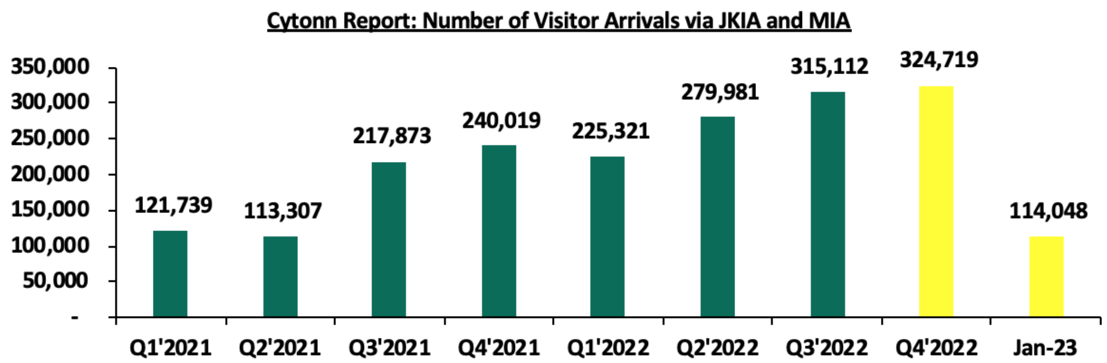
Kenya’s Public Debt Review 2023, & Cytonn Weekly #15/2023

Real Estate

I. **Industry Reports**

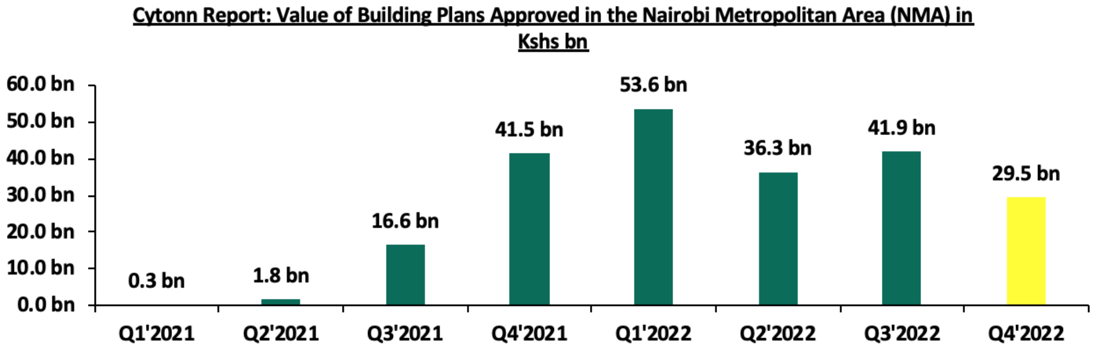
The Kenya National Bureau of Statistics (KNBS) released the Leading Economic Indicators (LEI) November 2022, December 2022 and January 2023 reports which highlighted the performance of major economic indicators such as international arrivals, building plan approvals, among others. The key highlights related to the Real Estate sector include;

i. Overall international arrivals through Jomo Kenyatta International Airport (JKIA) and Moi International Airport (MIA) increased by 35.3% to 324,719 in Q4’2022, from the 240,019 recorded in Q4’2021. On a q/q basis, the performance was a 3.0% increase, from 315,112 recorded in Q3’2022. Additionally, for the month of January 2023, the total number of arrivals increased by 63.1% to 114,048 from 69,932 recorded in January 2022. The improved performance can be attributed to; i) continued intensive marketing of Kenya’s tourism market by the Ministry of Tourism in collaboration with the Kenya Tourism Board, through platforms such as the Magical Kenya platform, ii) purposed efforts to promote local tourism highlighted under the Ministry of Tourism Strategy 2021-2025, and, iii) an upsurge in corporate and business meetings, events, and conferences from both the public and private sectors owing to the revamp of the economy during the post-COVID-19 and electioneering periods. The chart below shows the number of international arrivals in Kenya between 2017 and January 2023;



