Nairobi Hospitality Report 2017, & Cytonn Monthly – November 2017

Real Estate

Residential

During the month of November, Kenya Bankers Association (KBA), released their Q3'2017 Housing Price Index (KBA-HPI), which tracks both qualitative and quantitative factors that determine pricing in the housing sector. The key take-outs from the report were:

i. House prices increased by 0.4% in Q3'2017 compared to 1.0% increase in Q2'2017. The lower growth can be attributed to: (i) the observed slowdown in credit growth in the private sector at 1.6% over the 12-months to August 2017 from a 4-year average of 14.8% from January 2013, and (ii), a wait-and-see stance adopted by investors during the electioneering period,
ii. Apartments accounted for 82.7% of the total number of units sold in Q3'2017, with maisonettes and bungalows accounting for 10.7% and 6.6%, respectively, attributed to affordability of apartment units compared to maisonettes and bungalows.

For more details, please see our Cytonn Weekly #45.

Also, in his inauguration speech, the President of Kenya, Uhuru Kenyatta, announced plans to introduce an affordable housing scheme that will see every working family own a decent home. The Kenyatta Administration set a target of approximately 500,000 new homes by 2020. Though a timely move given the housing units deficit of approximately 2 mn as per African Development Bank, the Government will have to address the key factors that have been hindering a successful provision of affordable housing such as i) prohibitive land costs (as per the Cytonn Land Report 2017, land prices increased by 2.5x between 2011 and 2016), (ii) unfavorable policies such as the interests rate capping law that have depressed credit advancement to home buyers, and the private sector in general, iii) costly construction materials, (iv) high financing costs, and v) opacity on issuance of title deeds.

As per the Kenya National Bureau of Statistics' Economic Survey 2017, Nairobi County recorded only 8,623 private residential completions with 1,062 public, a total of 9,685 completions.

We maintain a positive outlook for the residential sector given the large housing deficit that stands at 200,000 units per annum, as a result of the expanding middle class and rapid urbanization rate of 4.4% p.a against a global average of 2.1%.

Commercial Offices

The United Nations submitted a proposal to the UN General Assembly to upgrade the infrastructure in its offices in Gigiri, Nairobi, to (i) achieve full environmental green building policies, (ii) accommodate more staff, and (iii) enhance ease of accessibility of the Gigiri offices for people with disabilities at a cost of Kshs 7.0 billion over the next 7-years. This is a right move by the institution in embracing green building technology as it sets the pace for construction of environmentally friendly buildings in the region. Green buildings have been proved to reduce operational costs and are a feature of most top-rated office buildings.

Gigiri, as per our Cytonn Office Report, is a good market with the highest Grade A office supply taking 75% of its market share, compared to other office nodes. Also, according to the report, the opportunity for office space is in Grade A office space given the continued entrance of multinational firms in the region who create demand for top notch office space. For more details, please see our Cytonn Weekly #45.

Retail

The sector showed better trends compared to the previous months, during which the real estate theme was characterized with such issues as outlets' closures due to financial constraints. During the month of November;

i. The newly expanded Village Market formally opened its doors, with the local dailies reporting high occupancy rates of 95%. The expanded section adds 230,000 SQFT of lettable space to the mall, adding 100 line shops, over 900 parking bays, a business conference hotel, children's play area, and a 30,000 SQFT gym, expected to be taken up by Ignite Fitness, a South African gym brand. Other international brands setting up shop at the mall include clothing stores such as Foschini, Celio and Markhams;
ii. French based retailer Carrefour opened its third local branch at the Thika Road Mall. The TRM space, previously occupied by the troubled Nakumatt, covers over 5,000 SQM of selling space. The location of the mall is apt for retailers given the densely populated areas of Roysambu and Kasarani, as well as the busy Thika Superhighway, all acting as a guarantee for high footfall;
iii. Quick Mart is set to open two new outlets in Nairobi on Kikuyu Road and along the Eastern Bypass, growing its total number of branches to 8;
iv. Massmart Holding's, a subsidiary of Game, announced plans to open a new store at the 200,000 SQFT Waterfront in Karen, set to open in January 2018, replacing Nakumatt, the initial proposed anchor tenant.

