Cytonn Monthly – February 2023

Real Estate

I. **Industry Reports**

During the month, the following industry reports were released and the key take-outs were as follows:

Cytonn Report: Notable Industry Reports During the Month

#	Theme	Report	Key Take-outs
1	Hospitality Sector	Annual Tourism Sector Performance Report - 2022 by the Tourism Research Institute (TRI)	• The number of international arrivals registered a 70.5% increase to 1,483,752 persons in 2022 compared to 870,465 persons in 2021, • The highest number of visitor arrivals were from the United States of America (USA) and Uganda, which registered total number of tourists at 209,360 and 151,121, respectively, and, • Inbound tourism earnings increased by 82.9% to Kshs 268.1 bn in 2022 compared to Kshs 146.51 bn in 2021, achieving a 90.5% recovery rate compared to 2019 pre-COVID levels which raked in Kshs 296.2 bn. For more information, see Cytonn Weekly #08/2023.
2	General Real Estate	Status of The Built Environment Report January - December 2022 by the Architectural Association of Kenya (AAK)	• In 2022, the construction cost per SQFT increased by 5.0% averaging Kshs 5,210 from Kshs 4,960 recorded in 2021, attributable to price increase of key construction materials such as cement, steel, paint, aluminium and Polyvinyl Chloride (PVC), • The Affordable Housing Programme (AHP) is on course with an active pipeline of 376 projects looking to deliver 599,000 units across the country, and, • The National Construction Authority (NCA) approved 4,377 applications for project registration with a combined worth of Kshs 280.9 bn out of a received total of 8,154 applications. For more information, see Cytonn Weekly #07/2023.

We expect Kenya's Real Estate sector to continue recording upward performance in terms of activity, driven by the recovery of the hospitality sector supported by increased tourist arrivals and inbound earnings. Conversely, the prevailing high construction costs amid inflationary pressures from both local and global shocks are expected to weigh down the optimum performance of the sector.

II. **Residential Sector**

Notable highlights in the sector during the month include;

i. The County Government of Nairobi began the second phase of its plan of redeveloping old County estates through construction of 33,000 new low-cost units. For more information, see our Cytonn Weekly #08/2023,
ii. Centum Real Estate, the development affiliate of Centum Investment Company PLC, completed the construction of phase one of its 32 luxurious four-bedroom duplexes dubbed 'Loft Residences', which sits on 3.9 acres situated in Two Rivers. For more information, see our Cytonn Weekly #07/2023,
iii. Madison Insurance entered into a Joint-Venture (JV) agreement with Housing Finance Company (HFC), a subsidiary of HF Group, to develop a Master Planned Community project dubbed 'Villakazi Homes' in Athi River, Machakos County. For more information, see our Cytonn Weekly #07/2023, and,
iv. Absa Bank Kenya PLC announced that it had availed funding worth Kshs 6.7 bn to property developer Acorn Holdings Limited (AHL), for the construction of 10 Purpose-Built Student Accommodation (PBSA) projects worth Kshs 11.0 bn. For more information, see our Cytonn Weekly #06/2023.

We expect the ongoing housing development activities in the residential sector to boost Kenya's Real Estate sector in terms of increasing homeownership percentages, and curbing the existing housing deficit. In addition, we anticipate demand for housing to grow further, owing to the country's high urbanization and population growth rates. However, the lack of long-term, affordable development financing attributed to banks charging high interest rates, and the subdued capital markets continue to weigh down the optimum performance of the sector.

III. **Commercial Office Sector**

During the month, JPMorgan Chase & Co, an American-based international investment bank, through State House Nairobi, announced plans to open its regional office in Nairobi, Kenya, serving as a central hub for its operations in East African region, with existing footprints in Nigeria and South Africa. Additionally, Commonwealth Enterprise and Investment Council (CWEIC), Commonwealth's official business networking organization, opened its regional office in Nairobi, Kenya, that will serve as East Africa's business hub for the organization which will help grow trade and investments in the region. For more information, see our Cytonn Weekly #08/2023.

We expect the expansion drive by multi-national firms seeking to conduct operations in the region will further attract more organizations into the Kenyan commercial office market, thereby bolstering performance of the sector. However, the existing oversupply of office space currently at 6.7 mn SQFT in the Nairobi Metropolitan Area (NMA) will continue to weigh down the overall performance of the sector.

