Unit Trust Funds Performance, Q1'2021, & Cytonn Weekly #41/2021

Real Estate

I. **Hospitality Sector**

During the week, Jameson Valley Holdings and Actis Limited, private equity firms, announced a Kshs 1.0 bn joint venture bid to buy three hotels, namely; Nairobi's Fairview Hotel and Town Lodge Hotel both located along Bishop Road Upperhill, and, City Lodge Hotel located in Two Rivers, Runda. The three hotels owned by South Africa's City Lodge Hotel Group were put up for sale in July 2021, and this deal is expected to be achieved through Ukarimu Real Estate Funds by means of a Special Purpose Vehicle (SPV) listed in Mauritius as Msafiri Limited. The hotels have a combined 382 rooms with City Lodge, Fairview and Town Lodge having 171,127 and 84 rooms, respectively. The City Lodge Group also plans to sell its Tanzanian City Lodge Hotel in Dar-es-Salaam, marking the exit of the Group portfolio in East African market after seven years of operation, citing; i) huge losses to the tune of Kshs 2.0 bn as at the end of 2020, ii) low occupancy and booking levels below expectations attributable to Covid-19 regulations with average market occupancies for serviced apartments declining by 31.3% points to 48.0% in 2020 from the 79.4% in 2019. City Lodge Group average occupancies for the year 2021 came in at 19.0% compared to 38.0% in 2020 and 55.0% in 2019 with the Two Rivers City Lodge Hotel occupancy estimated at 7%-10% in the same period, iii) the need to reduce debt levels in the Group, and, iv) necessity to boost liquidity in the remaining profitable hotels in South Africa, Botswana, Namibia and Mozambique.

The hospitality sector was one of the worst hit sectors by the pandemic attributable to international travel bans, travel advisories, lockdowns and social distancing measures meant to curb the spread of Covid-19 pandemic. This led to the decline in hotel bookings and occupancies and the closure of many hospitality-affiliated businesses while most looked to exit their investments amidst the tough operational environment. This is evidenced by our Nairobi Metropolitan Area Serviced Apartments Report 2020 where average market occupancies for serviced apartments declined by 31.3% points to 48.0% in 2020 from the 79.4% in 2019.

The table below shows the comparative analysis of NMA Serviced Apartments 2019/2020;

Comparative Analysis - 2019/2020 Market Performance

Westlands & Parklands

Kilimani

Limuru Road

Kileleshwa & Lavington

Upper Hill

Nairobi CBD

Thika Road

Average

Source: Cytonn Research 2020

Despite this, the sector performance has been improving with the lift of most Covid-19 bans and restrictions, and the gradual return to normalcy as vaccination picks pace. The number of operating hotels have improved over the last few months coming in at 96.0%, in September 2021 from 81.0% in April 2021. The graph below shows the overall percentage of the number of operating hotels in Kenya June 2020 – September 2021;

Source: Central Bank of Kenya

We expect the hospitality sector to continue on an upward trajectory in terms of overall hotels in operations, hotel bookings, and hotel occupancy following the ambitious international marketing, the return of flights and the mass vaccination currently underway in the country.

II. **Infrastructure**

During the week, the National Treasury announced that the government of Kenya will borrow Kshs 2.0 bn from an undisclosed financier to facilitate the dualling of the Eastern By-Pass which stretches from Mombasa Road to the Thika Superhighway. The road aims at reducing traffic congestion in the Nairobi’s Central Business District (CBD) by allowing motorists, especially those from the Jomo Kenyatta International Airport (JKIA), to use alternative routes through City Cabanas, Pipeline and Njiru areas to get to their destinations without transiting through the city. Additionally, the government borrowed Kshs 6.4 bn from Korean Export and Import Bank to finance the Bus Rapid Transit (BRT) project. The Korean loan is set to be serviced for a period of 40 years up to 2061 at an interest rate of 0.1% p.a and a service charge of 0.1% p.a on undisbursed loan amounts. There are plans to launch six BRT corridors in the Nairobi Metropolitan Area (NMA) by 2022 with the major ones located along the busy Thika and Mombasa Roads holding up to 950 high capacity buses with an aim to reduce travel time and cost by 70.0%. This is in line with the improving infrastructure agenda to; i) reduce traffic congestion in the Nairobi’s CBD to save on time and costs, ii) open up areas for investments, iii) enhance accessibility and efficiency in movements for economic growth, and, iv) make Kenya an East Africa’s investment hub through provision, maintenance and management of road infrastructure in support of Vision 2030 aspirations in order to provide safe, efficient, accessible, and, sustainable transportation services.

The loans therefore come as a way to partly service the FY’2021/22 infrastructure budget at Kshs 182.5 bn a 0.6% increase from the Kshs 181.4 bn allocated in FY’2020/21. Other major infrastructure projects listed in the current budget include the construction of the next phase of the Standard Gauge Railway (SGR) from Nairobi- Naivasha at Kshs 7.2 bn, the Nairobi Express Way at Kshs 63.8 bn and Lamu Port-South Sudan, Ethiopia Transport (LAPSSET) Corridor at Kshs 7.5 bn.

The graph below shows the budget allocation to the infrastructure sector over the last nine financial years;

Source: National Treasury

We expect the infrastructure sector to continue recording increased activities attributable to the government’s continued aggressiveness to ensure that all projects in the pipeline are completed through partnerships to fund the developmental fiscal deficits**.**

III. **Statutory Reviews**

During the week, the government of Kenya announced plans to review property rates after every five years as contained in the proposed National Rating Bill, 2021, to ensure the government does not lose out on the current capital appreciations of public land. The state seeks to have counties review their valuation rolls every five years with an allowable extension of up to 2 years, with the valuation being done under the current market prices. This follows the surging prices especially in the urban areas which deny counties revenues as they continue to use outdated laws and ratings as per the Rating Act of 1963 whose rates do not match the appreciations in the current market. In the proposed legislation, land valuers will be required to prepare a draft valuation roll listing all properties within the county and their details including; i) map area and description, ii) the name and address of the rateable owner, iii) use of the property, iv) assessment of improvement rate, and, v) nature of subdivision. This will include all public land except land used exclusively for public purposes, and those rateable property leased for foreign embassies and missions. Supplementary valuation rolls can also be prepared within the tenor to capture omissions from the main roll, any new rateable property, subdivisions and consolidations and rate amendments. The bill also seeks to setup a National Rating Tribunal to hear and determine matters relating to land valuations in the counties. The final valuation report is expected to include the valuation methodology, date of valuation, signature of the valuer and any other relevant information before adoption by the county governments.

The government continues to foster progressive legislations to align with the current market requirements in order to boost revenues in land transactions. We therefore expect an increase in revenues in the counties which will fund the County Development Agendas alongside the equitable share.

The real estate sector is expected to record improving performance from the recovery of the hospitality sector, the government's commitment to see pipeline projects to completion and the progressive regulations to increase the county revenue base to fund development.
