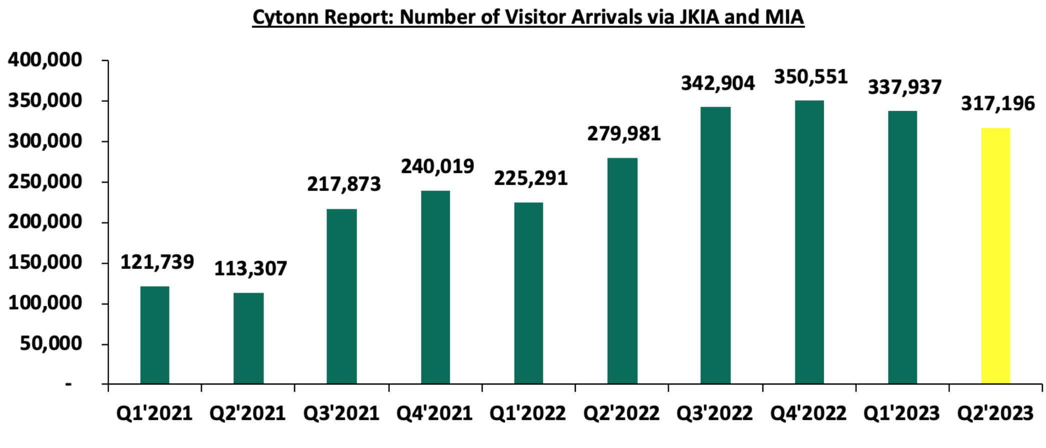
Kenya’s Listed Banks H1’2023 Report, & Cytonn Weekly #38/2023

Real Estate

I. **Industry Reports**

The Kenya National Bureau of Statistics (KNBS) released the Leading Economic Indicators (LEI) June and July 2023 Reports which highlighted the performance of major economic indicators. The key highlights related to the Real Estate sector include;

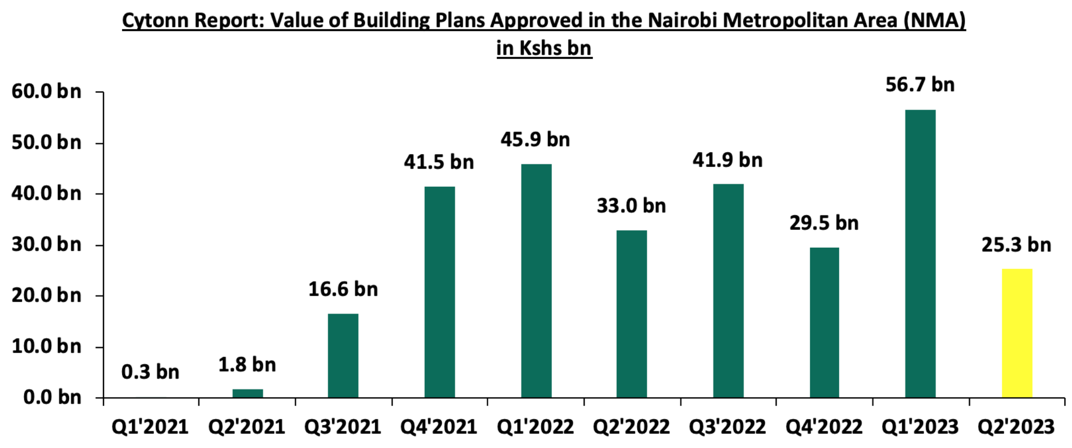
i. Overall international arrivals through Jomo Kenyatta International Airport (JKIA) and Moi International Airport (MIA) increased year-to-year (y/y) basis by 13.3% to 317,196 in Q2’2023, from the 279,981 recorded in Q2'2022. Additionally, for the month of July 2023, the total number of arrivals increased by 26.6% to 158,100 from 124,927 recorded in July 2022. The improvement in performance was attributed to; i) continued intensive marketing of Kenya’s tourism market by the Ministry of Tourism through platforms such as the Magical Kenya platform, ii) the Tourism Board’s alignment of its marketing initiatives towards strategies targeting emerging and established source markets, and, iii) an upsurge in corporate and business meetings, events, and conferences from both the public and private sectors with the new government regime. However, on a quarter-to-quarter (q/q) basis, the performance was a 6.1% increase from 337,937 recorded in Q1’2023, owing to easing of the holiday season within the sector. The chart below shows the number of international arrivals in Kenya between Q1’2021 and Q2’2023;



Source: Kenya National Bureau of Statistics (KNBS)