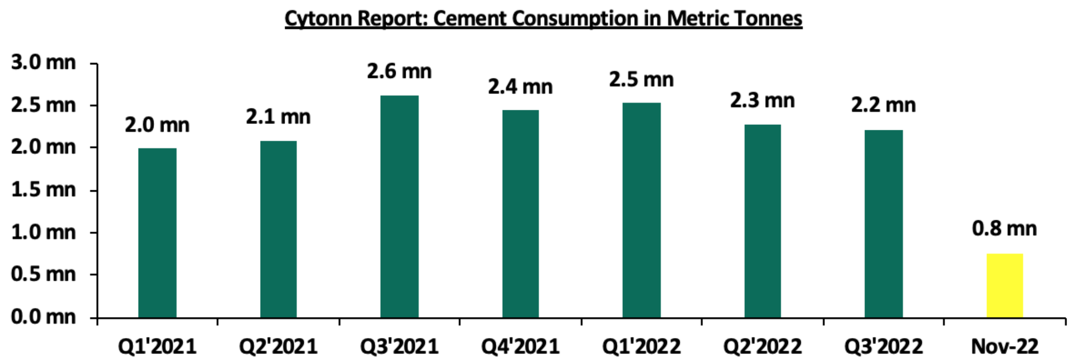
Source: Kenya National Bureau of Statistics (KNBS)

ii. The value of building plans approved in the Nairobi Metropolitan Area (NMA) decreased by 28.9% to Kshs 29.5 bn in Q4’2022, from Kshs 41.5 bn recorded in Q4’2021. On a q/q basis, the performance represented a 29.6% decline, from Kshs 41.9 bn recorded in Q3’2022. The decline in performance is attributable to; i) high development costs on the back of rising prices of construction materials such as cement, steel and PVC driven by inflationary pressure, and ii) pending of approvals amid delays in processing construction permits enhanced by backlogs in registry systems. The chart below shows the value of building plans approved in the Nairobi Metropolitan Area (NMA) between 2021 and 2022;



Source: Kenya National Bureau of Statistics (KNBS)

iii. The consumption of cement increased by 1.6% to 0.8 mn metric tonnes in November 2022, from 0.7 mn metric tonnes realized in October 2022, attributable to initiation of infrastructural developments by the government amid restructuring of the Ministries, Departments, and Agencies (MDAs) involved. On the other hand, the performance represented a 3.6% decline from 0.8 mn metric tonnes realized during November 2021. The decline in performance is attributable to increased costs of the commodity driven by prevailing inflationary pressures from local and external shocks. The chart below shows cement consumption in metric tonnes in Kenya between 2021 and November 2022;



Source: Kenya National Bureau of Statistics (KNBS)

We expect the Real Estate sector to register positive growth and increased performance mainly driven by the increasing number of visitor arrivals into the country boosting performance of serviced apartments and hotels in the country. However, the decline in construction activities with the reduction in the consumption of cement, driven by high construction costs on the back of inflationary pressures are expected to hamper the optimal performance of the sector.

II. **Industrial Sector**

During the week, Improvon, a South African based logistics and industrial developer, announced ongoing expansion efforts to set up mini-warehouse units at Nairobi Gate Industrial Park in Northlands City, Ruiru. The facility targets medium-sized firms seeking specialized logistics solutions and already hosts two 5,000 SQM depots. In the first phase, Improvon plans to erect 40 mini units, each comprising of 550 and 600 SQM in floor space at a rental rate of USD 6.4 (Kshs 860) per SQM, with 19 units already complete. Notable tenants that have already taken mini warehouse units at the facility include Probakery and Mac Coffee Kenya. In addition to mini-units, Improvon also aims to provide bespoke facilities of up to 10,000 SQM catered to large manufacturers. The decision to set-up the warehouse units is driven by;

i. The opening up of prime areas such as Ruiru and Limuru, which are easily accessible through the construction of bypasses around Nairobi city, enabling developers to quickly access Jomo Kenyatta International Airport and the standard gauge railway-linked Inland Container Depot

