Kenya Listed Banks H1’2022 Report, & Cytonn Weekly #36/2022

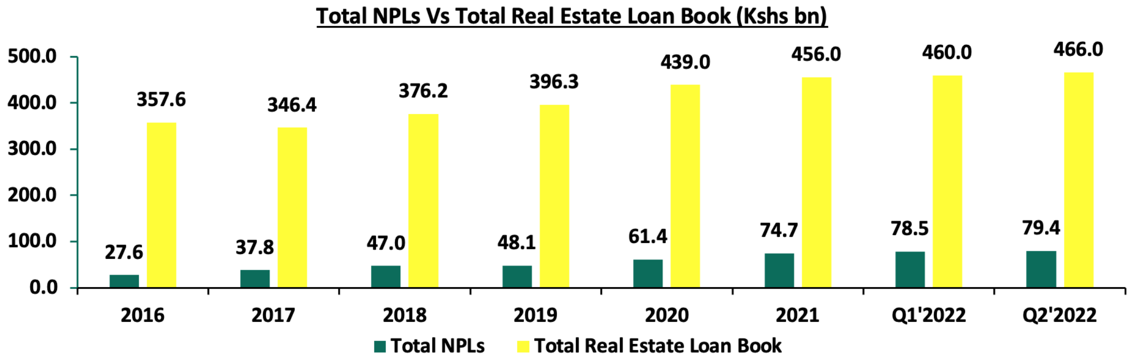
Real Estate

I. **Industrial Report**

During the week, the Central Bank of Kenya (CBK) released the Quarterly Economic Review Q2’2022, a report highlighting the status and performance of Kenya’s economy. The following were the key take outs from the report, with regards to the Real Estate and related sectors;

i. The gross loans advanced to the Real Estate sector increased by 1.3% to Kshs 466.0 bn in Q2’2022, from Kshs 460.0 bn in Q1’2022 representing a 4.0% YoY increase from Kshs 448.0 bn realized in Q2’2021. The performance was driven by the increased construction and development activities in the property sector which necessitated more capital,
ii. Gross loans advanced to the Tourism sector also increased by 1.8% to Kshs 113.0 bn in Q2’2022, from Kshs 111.0 bn in Q1’2022, in a bid to boost the sector’s performance through its marketing, sports, and leisure activities,
iii. Gross loans advanced to the Building and Construction sector increased by 2.9% to Kshs 142.0 bn in Q2’2022, from Kshs 138.0 bn in Q1’2022, mainly driven by continuous construction activities in select Real Estate sectors such as residential and infrastructure sectors, coupled with the increased construction costs, and,
iv. The Gross Non-Performing Loans in the Real Estate sector increased by 1.1% to Kshs 79.4 bn in Q2’2022, translating to a 17.0% non-performing loans ratio, from Kshs 78.5 bn recorded in Q1’2022 equivalent to 17.1% non-performing loans ratio. On a YoY basis, the performance represented a 16.4% increase from Kshs 68.2 bn realized in Q2’2021, attributed to increased Real Estate loan default rates amidst a rising cost of living.

The graph below shows the total Real Estate non-performing loans against the total loans advanced to the sector since 2016;



Source: Central Bank of Kenya (CBK)

We expect Kenya’s property sector performance to be driven by i) expected increase in visitor arrivals into the country which will boost the performance of the hospitality sector, and ii) the increased residential and infrastructural developments opening up various areas for investments. However, we note that access to credit in the sector remains subdued as evidenced by the overly slow growth in the loans advanced hence posing a funding challenge to the Real Estate sector. As the economy continues to recover, we expect the financing institutions to resume lending to the sector given that the number of defaults is also expected to decline.

II. **Commercial Office Sector**

During the week, Nairobi Garage, an office supply firm in Kenya, opened a two-floor outlet at Nairobi's 20th Century Plaza located along Mama Ngina Street. The new office space constitutes of 12,000 SQFT and adds to its five existing outlets located in Kilimani, Karen and Westlands. The move to open the new branch in Nairobi's CBD is mainly driven by;

i. Consumer preference to Nairobi's Central Business District (CBD),
ii. Remarkable infrastructure development in the city center such as paved walkways, expansion and rehabilitation of roads, Nairobi Expressway exit links, and, the commissioning of the redevelopment of the Central Railway Station, among others, which in turn boost accessibility and investments,
iii. Increasing popularity of shared working spaces which has continued to drive demand owing to their flexibility and already-available amenities as opposed to unfurnished offices spaces. Consequently, the serviced offices charge premium rates attracting higher yields, and,
iv. The need to leverage on the affordability of the office space at the CBD as opposed to other areas of the Nairobi Metropolitan Area as summarized below;