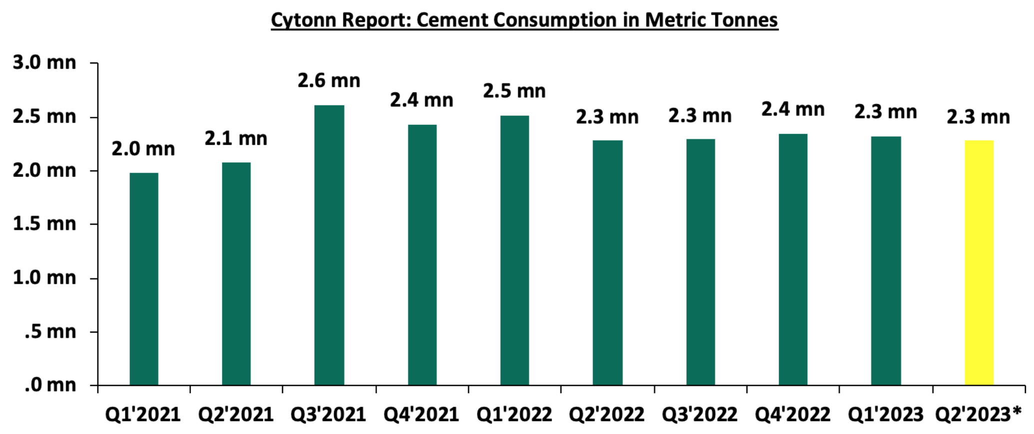
ii. The total value of building plans approved in the Nairobi Metropolitan Area (NMA) decreased y/y basis by 23.3% to Kshs 25.3 bn in Q2’2023, from Kshs 33.0 bn recorded in Q2’2022. In addition, on a q/q basis, the performance represented a 55.4% decline from Kshs 56.7 bn recorded in Q1’2023. The decline in performance was attributable to; i) high development costs on the back of rising prices of construction materials such as cement, paint, steel and Poly Vinyl Chloride (PVC) driven by inflationary pressure, and ii) pending of approvals amid delays in processing construction permits enhanced by backlogs in registry systems. However, for the month of July

2023, the total value of building plans approved increased by 29.3% to Kshs 23.2 bn from Kshs 18.0 bn recorded in July 2022, on the back of increased construction of residential and other buildings in the Real Estate sector within the year. The chart below shows the value of building plans approved in the Nairobi Metropolitan Area (NMA) between Q1'2021 and Q2'2023;



Source: Kenya National Bureau of Statistics (KNBS)

iii. The consumption of cement came in at 2.28 mn metric tonnes in Q2'2023, remaining relatively unchanged on a y/y basis. However, on a q/q basis, performance represented a 2.0% decrease from 2.33 mn metric tonnes recorded in Q1'2023. The decline in performance was attributable to; i) increased costs of the commodity driven by prevailing inflationary pressures on the back of local and external shocks, ii) an increase in pending approvals amid delays in processing construction permits owing to backlogs in registry systems, which led to an overall decrease in the consumption of construction materials, and, iii) reduced infrastructural developments by the government owing to the political transitions, policy shifts, budget constraints, and regulatory changes in the incoming government after the August 2022 general elections. The chart below shows cement consumption in metric tonnes in Kenya between Q1'2021 and Q2'2023;



** Averaged using April & May 2023 figures*

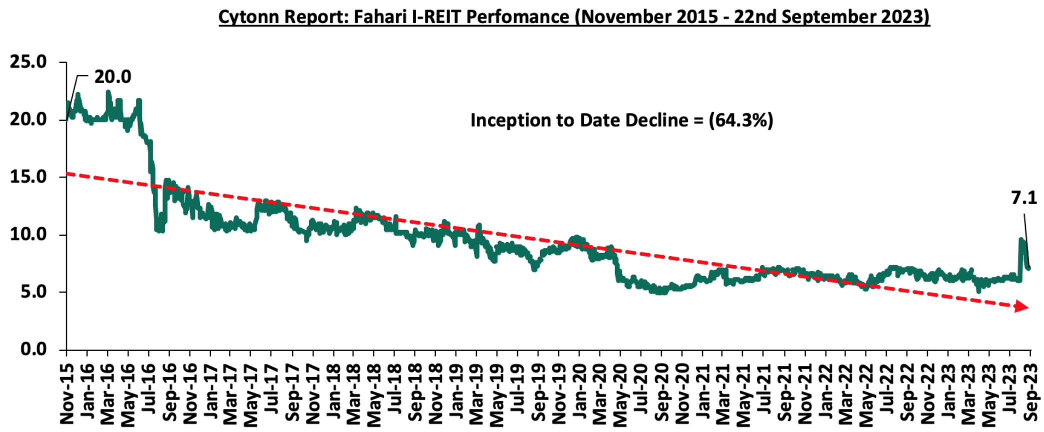
Source: Kenya National Bureau of Statistics (KNBS)

We expect the general Real Estate sector to continue growing in terms of performance mainly driven by the increasing number of visitor arrivals into the country which will enhance the performance of serviced apartments and hotel accommodations by boosting room and bed occupancies, restaurant activities and the generally the hospitality sector. However, the decline in construction activities evidenced by the reduction in the consumption of cement owing to rising construction costs on the back of inflationary pressures is expected to continue subduing the optimal performance of the sector.

