Cytonn Monthly - April 2018

Real Estate

In our Q1' 2018 Market Review, we stated that the real estate sector exuded signs of recovery following the end of the protracted electioneering period. This was evident this month, with; i) a number of reports being released showing positive growth in the sector, and ii) an increase in activities, both expansionary, and development as expounded below;

Industry Reports

During the month, a number of reports were released that indicated the real estate sector in Kenya was recovering from the slump witnessed last year. The recovery is mainly as a result of i) increased government support and ii) favourable operating environment following the conclusion of the protracted electioneering period. The various reports are as explained in the table below;

Report	Theme	Key Take Outs
Hass Consult House Price Indices	Residential	· The residential market picked up in Q1' 2018 following the conclusion of the prolonged electioneering period, · The asking prices for residential property sales increased by 2.4% during the quarter, while the asking rents also increased by 1.0% during the same period,
Hass Consult Land Price Indices	Land	· Land recorded a slow annual growth rate of 7.4% which represents a 4.7% points y/y decline from a growth rate of 12.1% in Q1' 2016,
Hass Consult County Land Index		· Land recorded an overall 1.4% q/q increase in asking prices, with satellite towns recording a 2.4% q/q growth in land prices, outperforming Nairobi suburbs, which recorded a 0.2% q/q increase,
Cytonn Nairobi Metropolitan Area Land Report		· Land prices in Nairobi Metropolitan Area grew by 3.7% in 2017, down from growth with a 6-Year CAGR of 17.0%, as a result of the extended electioneering period. The prices are however expected to grow by 10.2% in 2018, as a result of expected increased activity in real estate, due to conclusion of the electioneering period,
2018 East Africa Hotel Market Review by JLL	Hospitality	· Nairobi's performance in 2017, was subdued, registering the sharpest decline in RevPAR in East Africa, of 17.8% to USD 60 in 2017, · However, the sector's performance is expected to recover in 2018, on the back of growth in tourist arrivals, public sector support for tourism, as well as new air routes in the long term,
KNBS Economic Survey 2018		· Hospitality sector contribution to GDP grew by 0.1% points y/y, from 1.1% in 2016 to 1.2% in 2017, · The sector remained resilient to the tough political environment in 2017, and grew by 14.7%, from a 13.3% growth recorded in 2016, · The number of international arrivals grew by 8.1% to come in at 1.4 mn in 2017 from 1.3 mn in 2016,

During the month of April, the performance and activities of the various real estate themes are as highlighted below:

i. Residential

The residential sector recorded an increase in activities mainly driven by the government focus on affordable housing. During the month, a number of developers broke ground on real estate projects or announced plans to undertake development. These included:

i. Cytonn Real Estate, the development affiliate of Cytonn Investments broke ground on a Kshs 15.0 bn, 100-acre master planned project, in Ruiru, Kiambu County. The development will feature apartments, residential villas, recreational facilities such as a water park and swimming pools as well as a convenience centre, with approximately 1,000 SQM of retail space,
ii. Krishna Estates Limited, announced plans to put up a Kshs 1.2 bn residential flats project on 2-acres, comprising of 64 two-bedrooms, and 180 three-bedroom units, in Thindigua, along Kiambu Road, Cytonn Weekly #14 ,
iii. Rendeavour, the developer of Tatu City, announced plans to include a 300-acre affordable housing project within Tatu City. The development is set to commence in April 2019, and will see the development of 10,000 affordable housing units priced between Kshs 1.5 mn to 5.0 mn, Cytonn Weekly #17 ,
iv. Five joint venture firms including Kesa, Meridiam, JV Unicamp, PDM-Roko-CBA Capital Consortiums and a Chinese company, Chinese Overseas Engineering, have been chosen to build 23,400 hostel rooms in various universities across the country including; Moi University, Embu University and South Eastern Kenya Universities (SEKU). Moi University intends to build a 14,000-unit facility; Embu University will have a 4,000-bed facility while SEKU will have a 5,400-unit facility. Under the proposed PPP model, the hostels developers will gain returns on their investment through a built to rent operation for 15-20 years, after which they will recover their principal and interest then hand over the facility to the respective institutions of learning. The public-private partnership model has been floated over the last couple of years as the most efficient way to address the housing shortage in local universities but most partnerships such as the Kenyatta University and US-based Africa Integra for the construction of a 10,000-room facility at a tune of Kshs 5.1 bn announced in year2015, are yet to materialize due to the various challenges that face PPP models, but remain unaddressed, such as the inability to transfer public land to Special Purpose Vehicle, the long-term nature of PPPs, as well as vague compensation models for the private partners, Cytonn Weekly #17. The government is however planning to review this law and others to streamlined PPPs and affordable housing agenda, and,
v. The government through a concept paper in regards to the affordable housing initiative, intends to work with county governments and the National Social Security Fund (NSSF) to fasten the provision of affordable housing. The county governments will aid in creating the much-needed land banks as per the government target of a total of 6,800 acres across various counties that is 3,000 acres in Nairobi, 1,200 in Mombasa, 1,000 in Kisumu, 800 in Eldoret and 800 in Nakuru. To this end, the County Government of Homa Bay signed a memorandum of understanding during the month, with the National Government, for the development of 2,000 affordable homes where the County will provide 18 acres for the cause. Cytonn Weekly #17

We expect to continue witnessing increased activities in the residential sector in the year boosted by i) government initiatives, such as the focus on affordable housing ii) an available market given the shortage of housing units that stand at 2.0mn units with an effective annual shortfall of 200,000 units, and iii) positive demographic trends such as a rapid population growth of 2.6% p.a higher than global averages of 1.2%, and rapid urbanisation rates of 4.4% p.a compared to global average of 2.1% thereby creating demand for housing units in the country.

