Kenya Listed Banks Q1’2018 Report, & Cytonn Weekly #24/2018

Real Estate

During the week, the residential sector continued to attract activity, especially in line with the Kenya Central Government affordable housing initiative that could see the delivery of 1.0 mn units in the next four years across Kenya. The County Government of Kiambu has called for developers in the wake of its plan of putting up 12,500 housing units in a rent-to-own scheme that will target urban residents of Kiambu. The project is set to take up 50 acres of public land and will comprise of studio units, 1-bedroom, 2-bedroom and 3-bedroom units with a plinth area of 20 SQM, 30 SQM, 40 SQM and 60 SQM, selling at Kshs 0.6 mn, Kshs 0.8 mn, Kshs 2.0 mn and Kshs 3.0 mn, respectively. In addition, the County will have 7,000 units to replace old ones with first priority given to Ruiru, Juja and Kiambu towns making a total of 19,500 units to be delivered by 2022. The project aims at having 240 units per acre and will kick start with the development of 43 units, whose sizes remain undisclosed, for Thika Government Quarters residents at a cost of Kshs 30.0 mn, which translates to Kshs 697,674 per house, exclusive of land costs as it is on public land. Nairobi County also announced plans to have old low-rise units located in prime areas demolished to pave way for its own tenant purchase scheme that will see the development of 36,840 units. The demolishment will take place in public land earmarked in neighborhoods such as Starehe, Muguga Green, Shauri Moyo and Makongeni Estates for the development program. In our view, tenant purchase schemes are a step in the right direction in housing the low middle-income segment. As per the KNBS Kenya Integrated Housing Budget Survey, 89.5% of rural residents own homes in comparison to 26.5% of their urban counterparts, resulting to a huge housing deficit of approximately 2.0 mn, according to the National Housing Corporation, with the problem being more pronounced in urban areas. Affordable and social housing have been a challenge for private developers due to high land costs in Kenya, as well as lack of sufficient infrastructure in areas where land is affordable; on the other hand, public-private partnerships are challenged by: (i) Regulatory hindrances such as lack of a mechanism to transfer public land to a Special Purpose Vehicle (SPV) to facilitate access to private capital through the use of the land as security, (ii) Lack of clarity on returns and revenue-sharing, and (iii) Bureaucracy and slow approval processes. The partnership between the County Governments and private developers will therefore ease development costs and enhance the technical knowhow in the delivery of the units while paving way for more PPP models.

The Lands Ministry launched the Sessional Paper No. 1 of 2017 National Land Use Policy (NLUP), aimed at curbing land grabbing and poor land management. Land use planning puts order and regulates how land within urban cities is utilized, thus promoting efficiency and reducing land use conflicts. This in turn will enhance an orderly disposition of land leading to a methodical approach to developing neighborhoods especially with the relatively high rates of rural to urban migration. The policy is a prerequisite to the National Spatial Plan, County Spatial Planning Guidelines and the Physical Planning Act. In our view, this will especially aid in the delivery of the affordable housing units in the Big 4 Agenda, where availability of land has been a key challenge and will also enhance the efforts to improve the mortgage market, which has been laden with difficulties with property registration and titling. Other initiatives by the lands ministry include the digitization of the lands ministry, scrapping of the NEMA and titling search fees.

Also during the week, Azalea Holdings, the developers of The Hub announced plans to have Japanese retailer Miniso and international retailer Decathlon, setting up shop at the regional mall located in Karen. The mainstream retail sector in Nairobi has been on the decline in terms of performance, recording 9.0% points decline in occupancy to 80.3% in 2017 from 89.3% registered in 2016, mostly attributable to the increased supply of mall space and thus developers have to employ prudent methods of attracting clientele and enhancing footfall, especially by providing a wide variety of products. These methods include attracting retailers, especially international retailers looking to set up shop locally due to increasing demand driven by expansion of the middle-income class. Currently, major malls such as Two Rivers and Garden City have employed strategies such as provision of high quality space and green technology buildings that are known to attract foreign retailers. Notable international retailers that have set up shop include Carrefour, LC Waikiki, Subway and Burger King, among others, and these brands have gained traction as the middle class' tastes and preferences continue to broaden in line with international trends. Retail developers such as Two Rivers and Garden City who have enhanced their marketing strategies record higher occupancy rates averaging at 86.3% than the market average at 80.3%.