IV. **Retail Sector**

During the week, local retail chain Quickmart Supermarket opened a new outlet located in Thome, along the Northern Bypass road, bringing the retailer's number of operating outlets countrywide to 56. The retailer's decision to open a 24-hour store in Thome and surrounding areas is influenced by the desire to cater to the convenience preferences of shoppers within the residential locality. Moreover, the move is part of an aggressive expansion drive to promote the Quickmart brand as a household name among customers, thereby increasing its competitiveness against other retailers such as Naivas and Carrefour, and stamp its market dominance. This comes at a time where the formal retail penetration in Kenya is low, standing at 30.0% in 2018, coupled with gaps left by other retailers such as Nakumatt and Uchumi Supermarkets that exited the market.

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

Cytonn Report: 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 as at FY'2022	Branches opened in 2023	Closed branches	Current branches	Branches expected to be opened	Projected branches FY'2023
Naivas	Local	46	61	69	79	91	0	0	91	0	91
Quick Mart	Local	10	29	37	48	55	1	0	56	0	56
Chandarana	Local	14	19	20	23	26	0	0	26	0	26
Carrefour	International	6	7	9	16	19	0	0	19	0	19
Cleanshelf	Local	9	10	11	12	12	1	0	13	0	13
Tuskys	Local	53	64	64	6	4	0	60	4	0	4
Game Stores	International	2	2	3	3	0	0	3	0	0	0
Uchumi	Local	37	37	37	2	2	0	35	2	0	2
Choppies	International	13	15	15	0	0	0	15	0	0	0
Shoprite	International	2	4	4	0	0	0	4	0	0	0
Nakumatt	Local	65	65	65	0	0	0	65	0	0	0
Total		**257**	**313**	**334**	**189**	**209**	**2**	**182**	**211**	**0**	**211**

Source: Cytonn Research

Other notable highlights in the sector during the month include;

i. Local retail chain Cleanshelf Supermarket opened a new outlet located in Greenpark Estate along Mombasa road, Athi River bringing the retailer's number of operating outlets countrywide to 13. For more information, see our Cytonn Weekly #07/2023, and,
ii. International fast-food chain ChicKing, in partnership with M/s Crispy Limited, a local franchise, opened a restaurant outlet located in Mombasa along Nyerere Avenue, the first outlet in Kenya and the East African market. For more information, see our Cytonn Weekly #06/2023.

We expect performance of the Kenyan retail sector to be supported by the ongoing expansion drive by both local and international retailers, as they compete for dominance in the market. However, the fast-paced growth of e-commerce, and the oversupply of retail space standing at approximately 3.0 mn SQFT in the NMA retail sector and 1.7 mn SQFT in the non-NMA regions, will continue to hinder optimum performance of the retail sector.

V. Infrastructure Sector

During the week, the Northern Corridor Transit and Transport Coordination Authority (NCTTCA) announced a partnership with Superior Homes Kenya, a housing developer where Cytonn Investments is the second largest shareholder, to construct roadside stations along major highways. Superior Homes Kenya will develop the service and rest point areas along various transit routes within the country, which will feature self-contained facilities for long-distance truckers such as; i) safe parking spaces, ii) driver accommodation features, iii) convenience stores for food and beverage options, iv) health facilities, v) truck maintenance and refueling, and, vi) cargo handling. This is meant to enhance road safety by addressing driver fatigue experienced by long-distance transit drivers across the Northern Corridor. The move forms part of the NCTTCA strategy to fulfil its mandate of facilitating interstate and transit trade between landlocked countries of the Great Lakes region and the Kenyan maritime sea port of Mombasa. The Northern Corridor road network covers a total of 12,707 Km, distributed as follows; 567.0 Km in Burundi, 4,162.0 Km in Democratic Republic of Congo, 1,328.6 Km in Kenya, 1,039.4 Km in Rwanda, 3,543 Km in South Sudan, and 2,072 Km in Uganda.

The partnership to develop the roadside stations is meant to bridge the market gap of inadequate and informal truck stop facilities along major transit points such as Sultan Hamud, and areas between Mtito Andei and Salama, which is expected to be completed in March 2024. Upon completion, the roadside stations are expected to;

i. Spur economic growth of the areas supported by setting up of businesses such as shops and services to cater for truck drivers and other travelers, thereby boosting property prices within the key locations,
ii. Reduce fatigue related accidents by allowing drivers to rest and refresh themselves before continuing their journey, hence improving the safety and reliability of highways in the infrastructure sector, and,
iii. Improve transport logistics with the stations acting as logistics hubs, thereby improving efficiency of transport services and reduce transportation costs for commodities in the economy.