ii. Retail

In retail sector, foreign retailers continue making inroads in the Kenyan retail sector capitalizing on the financial woes of some of the major local retail chains. During the month, French-based retailer, Carrefour, opened its 5th outlet at the Sarit Centre Shopping Mall and announced plans to open a 6th outlet at the Village Market, taking up space vacated by Uchumi and Nakumatt, for Sarit Centre and Village Market, respectively. In addition to these stores, the retail store has four other stores at The Hub in Karen, Two Rivers Mall along Limuru Road, Thika Road Mall along Thika Superhighway and the Junction Mall along Ngong Road. The retailer ventured into the Kenyan market in May 2016, and has recorded revenues of up to Kshs 1.5 bn in the first seven-months of operations in its first outlet in The Hub Karen, hence supporting the aggressive expansion in the Kenyan market. The expansion activities by retailers indicate a healthy retail sector, which is supported by; (i) positive demographics evidenced by high population growth rate of 2.6% against global average of 1.2% that has led to sustained demand, (ii) high urbanization rates of 4.4% higher than global rates of 2.1% that has resulted in the need for more retail stores, (iii) high economic growth rates with a GDP growth rate averaging above 5.0% over the last 5 years thus boosting disposable incomes, and increasing purchasing power, (iv) rapid growth of infrastructure making more areas accessible to investors, (v) Kenya's growing position as a regional and continental hub hence witnessing an increase in multinationals operating in the county, (vi) huge opportunity, with Kenya having a formal retail penetration of 35% according to Oxford Business Group, compared to markets like South Africa with a penetration of 60%, and (vii) e-commerce as seen through the increased digitization of cash systems and a rise in mobile money and access to internet.

We thus have a positive outlook for the retail sector in Kenya. However, retailers, especially local chains will have to institute better financial and supply chain management processes, and strong corporate governance frameworks, in order to avoid pitfalls that Nakumatt and Uchumi are struggling with.

iii. Hospitality

During the month of April, the hospitality sector continued to attract investment from global players, this was seen through Movenpick, a 5-star brand by Movenpick Hotels and Resorts, and owned by the Kampala based, Golf Course Hotel, opening a new brand in Westlands. The 5-star hotel will feature 128 guest rooms of 54, 1 and 2 bed residential apartments, 94 suites, and 4,000 SQM of conference space. The brand will be joining other top brands currently operating in the country such as: Accor Hotel, Four Points by Sheraton, RadisonBlu Hotel, and Kempinski. The hotel industry in Kenya has been recording increased investment by both local and foreign retailers, with the total room nights in Nairobi growing with a 7-year CAGR of 4.6% from 1.5mn room nights in 2011 to 1.9mn room nights in 2017. The city has a cumulative supply of 5,620 top-rated hotel rooms and 2,945 more rooms are expected to come into the market in the next two years, with the completion of hotels such as: Avic Towers and Pullman in Westlands, and Radisson Residence in Kilimani. We, therefore, project further growth in the hospitality sector as a result of i) restoration of political calm, ii) the revision of negative travel advisories, warning international citizens, e.g. from the United States against visiting Kenya, iii) positive reviews from travel advisories such as Trip Advisor who ranked Nairobi as the 3rd best place to visit in 2018, only behind Ishigaki Island in Japan and Kapaa in Hawaii, and The Travel Corporation who ranked travel to Kenya as one of the top 10 transformative travel experiences in the world, iv) improved hotel standards as hotels rebrand while some embark on refurbishment and expansion, and v) improved flight operations and systems such as direct flights from the USA which are set to commence this year.

Other highlights of the real estate sector during the month of April 2018 include:

i. High Court Judge Wilfrida Okwany suspended a notice published on April 4, 2018, by the Ministry of Lands discontinuing manual transactions at both the Nairobi and Central Registries to pave way for online transactions. The digitization move was disputed by the Law Society of Kenya (LSK), which termed it as illegal on the basis that; i) it is against section 34 of the Advocates Act, which states, “no unqualified person shall, either directly or indirectly, take instructions or draw or prepare any document or instrument relating to the conveyancing of property”, (ii) Parliament was yet to pass a law that supports online land transactions, (iii) many Kenyans have no access to internet and using an online portal will expose them to the risk of being dispossessed of their lands, and (iv) online processing of land transactions would expose the property owners to risk of fraud and loss of property through acts such as hacking, Cytonn weekly #16 ,

ii. The National Assembly majority leader tabled a bill in Parliament seeking to amend the Stamp Duty Act to exempt first time home buyers from paying stamp duty. Stamp duty tax is paid on the market value of a property at the rate of 4.0% for urban areas and 2.0% for rural areas and is payable within 30-days of signing of the sale agreement. In our opinion, if the bill is passed, it will be a move in the right direction, as despite the minimal effect on the total house price, it will reduce the first time home buyers’ financial burden, Cytonn weekly #16 , and,
iii. In a bid to increase home affordability, the government, proposed the following legal amendments; i) the NSSF Act to raise member’s contribution from current rates of Kshs 400.0 to Kshs 1,080.0 and ii) the Income Tax Act that proposes to raise tax rebates to Kshs 8,000 under the Home Ownership Savings Plan, to employees who save with mortgage institutions from current Kshs 4,000. Cytonn Weekly #17

Our outlook for the real estate sector is positive given the conducive operating environment following the conclusion of the general elections, increased investor confidence as evidenced by inroads and expansion by both local and international retailers, as well as increased government interest as seen through the various incentives by the state such as the tabling of a bill to scrap off stamp duty for first time home buyers, inclusion of affordable housing among the top 4 key pillars of focus in the next 5-years, and the income tax act that proposes to raise tax rebates to Kshs 8,000 under the home ownership savings plan.
