recommendation with an upside of 10.0%, following a 5.6% w/w price decline

all prices in Kshs unless stated									
EQUITY RECOMMENDATION									
No.	Company	Price as at 05/08/16	Price as at 12/08/16	w/w Change	YTD Change	Target Price*	Dividend Yield	Upside/ (Downside)**	Recommendation
1.	KCB Group***	32.0	32.5	1.6%	(25.7%)	49.4	6.2%	58.2%	Buy
2.	Bamburi	165.0	165.0	0.0%	(5.7%)	232.0	8.1%	48.7%	Buy
3.	Kenya Re	19.8	19.9	0.5%	(5.5%)	26.7	3.8%	38.3%	Buy
4.	Centum	43.5	42.3	(2.9%)	(9.1%)	57.2	2.3%	37.6%	Buy
5.	HF Group	19.1	17.4	(8.7%)	(21.8%)	21.6	6.5%	30.7%	Buy
6.	ARM	32.0	30.5	(4.7%)	(26.9%)	39.7	0.0%	30.2%	Buy
7.	DTBK***	163.0	160.0	(1.8%)	(14.4%)	204.2	1.6%	29.2%	Buy
8.	Liberty	14.5	13.7	(5.5%)	(30.0%)	17.2	0.0%	26.0%	Buy
9.	CIC Insurance	4.3	4.0	(5.9%)	(35.5%)	4.7	2.2%	19.7%	Accumulate
10.	Barclays	9.9	10.0	1.0%	(26.8%)	10.9	10.0%	19.5%	Accumulate
11.	BAT (K)	859.0	858.0	(0.1%)	9.3%	970.6	6.3%	19.4%	Accumulate
12.	Co-op Bank	14.4	14.4	0.3%	(20.0%)	16.0	5.4%	16.5%	Accumulate
13.	NIC	32.3	31.8	(1.6%)	(26.6%)	35.7	3.9%	16.4%	Accumulate
14.	Equity Group	38.0	38.3	0.7%	(4.4%)	42.1	5.4%	15.5%	Accumulate
15.	Britam	13.3	12.5	(6.0%)	(3.8%)	14.1	2.3%	15.1%	Accumulate
16.	CfC Stanbic	82.5	80.0	(3.0%)	(3.0%)	83.6	7.5%	12.0%	Accumulate
17.	I&M Holdings	108.0	102.0	(5.6%)	2.0%	109.5	2.7%	10.0%	Accumulate
18.	Standard Chartered***	209.0	208.0	(0.5%)	6.7%	208.6	8.2%	8.5%	Hold
19.	Jubilee Insurance	474.0	470.0	(0.8%)	(2.9%)	477.8	1.8%	3.5%	Lighten
20.	Pan Africa	38.0	38.0	0.0%	(36.7%)	39.0	0.0%	2.6%	Lighten
21.	Safaricom	19.8	20.0	1.0%	22.7%	16.6	4.0%	(13.0%)	Sell
22.	NBK	8.7	7.5	(14.4%)	(52.7%)	5.4	0.0%	(27.5%)	Sell
**Target Price as per Cytonn Analysts estimates*									
***Upside / (Downside) is adjusted for Dividend Yield*									
****Indicates companies in which Cytonn holds shares in*									
Accumulate ? Buying should be restrained and timed to happen when there are momentary dips in stock prices.									
Lighten ? Investor to consider selling, timed to happen when there are price rallies									

We are neutral with a bias to positive on Equities given the higher earnings growth prospects, supported by a favorable macroeconomic environment.

Private Equity

Emerging Africa Infrastructure Fund (?EAIF?), a donor-backed private infrastructure development group, has loaned USD 20 mn to Helios Towers Africa (?HTA?), as part of syndicated loan worth USD 105 mn, to finance the purchase of approximately 950 telecommunications towers in the Democratic Republic of Congo (DRC). EAIF is a leading investor in digital communications infrastructure in Sub-Saharan Africa, with this being it?s fifth partnership with HTA due to its skilled, dependable, reliable and wholly supportive management.

The investment in advance telecommunication will be vital in unlocking more of DRC?s potential, supporting and boosting enterprise and business growth in the country by: (i) bringing remote communities into the economic mainstream through telecommunications, (ii) opening up markets to existing businesses, (iii) providing quick and reliable payments systems, (iv) improving financial inclusion through the payments systems, and (v) stimulating new business creation, especially in e-commerce and retail payments, that boosts national economic growth. This active participation of

EAIF and HTA?s in the telecommunication industry has proven to widen consumer choice that helps develop more competitive telco markets, resulting to enhanced national economic development.

The growth in the telecommunications sector is being driven by the increasing working population, demand for improved efficiency in service delivery and demand for capacity to carry out more services by telco firms, which is also evident from the over 6,500 towers across Africa that are owned by HTA.