Infrastructure

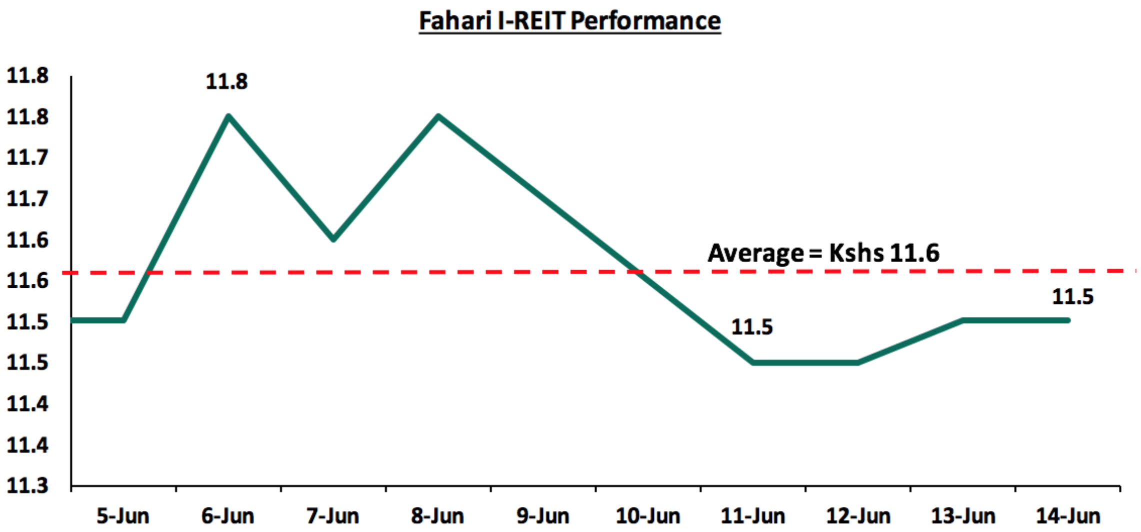
- The Miritini-Mwache-Kipevu link Road/Dongo-Kundu Bypass in Mombasa was launched by the President of Kenya, H.E Hon. Uhuru Kenyatta. The Kshs 11.5 bn project, which kick started in 2015, is 10.1 km and is part of Mombasa Port Area Road Development Project. It is expected to integrate the Port of Mombasa, Moi International Airport, Standard Gauge Railway Mombasa Terminus, the Nairobi-Mombasa Highway, among other routes, reducing congestion and stimulating tourism in the region by providing easy access to accommodation facilities,
- During the week, the dualling process of the Salgaa-Mau summit highway kicked off with China Railway as the main contractor. The government is set to spend approximately Kshs 500 mn for the 22 km long highway, to be completed by 2019. The upgrade will involve redesigning, construction of emergency runaway truck rumps, repair of guardrails, and installation of the requisite road signs. We expect this to open up the North Rift-located regions for investment activities thus improving the country's economy.

Other Weekly Highlights:

- Struggling Uchumi has announced plans to franchise its Lang'ata Hyper branch in its franchising model strategy that is aimed at improving its financial muscle following financial constraints and internal operational woes. The retailer is targeting 200 franchise mini-shops across the country,
- Kisumu County announced plans of setting up a Kshs 100 mn ICT Park. In our view, the ICT Park will create numerous employment opportunities thus elevating the face of the county. This in turn will create demand for real estate especially residential sector in the county which currently records 4.8% rental yield on average, as per Cytonn Research,
- Also, a local real estate development firm Exurbia Living launched a new housing project in Gikambura, Kikuyu. The project dubbed Jacob Gardens will be a controlled development of serviced 0.125 acre plots selling at Kshs 2.5 mn per plot. Kikuyu has been hailed as one of the best performing satellite towns with growth enhanced by good infrastructure such as the Southern Bypass, and proximity of key business districts such as CBD and Westlands.

Listed Real Estate

The Fahari I-REIT declined by 2.5% in share price, having closed at Kshs 11.5 during the week from Kshs 11.8 the previous week. The average price is Kshs 11.6, which is 10.6% higher than 2018's opening price of Kshs 10.5. We attribute the poor and unstable performance to poor investor knowledge and preference for better performing equities and government securities.



We expect the real estate sector to continue on an upward trajectory given (i) continued improvement in infrastructure, (ii) Government efforts in support of the sector in terms of incentives and initiatives such as the Land Sector Reforms and 15.0% reduction of corporate tax for select developers, and (iii) the expanding middle class. However, we expect the sector to continue facing development challenges due to tightened access to funding and thus developers have to come up with innovative ways of alternative funding such as REITs and structured product notes.