II. 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 7.1 per share. The performance represented an 8.5% decline from Kshs 7.8 per share recorded the previous week, taking it to a 5.3% Year-to-Date (YTD) growth from Kshs 6.8 per share recorded on 3 January 2023. However, the performance represented a 64.3% Inception-to-Date (ITD) loss from the Kshs 20.0 price. The dividend yield currently stands at 9.1%. The graph below shows Fahari I-REIT's performance from November 2015 to 22 September 2023;

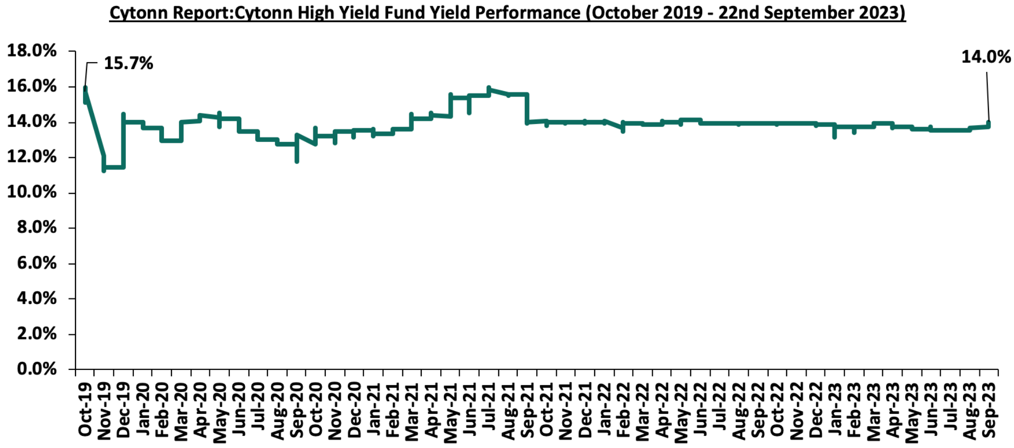


In the Unquoted Securities Platform, Acorn D-REIT and I-REIT traded at Kshs 25.3 and Kshs 21.7 per unit, respectively, as at 15 September 2023. The performance represented a 26.6% and 8.3% gain for the D-REIT and I-REIT, respectively, from the Kshs 20.0 inception price. The volumes traded for the D-REIT and I-REIT came in at 12.3 mn and 30.6 mn shares, respectively, with a turnover of Kshs 257.5 mn and Kshs 632.1 mn, respectively, since inception in February 2021.

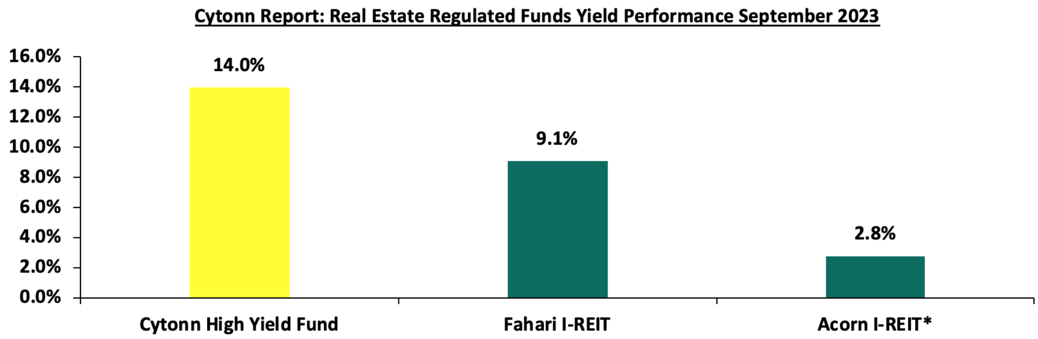
REITs provide various benefits like tax exemptions, diversified portfolios, and stable long-term profits. However the continuous deterioration in performance of the Kenyan REITs and restructuring of their business portfolio hampering major investment they had previously made are on top of other general challenges such as; i) inadequate comprehension of the investment instrument among investors, ii) prolonged approval processes for REITs creation, iii) high minimum capital requirements of Kshs 100.0 mn for trustees, and, iv) minimum investment amounts set at Kshs 5.0 mn, continue to limit the performance of the Kenyan REITs market.

b. Cytonn High Yield Fund (CHYF)

Cytonn High Yield Fund (CHYF) closed the week with an annualized yield of 14.0%. The performance represented a 0.2% points increase from 13.8% recorded the previous week, taking it to a 0.1% points Year-to-Date (YTD) growth from 13.9% yield recorded on 1 January 2023. However, the performance represented a 1.7% points Inception-to-Date (ITD) decline from the 15.7% yield. The graph below shows Cytonn High Yield Fund's performance from October 2019 to 22 September 2023;



Notably, the CHYF has outperformed other regulated Real Estate funds with an annualized yield of 14.0%, as compared to Fahari I-REIT, and Acorn I-REIT with yields of 9.1% and 2.8% 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:



** H1’2023*

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) positive demographic trends driving housing demand which poised to further increase construction activities, ii) boosted tourist arrivals that is supporting the hospitality sector, and iv) rapid expansion of investors to serve the retail sector. However, the sector's optimal performance is expected to be subdued by the rising construction costs on the back of inflationary pressure, oversupply of physical space in the commercial office and retail sectors leading to slower uptake of new spaces, and limited investor knowledge in REITs coupled with high minimum investment amounts that are stymying the asset class.