Unit Trust Funds Performance, Q2'2020, & Cytonn Weekly #46/2020

Real Estate

i. Industry Reports

During the week, the Kenya Bankers Association released the Housing Price Index, November 2020 Report, highlighting that house prices contracted by 0.1% in Q3'2020, a marginal improvement from the 0.2% contraction in Q2'2020. The declines in the house prices is attributed to the softening of the economy and the decline in consumption expenditure, which has affected both demand and supply in the residential market. Other key take-outs from the report include;

- Demand for apartments declined by 63.0%, while demand for bungalows and maisonettes expanded by 9.0%, and 72.0%, respectively, attributable to the relatively stronger demand at the top end of the market,
- Apartments accounted for approximately 43.0% sales, maisonettes and bungalows accounted for 21.0% and 33.0%, respectively, while townhouses accounted for 2.0% of the concluded sales in Q3'2020, and,
- Lower mid-end residential markets within the Nairobi Metropolitan Area such Athi River and Kasarani recorded the highest activities accounting for 52.6% of the sales during the quarter, with upper-mid-end areas such as Thindigua and South B at 31.6%, and high-end markets such as Kileleshwa and Kitisuru at 15.8% of the sales, reinforcing buyers' search for affordability.

Hass Consult also released the Q3'2020 House Price Index, and the key take-outs were;

- House prices recorded sluggish growth increasing by 0.3% over the quarter and 2.3% on an annual basis, attributable to reduced transactions as investors adopt a wait and see approach in the midst of uncertainty and reduced disposable income,
- Muthaiga detached units recorded the highest quarterly price appreciation of 1.4% while apartment's prices in Thika posted the highest increase at 1.8% q/q. On the other hand, Riverside apartments posted the highest quarterly and annual drop in price appreciation at 2.0% and 8.4% respectively, and,
- Overall, rental prices increased by 2.5% q/q and 4.9% y/y, with Ruiru recording the highest rental appreciation of 3.7% over the quarter. Apartments recorded an annual increase of 5.8% in the rental rates compared to detached and semi-detached units which recorded an annual increase of 5.1% and 3.5%, respectively. The relatively higher rental rates are attributed to the growing demand for rental housing amid reduced disposable income given the tough economic environment.

The above findings are in tandem with Cytonn's Q3'2020 Markets Review Report, which highlighted that the market recorded subdued performance during the quarter due to the tough economic environment evidenced by the (0.1%) decline in prices during the quarter. In terms of annual uptake, detached units recorded an average of 16.9% compared to apartments at 18.9%, indicating the continued demand for apartments supported by affordability amid reduced disposable income. We expect total returns to investors to remain suppressed in the last quarter of 2020 as developers continue to offer discounts to homebuyers. The investment opportunity for apartments lies in the lower mid-end market in areas such as Thindigua and South C, which continued to post above-market returns and annual uptake. For detached units, opportunity lies in upper mid-end segment in submarkets such as Ridgeways and Runda Mumwe due to the attractive rental yields.

Hass Consult also released Q3'2020 Land Price Index, and the key take-outs were;

- Land prices within Nairobi suburbs softened recording a 0.9% decline over the quarter, and 2.2% on an annual basis while satellite towns recorded a marginal drop of 0.1% q/q, attributed to suppressed demand, and an overall increase of 0.5% y/y,
- Spring Valley registered the highest quarterly increase in land prices at 3.6%, and a 4.2% price appreciation y/y while Riverside posted the biggest quarterly drop of 3.8%, with an annual price correction of 8.1% within the Nairobi suburbs, and,
- Ongata Rongai recorded the highest appreciation among satellite towns at 4.7% q/q and 10.8% y/y, supported by the affordability of land and improving infrastructure. On the other hand, Kiambu recorded the highest quarterly and annual price correction of 5.2% and 8.0%, respectively, attributed to relatively high land prices compared to other satellite towns with the average price per acre at Kshs 39.7 mn.

The land price index is not in line with the Cytonn Q3'2020 Markets Review according to which the land within the Nairobi Metropolitan Area recorded an overall annualized capital appreciation of 2.4%, indicating that investors still consider land a good investment asset in the long term. According to the report, land in satellite towns recorded an annualized appreciation of 4.7% while land within Nairobi suburbs recorded an average of 0.9%. The investment opportunity lies in sub markets such as Kitisuru, Ridgeways and Kasarani, which recorded relatively high annualized capital appreciation of 4.6%, 4.2% and 4.8% respectively. For satellite towns, Athi River recorded the highest annualized capital appreciation of 9.6% for unserviced land whereas Thika recorded the highest appreciation for site and serviced land at 7.3%.