(ICD) in Syokimau,

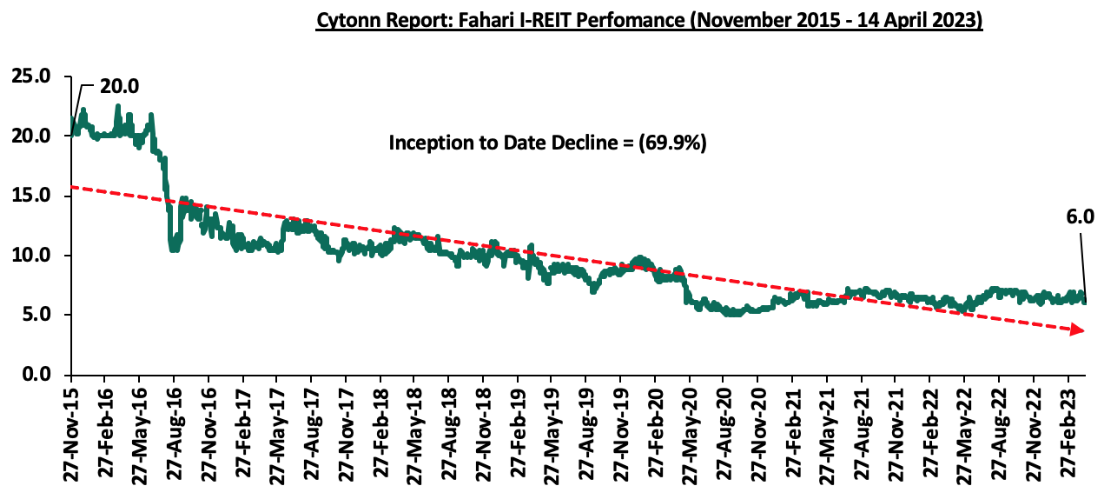
ii. The increasing demand from small and medium-sized enterprises (SMEs), agro-processors, and Fast-Moving Consumer Goods (FMCG) firms for warehousing, which has prompted developers to focus on quality industrial space with ample amenities, parking and, road infrastructure, and,
iii. The strong market fundamentals of the industrial sector, driven by Kenya's positive urbanization rate at 3.7%, compared to the global average rate of 1.6% as at 2021, which is attracting investors to strategically locations that have favorable development policies such as the Northlands City in Ruiru.

We expect the industrial sector to continue recording growth, driven by the rising demand for quality industrial facilities eyeing to cater to the growing demand for prime warehousing and logistics solutions in easily accessible areas, outside the traditional hub of Nairobi's Industrial Area and along Mombasa Road. This will provide more investment opportunities in the industry, allowing further diversification of Kenya's Real Estate sector.

III. Regulated Real Estate Funds

a. Real Estate Investment Trusts (REITs)

In the Nairobi Securities Exchange, ILAM Fahari I-REIT closed the week trading at an average price of Kshs 6.0 per share. The performance represented a 12.0% decline from Kshs 6.8 per share recorded the previous week, taking it to an 11.2% Year-to-Date (YTD) decline from Kshs 6.8 per share recorded on 3rd January 2023. In addition, the performance represented a 69.9% Inception-to-Date (ITD) loss from the Kshs 20.0 price. The dividend yield currently stands at 10.8%. The graph below shows Fahari I-REIT's performance from November 2015 to 14th April 2023;