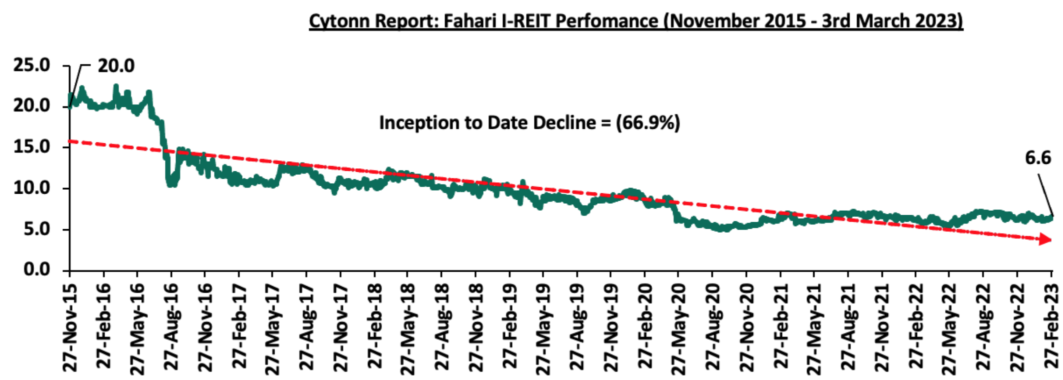
Other notable highlights in the sector during the month include;

i. Kenya Railways Corporation (KRC) commenced construction of the first phase of the Kshs 30.0 bn Railway City project which was launched in by President William Ruto in December 2022. For more information, see our Cytonn Weekly #07/2023, and,
ii. The Kenya National Highways Authority (KeNHA) announced plans to begin rehabilitation and improvement of sections of Mombasa road which were damaged during the construction of the Nairobi Expressway, within the next 2 months. Additionally, two major roads; Murang'a-Kangema and Murang'a-Kiriaini-Othaya located in Murang'a County were upgraded to national status for the purpose of rehabilitation and other maintenance works. For more information, see our Cytonn Weekly #06/2023.

We expect the ongoing efforts to develop road networks and other support facilities in the infrastructure sector to promote economic activities, subsequently driving performance of the general Real Estate sector in Kenya. On the other hand, infrastructural development activities are expected to be set back by the 21.4% reduction in budgetary allocation to the State Department of Infrastructure to Kshs 174.0 bn, from the Kshs 221.3 bn previously allocated for the year ending June 2023. Consequently, we expect the sourcing of funds for more infrastructure projects in the country to further shift to alternative financing strategies such as Public-Private Partnerships (PPPs).

VI. Real Estate Investment Trusts (REITs)

In the Nairobi Securities Exchange, ILAM Fahari I-REIT closed the week trading at an average price of Kshs 6.6 per share. The performance represented a 2.5% gain from Kshs 6.5 per share recorded the previous week, taking it to a 2.4% Year-to-Date (YTD) decline from Kshs 6.8 per share recorded on 3rd January 2023. In addition, the performance represented a 66.9% Inception-to-Date (ITD) loss from the Kshs 20.0 price. The dividend yield currently stands at 7.6%. The graph below shows Fahari I-REIT's performance from November 2015 to 3rd March 2023;



In the Unquoted Securities Platform, Acorn D-REIT and I-REIT traded at Kshs 23.9 and Kshs 20.9 per unit, respectively, as at 3rd March 2023. The performance represented a 19.4% and 4.4% gain for the D-REIT and I-REIT, respectively, from the Kshs 20.0 inception price. The volumes traded for the D-REIT and I-REIT came in at 12.3 mn and 29.4 mn shares, respectively, with a turnover of Kshs 257.5 mn and Kshs 600.4 mn, respectively, since inception in February 2021.

Notably, during the month, the Capital Markets Authority (CMA) in collaboration with the Sanduku Investment Initiative, the Association of Pension Trustees and Administrators of Kenya (APTAK) and the Nairobi Securities Exchange (NSE) announced ongoing plans to create a Kenya National REIT (KNR) as an accreditation body for REITs and their stakeholders within the Kenyan REITs market. For more information, see our Cytonn Weekly #06/2023.

REITs provide numerous advantages, including access to more capital pools, consistent and prolonged profits, tax exemptions, diversified portfolios, transparency, liquidity and flexibility as an asset class. Despite these benefits, the performance of the Kenyan REITs market remains limited by several factors such as; i) insufficient investor understanding of the investment instrument, ii) time-consuming approval procedures for REIT creation, iii) high minimum capital requirements of Kshs 100.0 mn for trustees, and, iv) high minimum investment amounts set at Kshs 5.0 mn discouraging investments.

We expect the performance of Kenya's Real Estate sector to remain on an upward trajectory, supported by factors such as; i) the aggressive expansion drive in the retail sector, and, ii) diversification in the infrastructure sector which is geared to increase economic activities. However, the existing oversupply of physical space in selected sectors, high construction costs to developers, and low investor appetite for REITs are expected to continue subduing the performance of the sector.

Liason House, StateHouse Avenue
The Chancery, Valley Road
www.cytonn.com