ii. Residential Sector

During the week, Centum Real Estate launched a Kshs 2.0 bn housing project, Loft Residences in Gigiri area. The project, which is set for completion in 2022, is expected to have 56 units on 7 blocks. The 280 SQM four bedroom duplex units are valued at Kshs 40.0 mn for the upper floor units and Kshs 42.5 mn for the lower floor units. The unit prices translate to an average of Kshs 147,321 per SQM, 11.1% higher than the upper mid-end residential market average value of Kshs 132,573 per SQM according to the Cytonn Q3'2020 Market Review. The launch of Loft Residences follows the successful completion and handing over of the developer's two projects, Awali Estate at Vipingo Ridge in Kilifi County and Pearl Marina apartments in Entebbe in October 2020, and the recent launch of 365 Pavilion Place Apartments in Ruaraka and 265 Elmer One in Kasarani. In our view, the launch of the project is a sign of investor confidence in Gigiri area which is ideal for diplomats as the target clients working for the various international agencies such as the United Nations (UN). Gigiri as investment submarket is supported by; i) the area being categorized as a blue diplomatic zone, ii) close proximity to amenities such as Rosslyn Riviera Mall and Two Rivers Mall, iii) ease of accessibility as the area is served by the Limuru Road, and, iv) close proximity to diplomatic offices such as the United Nations headquarters.

The table below shows upper mid-end residential apartments performance in Q3'2020;

(All values in Kshs unless stated otherwise)

Upper Mid-End Residential Apartments Performance, Q3’ 2020

Loresho

Westlands

Parklands

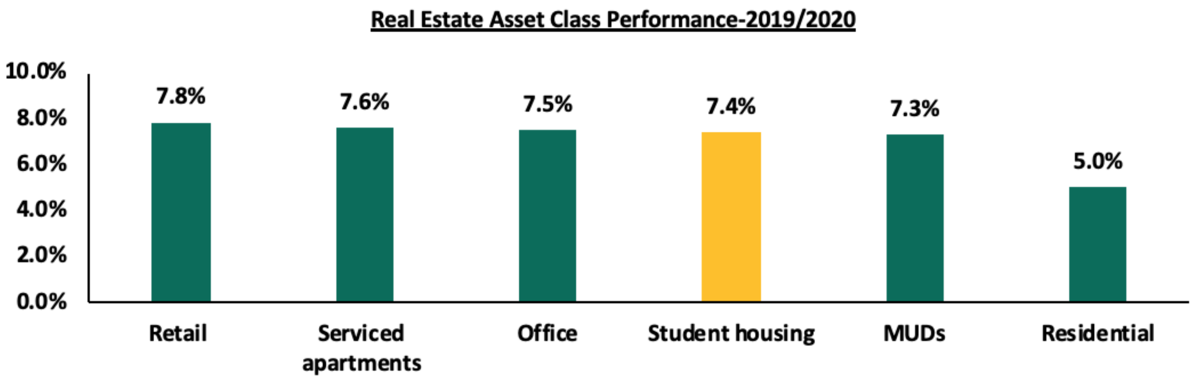
Kileleshwa

Upper Hill

Kilimani	[illegible]
Average	[illegible]

Source: Cytonn Research

Acorn Group, a Kenya-based real estate developer, announced that it is set to build two hostels next to the University of Nairobi Chiromo Campus, along Science Crescent Road, off Riverside Road to host approximately 3,000 students. One of the projects will be under the Qejani brand and is expected to accommodate approximately 2,112 students. The development will consist of 704 units on 18-floors. The units will include; double and quadruple where students will be sharing study and common rooms. The second project will be under the Qwetu brand and it is expected to accommodate approximately 837 students. This project will consist of 574 units on 16 floors and the room typologies will include; single, twin and cluster units. The developer has continued to focus on student housing having developed other hostels under the Qwetu brand in Ruaraka, Parklands and Jogoo Road. The focus on the concept is supported by; i) student housing deficit which is driven by continued increase in student numbers, ii) expanding middle class leading to growth in disposable incomes thus driving student mobility as more people seek quality higher education, creating more markets for student housing, iii) hedge against economic headwinds as student enrolment increases every year despite the economic climates, and, iv) attractive returns- according to Cytonn's topical Student Housing Market in Kenya, student housing posted relatively high rental yields averaging 7.4% and surpassing Mixed-use developments (MUDs) and residential sectors with 7.3% and 5.0%, respectively, as shown below:



Source: Cytonn Research

We expect the residential sector to record increased activities supported by the continued launch of projects and focus on student housing accommodation as the real estate sector continues to witness gradual recovery from the effects of COVID-19 pandemic.

iii. Retail Sector

During the week, Quickmart supermarket opened its latest outlet in Nanyuki Mall, Nanyuki town, as the anchor tenant taking up space left behind by the struggling retailer, Tuskys. This brings the total number of Quickmart's outlets to 35, with 6 outlets opened in 2020. The move by the retailer to invest in the Nanyuki retail market is supported by; i) positive demographics with Nanyuki having a population of 72,813 as of 2019, 47.9% higher than 49,233 recorded in 2009, according to the Kenya

National Bureau of Statistics (KNBS) Population and housing census report, ii) the attractiveness of the region as a tourist hub as Nanyuki hosts key tourist attractions such as the Ol Pejeta Conservancy and Mount Kenya National Park, and, iii) a growing middle class with increased consumer purchasing power.