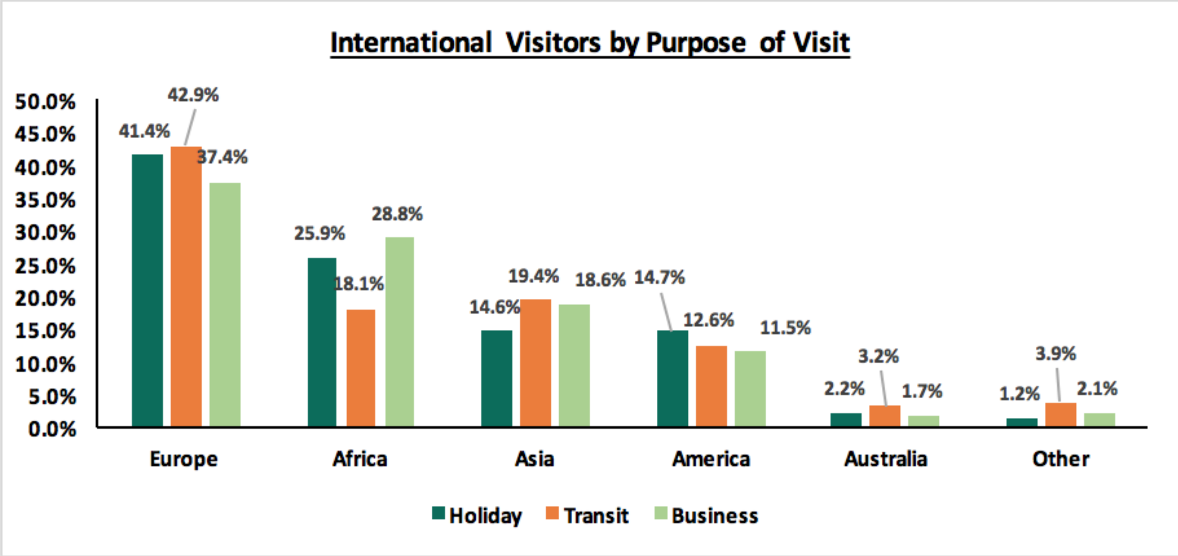
Other retailers such as Tuskys and Naivas also increased their portfolios during the month as the sector continues to attract interest from both international and local retailers indicating a probable upward growth of the sector. For more of these details please visit Cytonn Weekly #47.

We project an improved performance of the sector in 2018 on the back of stabilizing macroeconomic and political environment.

Hospitality

During the month, the hospitality sector continued to decline in performance given the political headwinds. According to Jambojet's Chief Executive, Willem Hondius, the extended electioneering period resulted in a 16% decline in flight bookings for the period June to October, for the airline. However, visitors' arrivals increased in the period January to July this year by 32.1% to 105,241 in July from 79,690 in January, as per The Kenya National Bureau of Statistics, Leading Economic Indicators July 2017. However, the arrivals dropped to an annual low in the months of October and November, which recorded 66,897 and 64,091 tourist arrivals, respectively, attributable to the political tensions in the said period. We remain positive about the sector's performance, which we expect will rebound in 2018 given government incentives:

i)The Kenyan President, in his inauguration speech, announced liberal entry for all African visitors into Kenya, meaning that visitors from all African Nations shall be receiving visas at the port of entry, a move that we expect to motivate and thus, increase visitors' arrival from African nations. As of 2016, African countries accounted for the second largest visitors' arrival to Kenya after Europe for holiday and business visits as shown below;



Source: Cytonn Hospitality Report 2017

ii)The African Development Bank (AfDB) approved a Kshs 16.5 bn loan for building a 4.9 km long second runway at the Jomo Kenyatta International Airport to enhance mobility at the airport. The runway will enable support more air traffic and offer extra parking slots for aircrafts, among other perks. Currently, the airport has a capacity of 6 mn passengers annually, which is set to increase to 12.5 mn per annum passengers once the runway is completed, as per reports in the local dailies,

iii)World Travel Market London in association with Euromonitor International named Kenya as one of the leading hotspots for luxury hotel investments in Africa, after South Africa,

iv)Additionally, TravelBird, an online travel and vacation booking firm based in Amsterdam, ranked Nairobi City as the 93rd (out of top 500 global tourist destinations) most welcoming city in the world ahead of major cities such as Budapest (Hungary), Cairo (Egypt) and Bucharest (Romania).

Other highlights in the hospitality sector included:

i. Hotel chain Hemingways Collection announced plans to officially open the sale of its new venture, Watamu Residences in Watamu, this week. The development will comprise of 3 one-bedroom units, 16 two-bedroom units and 2 four-bedroom units selling at Kshs 45 mn, Kshs 60-80 mn and Kshs 140 mn, respectively,
ii. Marriott International, opened 172-roomed Four Points by Sheraton Nairobi Airport hotel at Jomo Kenyatta International Airport (JKIA),
iii. The National Museum of Kenya (NMK) announced that it is seeking to raise Kshs 1.5 bn to construct Africa's biggest biomes and cultural artefacts collection museum center on a 5-acre land parcel at Ololua Forest, Nairobi. Kenya National Economic Survey 2017 Report shows that the number of visitors to museums, snake parks and historical sites increased at a 3-year CAGR of 6.2% in 2013/2016 period, reporting a 15.8% increase in the number of visitors from 797,500 in 2015 to 923,100 recorded in 2016,
iv. Following its regional expansion strategy, Jambojet, the affordable airline subsidiary of Kenya Airways, announced plans to commence flights to Tanzania and Uganda by February 2018, with plans underway to venture into other African countries. Currently the airline operates local flights only,
v. Paddock Investments renewed plans to build a 220 bed, 4-star hotel on 8.4 acres in Runda Estate. The firm forwarded a new request to the National Environmental Management Authority (NEMA) to build the Kshs 1.0 bn hotel, having previously faced opposition from the Runda Gated Community Association.

