Sub-Saharan Africa (SSA) Eurobonds, & Cytonn Weekly #03/2019

Real Estate

I. **Residential Sector**

During the week, the Kenyan Government invited private developers to participate in the affordable housing initiative, by redeveloping government single dwelling estates to high-rise complexes. Developers are required to file for bids for Lot 1A, Lot 1B and Lot 1C, which refer to flagship projects, social housing projects and county projects, respectively, by 21st January 2019. Lot 1A, 1B and 1C are expected to consist of 167,640 units, which is 33.5% of the 500,000 units expected to be developed for the low and middle-income households in the next three-years. A total of 7,000-acres of public land has been reserved for the project, which will consist of studio, 1-bed, 2-bed and 3-bed apartments. Over the last year, the government has provided incentives and policy reviews all in support of the affordable housing initiative, expecting to push developers towards provision of more housing for the lower-middle and low-income section of the population. Some of the initiatives include: (i) establishment of the Kenya Mortgage Refinancing Company (KMRC) facilitating provision of mortgages to buyers at affordable rates, (ii) a 15.0% tax relief for first-time buyers up to a maximum of Kshs 108,000 p.a., and (iii) exemption of first time homebuyers from stamp duty tax. The affordable initiative structure involves the government partnership with private sector through Public-Private Partnerships (PPP's), where the government provides development land and the private sector offers financing and development capabilities. However, realizing this PPP structure has been difficult due to several challenges, which the government is addressing, among them being:

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,
iii. The extended time-frame of PPPs while private developers prefer to exit projects within 3-5 years, and,
iv. Bureaucracy and slow approval processes.

In our view, to achieve the affordable housing initiative, the government, in addition to addressing the PPP structure to be favourable for the private sector, needs to establish other financing methods such as tapping into capital markets, and provide incentives for the mortgage market to support both the developers and off-takers.

II. **Retail Sector**

During the week, Burger King, an American fast food restaurant chain, opened a new store at Shell Fuel Station on James Gichuru Road in Lavington, bringing its total number of outlets in Kenya to five. In addition, local retailer, Quickmart Supermarkets also announced plans to open a 10,000 SQFT 24-hour store at Westfield Mall in Lavington, fronting Gitanga Road, bringing its total retail stores to 10. The Lavington area has attracted various retailers over the last 2-years such as Java House and KFC, mainly due to the area serving as an affluent neighborhood hosting middle to highend income earners with high consumer purchasing power and thus investors are willing to pay higher rents for retail space in the area.

The increased retailers has thus improved the retail space performance in Lavington, making it the third best performing submarkets in Nairobi, with an average yield of 10.7% compared to a market average of 9.0% and average occupancy rates of 97.0% compared to a market average of 79.8% in 2018.

The table below shows the performance of the submarkets within Nairobi:

Summary of Nairobi's Retail Market Performance 2018

Location	**Rent Kshs/SQFT 2018**	**Occupancy Rate 2018**	**Rental Yield 2018**
Westlands	219.2	88.2%	12.2%
Karen	224.9	88.8%	11.0%
Kilimani/Lavington*	167.1	97.0%	10.7%
Ngong Road	175.4	88.8%	9.7%
Thika Road	177.3	75.5%	8.3%
Kiambu Road	182.8	69.5%	8.1%
Mombasa Road	161.5	72.4%	7.9%
Eastland's	153.3	64.8%	6.8%
Satellite Towns	142.1	73.7%	6.7%
Average	**178.2**	**79.8%**	**9.0%**

Kilimani includes Lavington and Kileleshwa

Source: Cytonn Research

We expect the continued entry of international retailers and expansion of local retailers within Lavington and the general Kilimani submarket supported by (i) increased disposable income due to an expanding middle class, and (ii) provision of higher quality amenities. We also expect increased activity from private developers attributed to attractive rental yields and occupancy rates at 9.9% and 84.5%, respectively.

III. **Hospitality Sector**

During the week, Kenya Airways and local airline Silverstone, announced plans to introduce daily direct flights from Nairobi to Seychelles, and from Nairobi to Lodwar, respectively. The move is in light of the increased air transport recorded in 2018, with several airlines recording increased frequencies in and out of the country, some of which include Ethiopian Airlines, which increased their weekly frequencies from Addis Ababa to Mombasa from 7 to 14 per week. In our view, the improving air transport, political stability and continued marketing of Kenya as an experience destination, will result in increased tourist arrivals, which according to Kenya National Bureau of Statistics (KNBS), recorded a 39.8% increase from 1.4 mn 2017 to 2.0 mn in 2018, and we expect the numbers to grow by 30.0% y/y to 2.6 mn in 2019. As a result, we expect continued demand for hospitality services, with serviced apartments expected to record relatively high occupancies of above 80.0% in 2019, according to our Cytonn 2019 Markets Outlook.

We expect increased activities in the real estate sector mainly residential, retail and hospitality themes, supported by (i) increased government push towards the affordable housing agenda (ii) entry of international retailers and expansion of the already existing

brands, and (iii) continued marketing of Kenya as an experience destination enhancing confidence in Kenya as a travel destination.