In terms of performance, Nanyuki which falls under the Mt. Kenya Region, was the best performing region in the retail market according to the Cytonn's Kenya Real Estate Retail Sector Report 2019 with average yields of 8.6%, 1.6% points higher than the market average of 7.0%. The performance is attributed to high occupancy rates at 80.0%, 2.7% points higher than the market average of 77.3% and high rental rates of Kshs 129.8 per SQFT, which is 10.0% higher than the market average rates of Kshs 118.0 SQFT. The region accounts for 7.7% retail market share and its performance was mainly driven by low supply of malls in the region. However, with the existing pandemic, the performance is expected to slightly go down as most retail chains scale down their operations to cushion themselves against the pandemic.

The table below shows a summary of 2019 retail performance in key urban cities in Kenya;

(All values in Kshs unless stated otherwise)

Summary of 2019 Retail Performance in Key Urban Cities in Kenya

Region	Rent 2019	Occupancy Rate 2019	Rental Yield 2019
Mt. Kenya	129.8	80.0%	8.6%
Nairobi	168.6	75.1%	8.0%
Eldoret	131.0	82.3%	7.9%
Mombasa	122.8	73.3%	7.3%
Kisumu	96.9	75.8%	5.6%
Nakuru	59.2	77.5%	4.5%
Average	118.0	77.3%	7.0%

Source: Cytonn Research

The table below shows the summary of the number of stores of the key local and international retail supermarket chains in Kenya;

Main Local and International Retail Supermarket Chains

Name of Retailer	Initial number of branches	Number of branches opened in 2020	Closed branches	Current number of Branches	Branches expected to be opened	Projected total number of branches
Naivas Supermarket	65	5	0	66	4	70
Tuskys	64	2	14	50	0	50
QuickMart	29	6	0	35	0	35
Chandarana Foodplus	19	1	0	20	0	20
Carrefour	7	1	0	8	3	11
Uchumi	37	0	33	4	0	4

Going forward, we expect the retail sector's performance to be cushioned by; i) the continued expansion of both local and international retailers taking up space left behind by struggling brands, ii) improving infrastructure such as the expansion of Ngong Road, iii) positive demographics with Kenya's current urbanization and population growth rates at 4.0% and 2.2% against a global average of 1.9% and 1.1%, respectively, according to the World Bank, iv) changing tastes and preferences of consumers, and, v) shifting consumer trends which have fuelled the entry of international retailers thus increasing demand for formal retail space. Nevertheless some of the challenges expected to face the sector include; i) exit by some retailers to cushion themselves against the impact of the COVID-19 pandemic, ii) growing focus on e-commerce thus reduced demand for physical space, iii) the existing oversupply of 2.8 mn SQFT of retail space in certain locations which is likely to result in pressure on landlords to provide concessions and other incentives to attract new clientele or retain existing tenants, and, iv) reduced consumer spending power attributed to the tough economic environment.

iv. Hospitality

During the week, Kenya was voted as Africa's leading tourist destination in the World Travel Awards, supported by the epic savannah landscapes, wildlife, beaches and lakes among other tourist attraction centers. Additionally, Kenyatta International Conference Centre (KICC) was voted as Africa's leading meeting and conference center. Fairmont Mount Kenya grabbed the title of Africa's leading hotel, while the Aberdare Country Club was voted Africa's leading Green Hotel. Additionally, Kenya Airways was ranked as Africa's leading Airline-business classes and Africa's leading Airline-economy class. The wide array of awards indicates continued confidence in Kenya's hospitality industry despite the impact of COVID-19 pandemic. Currently, the sector is undergoing gradual recovery supported by; government strategies such as the Ministry of Tourism Post-Corona recovery funds aimed at offering financial aid to hotel and other establishments in the hospitality industry through the Tourism Finance Corporation (TFC), repackaging of the tourism sector products to appeal to domestic tourists, and, relaxation of travel advisories aiming at increasing the number of international tourist arrivals into the country. We expect the positive accolades to boost investor confidence in the sector coupled by; improved security, political stability, and improving infrastructure.

The real estate sector is expected to continue recording activities driven by the launch of residential projects, focus on student housing, expansion of local retail chains taking up prime spaces left behind by struggling retailers, and recovery of the hospitality sector as it leverages on positive accolades.