Real Estate

Earlier in the week, the Kenyan Government announced that it was in the process of shortlisting the 10 applications it received from investors who want to set up tanneries within the 500-acre Leather Industry Park (?LIP?), which is to be located In Kinanie which is in the Athi River area of Machakos County, currently managed by the Export Promotions Zone Authority (?EPZA). The National Environmental Management Authority (NEMA) concerns, which had previously been raised over pollution of Athi River, have been addressed by the plans to have a common effluent treatment plant whereby all effluent will be released to Athi River after treatment. The actualization of the LIP will boost the real estate industry within Kinanie area and its vicinity as a result of:

I. Improved infrustructure, which will be developed in the Athi River area, especially with the development of the interior roads such as Kenol-Kangundo Road and Makutano-Kitui Road off Mombasa road
II. Influx of skilled workers and casual labourers to an approximate number of over 35,000 persons, who will directly be employed in the LIP,
III. Other than the LIP, Athi River presents an attractive residential destination for home-owners seeking a greater quality of life, while being able to commute to work in the Nairobi Central Business District.

Despite technology advancement, the Textile, Clothing, Leather and Footwear (TCLF) subsector still remains one of the most labour intensive industries. Seasonal demand for the finished products and high demand for cheap labour drives the high reliance on labour contractors. The impliaction of this is that the employees in the tanneries will be lower end income earners hence they will prefer to rent houses within the vicinity to keep on transport costs at a minimum and also due to lack of job security. Therefore, there is a great opportunity of provision of affordable rental houses, and a lack of this would result in mushrooming of slums around the area. Cytonn Real Estate has a futuristic mixed use masterplan development in this neighbourhood dubbed Newtown. This will complement the LIP initiative as the city features a logistic park that will come handy for packaging further enhancing the value of the goods.

In further news positively impacting infrustructure development, the Transport Cabinet Secretary announced the plans by Government to construct an elevated highway in Nairobi from the Jomo Kenyatta International Airport (JKIA) to Rironi in Limuru which is approximately 25km North West of Nairobi. The three-phased project seeks to easen traffic snarl up currently experienced along the busy highway, although this comes at a cost the the road users, which is a toll fee approximated to be between Kshs 500 to Kshs 1,000 per vehicle for those users who wish to evade heavy traffic. The cost of the project is approximated to be Kshs 140 bn, and commencement of the first phases pegged on funding from the World Bank and the African Development Bank. In addition to this highway, the Western Bypass, at design stage, will further open up neighbourhoods such as Kikuyu and its environs, which primarily have been utilized for agricultural purposes. We therefore anticipate escalation of property prices in the parts of Kiambu and Nairobi served by the highways resulting from improved accessibility to the CBD. Currently the land prices in Kikuyu average at Kshs 50 mn per acre, and this varies depending on the lands proximity to the Southern Bypass and Nakuru-Nairobi Highway. Monthly rent for 2-bedroom apartments is approximately Kshs 33,000, while that of a 3-bedroom unit is approximately is Kshs 45,000. The average price for 2 and 3-bedroom units are Kshs 6.6 mn and 8.3 mn, respectively. The average price appreciation rate for apartments in the area is 14.84% p.a. and a rental yield of 6.34%, hence an investor can realise a total return of 21.18%

The Kenya Tourism Regulatory Authority concluded its recent hotel rankings for Mt. Kenya region, The Kenyan coast, Western Kenya and the greater Rift Valley region as summarized in the table below. The Mt. Kenya region stood out with 5 developments in the area getting a 4-star rating and above. This comes amidst poor performance in the hotel sector especially in the coastal region resulting from reduced international tourists? arrivals. In 2015 the percentage of domestic tourists was 59.1%, as opposed to 40.9% who were international tourists. It is expected that this rating will open the Mt. Kenya region to a wider target market of both the local and international tourists as it continues to offer packages for the domestic market such as weekend getaways and family packages.

Category of Establishment	3-Star	4-Star	5-Star
Vacation Hotels	8	8	2
Town hotels	11	3	-
Lodges	13	9	2
Tented camps	6	10	2
Villas, Cottages & Apartments	3	1	1
Restaurant	1	-	-
TOTAL	42	31	7

In our opinion, we expect that the tourism sector as a whole will continue to improve and subsequently, we shall have increased investments in the sector. We also anticipate entrance of international brands into the Kenyan market as it continues to thrive. We are currently working on the hospitality industry report.

