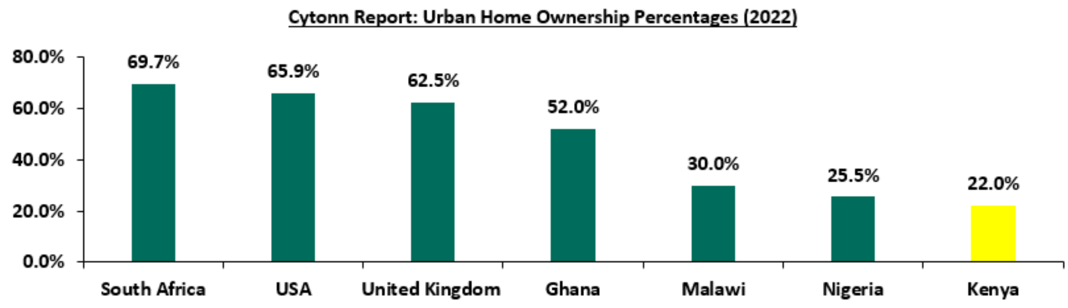
Education Investment Plans in Kenya, & Cytonn Weekly #29/2023

Real Estate

I. **Residential Sector**

During the week, the International Finance Corporation (IFC), the development and investment affiliate of the World Bank Group, disclosed details of its proposed Kshs 3.0 bn (USD 20.9 mn) equity co-investment package to support the development and acquisition of approximately 5,000 newly built, resource-efficient, and affordable green housing properties in the Nairobi Metropolitan Area (NMA), with a minimum of 15.0% of the committed funds set to be allocated selectively to other counties in Kenya. IFC will be partnering with IHS Kenya Green Housing Partnership LLP, and IHS Kenya Green Housing SCS, with the IFC investing up to Kshs 1.6 bn (USD 10.9 mn) from its own account and up to Kshs 1.4 bn (USD 10.0 mn) from the Market Accelerator for Green Construction Program (MAGC), which is a partnership entity between the United Kingdom and the IFC. This blended concessional finance will be 1.2% of the total fund estimated to be worth Kshs 19.9 bn (USD 140.0 mn) from various institutional investors. The management of the Fund will be handled by IHS Kenya Green Housing Fund GP Limited, which is a Nairobi-based private equity firm specializing in affordable housing in Africa. Currently, IHS manages four affordable housing funds in the Southern African region and owns a listed Real Estate Investment Trust (REIT) on the Johannesburg Stock Exchange. With operations in South Africa, Namibia, Botswana, and Kenya, IHS has a strong track record in the African affordable housing sector. However, IFC has not made public the counties that will benefit from its investment or when the affordable housing projects in the country will commence after securing the funds.

We expect the investment by the IFC to be crucial in supporting the prioritized efforts of the current administration to address the annual housing deficit in Kenya, which is estimated to be at 80.0% according to the National Housing Corporation (NHC). The government aims to address this deficit by partnering with the private sector and implementing public sector interventions to provide supporting infrastructure, and streamline transactions in the sector for execution of affordable housing options for its citizens. Additionally, this major move will assist boost the low home ownership rate in Kenya, particularly in urban centers, which stands at 21.3% in contrast to other countries such as South Africa and Ghana, where the home-ownership rates in urban areas are much higher at 69.7% and 52.0%, respectively. The graph below shows the urban home-ownership rate in Kenya compared to select countries as of 2022;



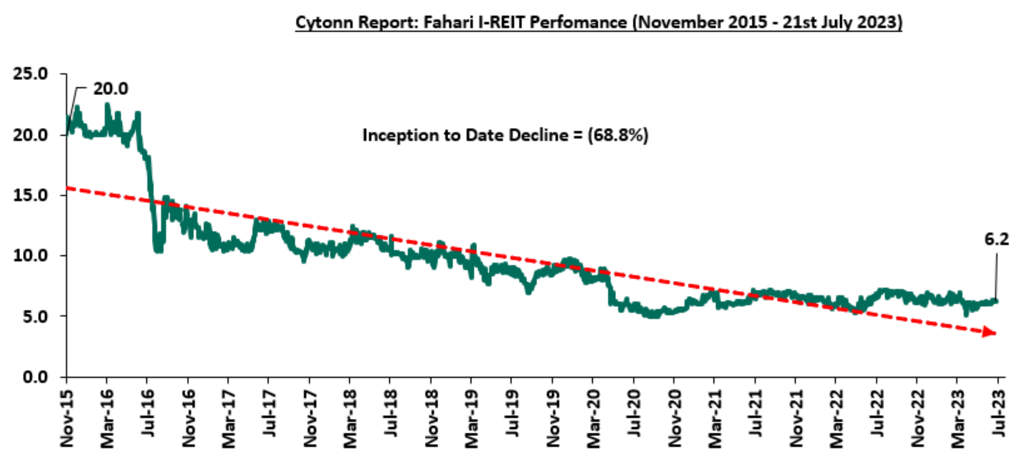
Source: Centre for Affordable Housing Africa, US Census Bureau, UK Office for National Statistics

However, exorbitant cost of financing in the development of housing units remains one of the key challenges facing the Kenyan residential sector. This is influenced by factors such as; i) expensive land prices, ii) rising costs of construction, iii) low income levels, iv) undermined capital markets, and, v) limited access to affordable long-term home loans. As a countermeasure to address some of these factors, the government, together with the World Bank, Primary Mortgage Lenders (PMls), and other financial institutions, established the Kenya Mortgage Refinancing Company (KMRC) in 2018. The KMRC, the sole mortgage refinancer in the country, continuously provides long-term funds to PMLs, such as banks, with the goal of unlocking affordable home loans for Kenyan citizens.