Nairobi Metropolitan Area Serviced Office Performance

Location	Rate (Kshs Per SQFT 2021)		Rate (Kshs Per SQFT 2022)		Serviced Offices Rental growth (%)	Un-serviced Offices Rental growth (%)
	Serviced Offices	Un-serviced Offices	Serviced Offices	Un-serviced Offices		
Westlands	204	93	212	104	3.9%	10.6%
Karen	186	104	192	106	3.1%	1.9%
Parklands	174	106	169	91	(3.3%)	(16.5%)
Gigiri	181	116	-	119	-	2.5%
Upperhill	-	92	235	94	-	2.1%
Kilimani	190	82	194	91	2.2%	9.9%
Nairobi CBD	160	93	164	82	2.6%	(13.4%)
Msa Rd	105	73	-	73	-	0.0%
Thika Rd	116	80	112	79	(3.6%)	(1.3%)
Nodes Average	**161**	**93**	**183**	**93**	**0.8%**	**0.0%**

Source: Cytonn Research

We note that shared office spaces have continued to give better returns as compared to unfurnished office spaces as evidenced by the higher average rate per SQFT which came in at Kshs 183 for serviced offices in comparison to Kshs 93 per SQFT for un-serviced offices. Overall, the commercial office sector continues to record gradual expansion driven by the aggressive development activities which we expect to help boost the performance of the sector. However, the excess supply of office space in the Nairobi Metropolitan Area currently at 6.7 mn SQFT, continues to remain a major challenge hindering the optimum performance of the sector.

3. **Retail Sector**

a. **Naivas Supermarket Opens its 85th Outlet at Eldoret's Elgon View Mall**

During the week, Naivas Supermarket opened a new outlet at Elgon View Mall in Eldoret, bringing its total branches countrywide to 85. The new outlet covering 39,999 SQFT, is the 4th outlet opened by the retailer in Eldoret town, with the other three being located at Zion Mall, Referral, and Sokoni. Naivas has been on an aggressive expansion spree taking up new and spaces vacated by troubled retailers, in a bid to maintain market dominance as a result of swift market competition from its peers such QuickMart which has opened three new outlets so far this year. The new outlet is the 6th to be opened so far in 2022, with the retailer planning to open another one in Meru town by the end of the year. The decision to open the new outlet in Eldoret was mainly driven by;

i. Availability of prime retail space for uptake,
ii. Strategic location of the retail center along Stendi Kisa-Yala Road which promotes quick access to the retail store, and,
iii. Uasin Gishu's relatively high population growth rate currently at 2.7%, compared to Kenya's 2.3%, which in turn boosts the footfall of the retail spaces in the area, as a result of a rapid demand for goods, services, and retail spaces. As per our Kenya Retail Report 2022 retail spaces in Eldoret recorded an average occupancy rate of 86.1%, 8.8% points higher than the market average of 77.3%, as indicated in the table below;

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

Main Local and International Retail Supermarket Chains

Name of retailer	Category	Branches as at FY' 2018	Branches as at FY' 2019	Branches as at FY' 2020	Branches as at FY' 2021	Branches opened in 2022	Closed branches	Current branches	Branches expected to be opened	Projected branches FY'2022
Naivas	Local	46	61	69	79	6	0	85	1	86
QuickMart	Local	10	29	37	48	3	0	51	0	51
Chandarana	Local	14	19	20	23	1	1	24	4	28
Carrefour	International	6	7	9	16	0	0	16	0	16
Cleanshelf	Local	9	10	11	12	0	0	12	0	12
Tuskys	Local	53	64	64	3	0	61	3	0	3
Game Stores	International	2	2	3	3	0	0	3	0	3
Uchumi	Local	37	37	37	2	0	35	2	0	2
Choppies	International	13	15	15	0	0	13	0	0	0
Shoprite	International	2	4	4	0	0	4	0	0	0
Nakumatt	Local	65	65	65	0	0	65	0	0	0
Total		**257**	**313**	**334**	**186**	**10**	**179**	**196**	**5**	**201**