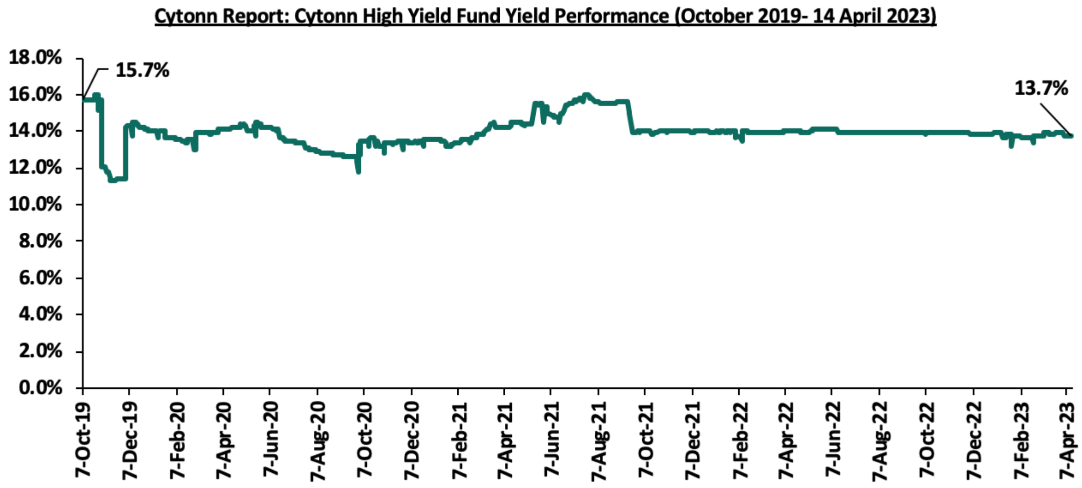


In the Unquoted Securities Platform, Acorn D-REIT and I-REIT traded at Kshs 23.9 and Kshs 20.9 per unit, respectively, as at 14 April 2023. The performance represented a 19.4% and 4.4% gain for the D-REIT and IREIT, respectively, from the Kshs 20.0 inception price. The volumes traded for the D-REIT and I-REIT came in at 12.3 mn and 29.6 mn shares, respectively, with a turnover of Kshs 257.5 mn and Kshs 603.2 mn, respectively, since inception in February 2021.

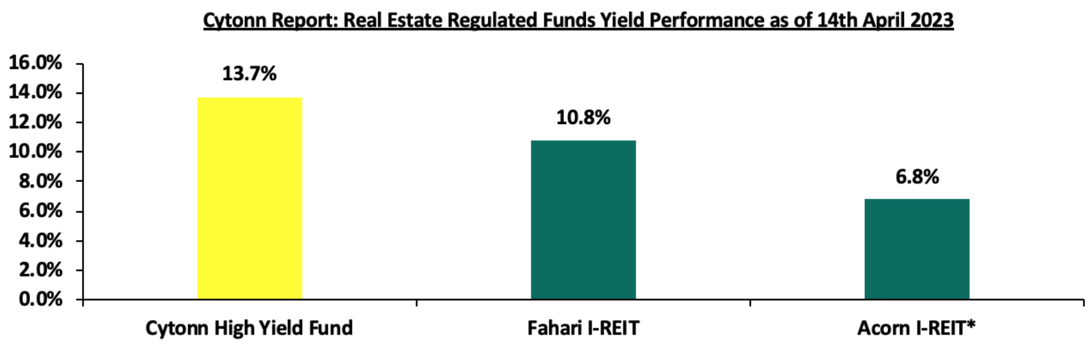
REITs provide numerous advantages, including; access to more capital pools, consistent and prolonged profits, tax exemptions, diversified portfolios, transparency, liquidity and flexibility as an asset class. Despite these benefits, the performance of the Kenyan REITs market remains limited by several 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.

b. Cytonn High Yield Fund (CHYF)

Cytonn High Yield Fund (CHYF) closed the week with an annualized yield of 13.7%, remaining relatively unchanged from the performance recorded the previous week. The performance represented a 0.2% points Year-to-Date (YTD) decline from 13.9% yield recorded on 1 January 2023 and 2.0% points Inception-to-Date (ITD) loss, from the 15.7% yield. The graph below shows Cytonn High Yield Fund's performance from November 2015 to 14 April 2023;



Notably, the CHYF has outperformed other regulated Real Estate funds with an annualized yield of 13.7%, as compared to Fahari I-REIT and Acorn I-REIT with yields of 10.8%, and 6.8% respectively. As such, the higher yields offered by CHYF makes the fund one of the best alternative investment resources in the Real Estate sector. The graph below shows the yield performance of the Regulated Real Estate Funds;



**FY'2022*

Source: Cytonn Research

We expect the performance of Kenya's Real Estate sector to remain on an upward trajectory, supported by factors such as; i) expansion of activity in the hospitality sector with increase in international arrivals, and growing focus into the industrial sector which will open up more areas for more opportunities in Real Estate. However, the rising costs of construction on the back of prevailing inflationary pressure that is hampering development activity, oversupply of physical space in select sectors, and low investor appetite for REITs are expected to continue subduing the optimal performance of the general Real Estate sector.