II. **Real Estate Regulated 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 6.2 per share. The performance represented a 0.6% decline from Kshs 6.3 per share recorded the previous week, taking it to an 8.0% Year-to-Date (YTD) decline from Kshs 6.8 per share recorded on 3 January 2023. In addition, the performance represented a 68.8% Inception-to-Date (ITD) loss from the Kshs 20.0 price. The dividend yield currently stands at 10.4%. The graph below shows Fahari I-REIT's performance from November 2015 to 14 July 2023;



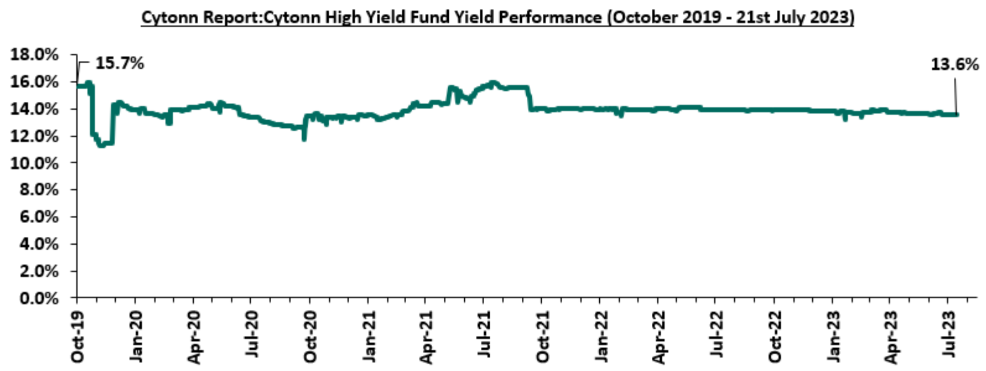
In the Unquoted Securities Platform, Acorn D-REIT and I-REIT traded at Kshs 23.9 and Kshs 21.6 per unit, respectively, as at 14 July 2023. The performance represented a 19.5% and 8.0% gain for the D-REIT and I-REIT, respectively, from the Kshs 20.0 inception price. The volumes traded for the D-REIT and I-REIT came in at 12.3 mn and 30.1 mn shares, respectively, with a turnover of Kshs 257.5 mn and Kshs 620.7 mn, respectively, since inception in February 2021.

REITs provide numerous advantages, including; access to larger 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

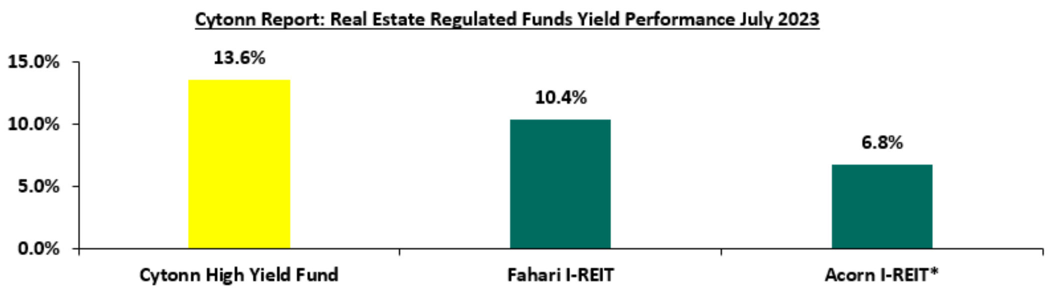
100.0 mn for trustees, and, iv) high minimum investment amounts set at Kshs 5.0 mn discouraging investments.

b. **Cytonn High Yield Fund (CHYF)**

Cytonn High Yield Fund (CHYF) closed the week with an annualized yield of 13.6%, remaining relatively unchanged from the previous week. The performance also represented a 0.3% points Year-to-Date (YTD) decline from 13.9% yield recorded on 1st January 2023, and 2.1% points Inception-to-Date (ITD) loss from the 15.7% yield. The graph below shows Cytonn High Yield Fund's performance from October 2019 to 21 July 2023;



Notably, the CHYF has outperformed other regulated Real Estate funds with an annualized yield of 13.6%, as compared to Fahari I-REIT and Acorn I-REIT with yields of 10.4%, and 6.8% respectively. As such, the higher yields offered by CHYF makes the fund one of the best alternative investment resource 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) initiatives by the government and private sector to prioritize affordable housing, ii) infrastructure developments facilitating investments, and iii) positive demographic trends facilitating increased housing demand. There are, however, a number of challenges that remain, including oversupply in certain real estate sectors, including commercial office and retail, which are both oversupplied, ii) escalating construction costs due to rising inflation, and iii) limited investor knowledge and interest in REITs, which is expected to hinder the sector's optimal performance.