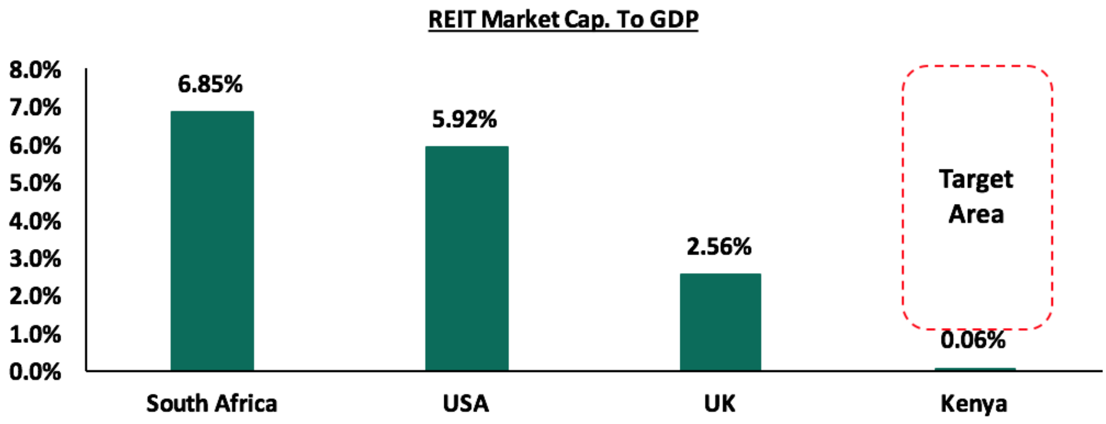
Real Estate Listings in Kenya

Listed real estate investment stocks in Kenya have so far delivered a disastrous track record, subscriptions have been low and price performance post issuance has been significantly negative. Yet, real estate remains a very attractive sector driven by demand outstripping supply in the low to mid income segment.

1. The Stanlib Fahari I-REIT achieved only 29% subscription, and is now trading at Kshs 13.75, 31.25% below its issuance price of Kshs 20. Additionally, the REIT has recently applied for regulatory extension to meet reporting obligations
2. Home Afrika went public in 2013 at Kshs 12.0 per share and is now trading at Kshs 1.25, which is 89.6% below its issuance price, and,
3. The Fusion D-REIT offering has been extended twice indicating failure to raise required amounts. There is little clarity on its closure which was scheduled for 4th August.

A vibrant real estate capital market is essential in two key respects:

i. First, an enormous amount of funding is required for the reduction of the housing deficit. The traditional sources of real estate funding, such as bank debt and private equity, are not sufficient to meet the financing demands required by real estate. A vibrant real estate capital market is essential to addressing the housing deficit.
ii. Secondly, is the need for real estate-backed investment returns; Listed real estate investments are crucial to diversifying and fortifying investment portfolios, especially long-term portfolios such as pension funds. Real estate is a good supplement to volatile stocks and lower yielding bonds. For individual investors, they get both the benefits of high and stable yields, but with prospects of long-term capital appreciation. The REIT Market Cap to GDP for Kenya compared to other countries shows significant opportunity for REITs, which is currently 0.06% of GDP in Kenya compared to 6.9% in South Africa, indicating room for growth for Real Estate listings in the capital market hence making real estate an investible security.



So, if there is money interested in real estate opportunities and there is real estate in need of money, why are we having difficulty gaining momentum in real estate listed investments and what can we do?

i. REITs are a new product and may require initially an industry initiative or a government sponsorship. Rather than each player trying to launch their own REIT, we should find a few strong real estate and investment players to collaborate on a club deal that has broad support with the goal of not just economic viability but also proofing the REIT concept to the market so that there is a success story. So far, all the real estate market listings (Home Africa, Fahari I-REIT and Fusion D-REITs) have not been successful, and this makes it extremely difficult for future offers. It is possible that the market for REITs could effectively have closed down for the foreseeable future,
ii. Get broad institutional support before launching another real estate listing. In markets such as Japan, the main buyers of REIT stocks are financial institutions. We need to educate and bring on board the main institutional investors to commit to supporting the REIT before launching,
iii. Bringing down the minimum amounts required for investments. The current amounts, for example, the minimum of Kshs. 5 million for the Fusion D-REIT is very high and locks out most investors,
iv. Broad investor education in simple terms that investors can understand backed by demonstrable examples,
v. Providing some level of principal plus minimum return guarantees to the buyers to get them comfortable that issuers are convinced about their REIT,
vi. Improved corporate governance around issuance. The first REIT offering is already asking for more time for regulatory compliance, and
vii. REITs to be more selective in the assets they put in the portfolio so that they are compelling and can deliver clearly superior returns.

Kenya has always been at the forefront of technology and financial innovation in the region. The launching of REITs in the local markets was a good step. The REIT agenda has certainly suffered some significant challenges. It is time for the industry players in financial services, real estate and regulators to review the initiative and give it new impetus. Failure to rejuvenate the REIT market would be very negative to the market.