Following the closure of the electioneering chapter, we expect the sector to fully recover

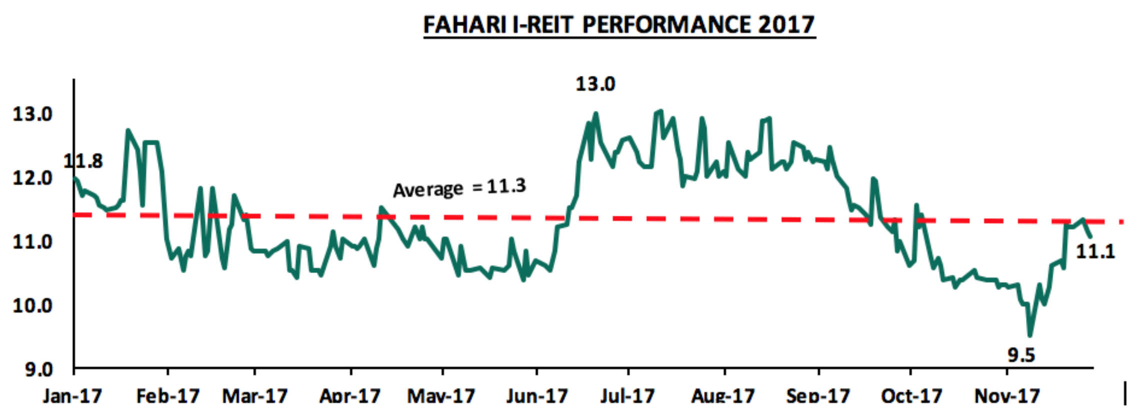
characterized by increased tourist arrivals and thus, increased hotel occupancy rates

Other highlights in real estate included:

i. KURA announced an earlier-than-planned completion of Ngong Road's Phase 1 upgrade. The upgrade which was set for completion in April 2018 is expected to be complete by end of December this year. Phase 1 runs from Kenya National Library to Ring Road Kilimani Junction; Phase 2 from Ring Road Junction to Dagoretti Corner, while Phase 3 will run from Dagoretti Corner to Karen Shopping Centre;
ii. Britam Holdings, an insurance, pensions and asset management company, announced that it will be spending half of its Kshs 9.0 bn equity fund in new real estate projects as part of the firm's strategic plan for 2016- 2020. One of the project in its pipeline, which is being developed under the insurance company, is the Kshs 3.3 bn serviced apartments in Kileleshwa, projected for completion in 2019; it is not clear how the real estate strategy and investments will be managed between the various businesses – the group, the insurance company and the investment management arm, all of which have separate mandates;
iii. Kings Pride Properties Limited, a local real estate developer, is reported in the local dailies to have signed a deal with Milost Global Inc., a New York based private equity firm with over USD 25.0 bn in committed capital, to get Kshs 45.0 bn in equity cum debt financing for the expansion of their real estate developments;
iv. The Transport Ministry announced plans to commence the construction of the Kshs 62 bn LAPSSET project by mid-next year. The first section will cover Lamu-Garissa-Isiolo Highway, which is expected to take 4-years. The LAPSSET, which will be Eastern Africa's largest infrastructure project, was launched in 2013 with a planned development cost of Kshs 2 tn. We expect the road to open up other areas for investment such as North-Eastern Kenya, and lead to an increase in land prices.

Listed Real Estate

In the listed real estate sub-sector, the Fahari I-REIT's share price increased by 7.8% m/m closing at Kshs. 11.05 in the month of November from Kshs. 10.25. Since its inception, the instrument has shed 46.8% of its value, from Kshs 20.8 (the price at which it was floated at), in November 2015. We attribute the improvement to the recent measures by Capital Markets Authority to improve listed real estate's performance by exempting it from value Added Tax, in addition to its exemption from capital gains tax and stamp duty by Kenya Revenue authority (KRA), while also investor demand given the attractive entry points and low valuations given the drop in prices.



Source: Bloomberg

We anticipate further growth in the real estate sector and a better performance in 2018 than 2017 as a result of (i) improving operating environment, (ii)end of the political uncertainties and (iii) probable revision of unfavorable policies such as the 2015 Bank

Amendment Act leading to improved credit advancement to the private sector, which is crucial to the capital intensive real estate sector.

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