Source: Cytonn Research

b. **Optica Limited Opens a New Outlet at Nextgen Mall**

During the week, local eye-wear Optica Limited opened a new outlet at Nextgen Mall, along Mombasa Road bringing its total outlets countrywide to 65. The retailer has opened three new outlets so far this year at Rubis Business Block in Kitengela, and in Argwing's Arcade in Kilimani, both in May 2022, and another in Ruiru's Kamakis, in January 2022. The opening of the new outlet at Nextgen Mall was driven by:

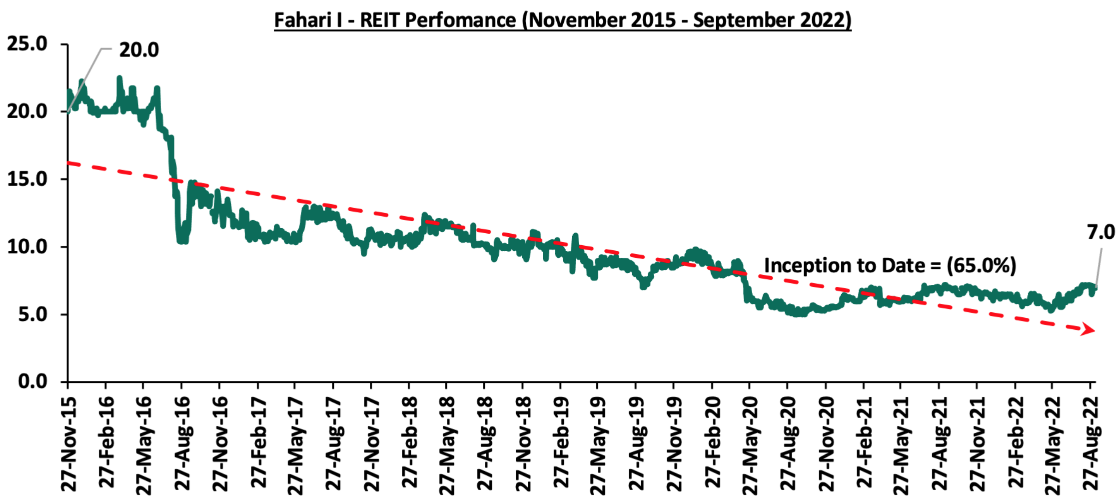
i. Suitable location of the outlet along the busy Mombasa Road which enhances accessibility to the store and its overall footfall,
ii. Availability of prime retail space for uptake,

iii. Its expansion strategy to further reach out its product and services to target clients,
iv. Increasing demand for prescription sunglasses which also offers protection from UV rays, and,
v. Affordability of retail spaces in the area evidenced by our Kenya Retail Report 2022 which highlighted that retail spaces located along Mombasa Road recorded average rental rates per SQFT of Kshs 150, 13.3% lower than the market average of Kshs 173 per SQFT.

The increasing investor confidence in the retail sector has continued to support rapid expansion by local and international retailers and consequently cushioned the performance of the sector. However, we expect the oversupply of mall spaces coupled with the existence of e-commerce to continue weighing down the optimum uptake of space and the overall performance.

IV. **Real Estate Investment Trusts (REITs)**

In the Nairobi Stock Exchange, ILAM Fahari I - REIT closed the week trading at an average price of Kshs 7.0 per share representing a 9.4% Year-to-Date (YTD) increase from Kshs 6.4 per share. On an Inception-to-Date (ITD) basis, the REIT's performance continues to be weighed down having recorded a 65.0% decline from Kshs 20.0. The graph below shows Fahari I-REIT's performance from November 2015 to September 2022:



In the Unquoted Securities Platform, Acorn D-REIT and I-REIT closed at Kshs 23.8 and Kshs 20.8 per unit, respectively, as at 2nd September 2022. The performance represented a 19.0% and 4.0% gain for the DREIT and I-REIT, respectively, from the Kshs 20.0 inception price. The volumes traded for the D-REIT and I-REIT came in at 5.5 mn and 14.5 mn shares, respectively, with a turnover of Kshs 117.0 mn and Kshs 300.3 mn, respectively since Inception-to-Date.

The performance of Kenya's Real Estate sector is expected to be on an upward trajectory driven by the slow but rising expansion in the office market, aggressive expansion in the retail sector, and, the improving construction activities in the residential and infrastructure sectors. However, the existing oversupply of office and mall space, financial constraints, and investor's inadequate appetite for the Kenyan REIT instrument is expected to hinder the optimum investments in the property market.