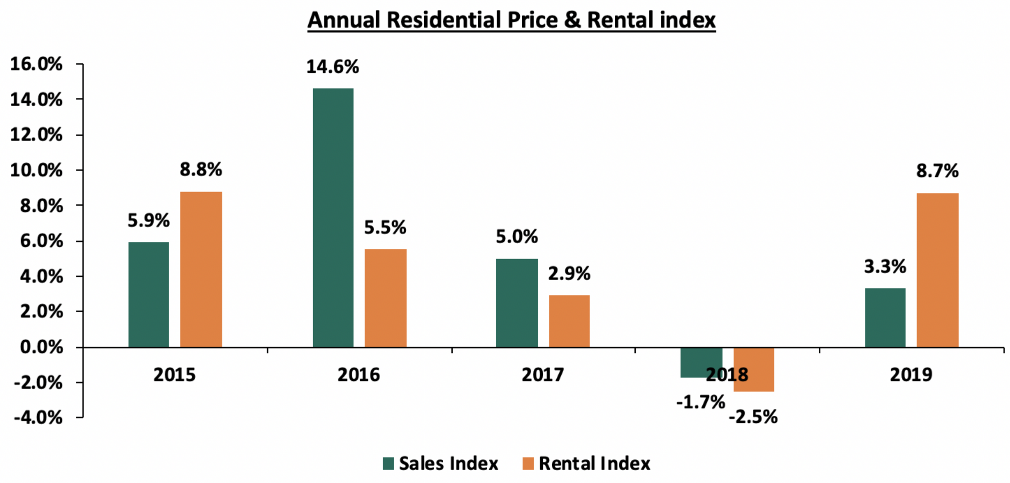
Kenya Listed Banks FY’2018 Report & Cytonn Weekly #16/2019

Real Estate

I. **Industry Reports**

During the week, Hass Consult released the Hass Q1 2019 Property Sales and Rental Index, which indicated that the Nairobi Metropolitan Area residential market registered an annual price appreciation of 3.3% as at Q1’2019, compared to a 1.7% decline recorded in Q1’2018; while q/q prices depreciated by 2.6%, compared to an appreciation of 2.4% in Q1’2018. Other key take-outs from the report were as follows:

- Detached units and apartments recorded an average y/y price appreciation of 5.1% and 1.7%, on average, and a q/q depreciation of 1.6% and 0.6%, respectively. We attribute the subdued apartments annual performance to increase in apartments supply resulting in competitive pressure on price growth,
- On quarterly performance, semi-detached units registered a price appreciation of 1.6%, compared to apartments and detached units which posted a depreciation of 0.6% and 4.4%, respectively,
- In the high-end market, Muthaiga, Nyari, and Karen posted the best q/q performance with average price appreciation of 4.4%, 1.8% and 1.6%, respectively, whereas Nyari Estate and Karen recorded the highest annual price appreciation at 12.5% and 8.3%, respectively, which we attribute to sustained demand from local wealthy investors. The report attributes the subdued high-end market performance to changing economic trends marked by foreign governments cutting down on international and aid-funded activities leading to vacation of properties by expatriates,
- In the upper mid-end market, Loresho, and Lavington recorded the best annual price appreciation at 9.9% and 7.8%, with the q/q appreciation coming in at 3.4% and 2.3%, respectively,
- Among Satellite Towns, Ngong, Athi River, and Kiambu were the best performers with annual price appreciation of 13.7%, 9.3% and 8.0%, respectively. Athi River and Limuru posted the highest q/q price appreciation at 3.1% and 2.4%, respectively,
- On the rental index, apartments posted the highest annual rental price increase at 19.8%, in comparison to semi-detached and detached with 11.1% and 2.7%, respectively. During the quarter, detached units posted a decline in rental prices by 1.0% in comparison to apartments and semi-detached which grew by 4.8% and 1.7%, respectively,



Source: Hass Consult

The report is in tandem with our Cytonn Q1'2019 Markets Review, findings that showed subdued performance in the high-end market with the upper mid-end market recording the best performance. According to the Cytonn Q1'2019 Market Review, the upper mid-end market recorded an average price appreciation of 4.2%, the highest in the overall residential market. We expect the mid-end and lower mid-end sectors to continue exhibiting better returns owing to growing middle class and demand for affordable housing.

In the Hass Land Index, the key take-outs were as follows:

- Land price growth in Nairobi's suburbs improved marginally, recording an annual growth of 1.4% and a q/q growth of 0.5%, whereas Satellite Towns recorded 1.5% annual growth and 0.2% q/q growth in Q1'2019, 0.3% points lower than land in Nairobi suburbs. The improved performance in Nairobi is attributed to increased demand for development land owing to presence of good infrastructure in comparison to most satellite towns and proximity to key amenities,
- Well-developed suburbs recorded price declines owing to correcting prices as they reach their highest potential price levels with areas like Kilimani and Spring Valley posting land annual price declines of 1.1% and 0.6%, respectively, due to a large inflow of new supply,
- Desirable areas with ample land supply recorded a slow price growth due to competitive pressure on land pricing. These include areas like Karen, Runda and Lavington, which posted average annual price growth of 3.2%, 2.2%, and 0.5%, respectively, and quarterly appreciation of 0.5%, 0.3% and negative 0.4%, in comparison to areas like Loresho and Ridgeways, which posted the highest annual price appreciation with 9.9% and 8.6%, and a q/q price appreciation of 3.7% and 2.2%, respectively, driven by demand from developers amidst reducing availability of land for development in the suburbs, and,
- In Satellite Towns, Mlolongo recorded the highest annual land price appreciation at 9.7%, while Syokimau registered the best quarterly appreciation at 3.2%. The two areas are boosted by a surge in demand by homebuyers owing to their close proximity to the JKIA and ease of transit due to the Nairobi Railway and Standard Gauge Railway (SGR).

The report is in tandem with our Q1'2019 Markets Review, according to which the sector recorded average price appreciation of 0.5% with Satellite Towns posting an average of 2.1% while commercial areas like Kilimani and Upperhill generally posted a decline of 3.5% on average owing to a price correction. However, we expect the land sector in satellite towns to continue recording improved performance going forward, fuelled by; (i) the continued demand for development land especially in satellite towns where it is more affordable and available in bulk, (ii) improving infrastructure such as the road network and sewer connections, and (iii) the digitalization of the Ministry of Lands which will enhance land administration.

Broll, a commercial real estate consultancy firm, released their Kenya Logistics Market Report, which tracks performance of the industrial sector in Nairobi. The key takes outs from the report were as follows:

- Price per acre for industrial serviced plots located in Nairobi's periphery, increased by an 11.1%, 3-year CAGR to Kshs 37.7 mn as at 2018 from Kshs 27.5 mn in 2015. The price was supported by demand for logistics space away from the relative congestion of Nairobi's industrial areas to satellite towns such as Kiambu and Machakos which also offer good infrastructure,
- As at December 2018, the total industrial space supply was at 1.2 mn SQM, a 9.1% increase from 1.1 mn SQM as at December 2017. The rise in industrial space was driven by increased activity in the logistics sector supported by continued foreign investment, as Kenya remains a regional hub and a key gateway to Eastern and Central Africa markets. New developments include the African Logistics Property at Tatu City and Viken Thirty Industrial Parks, while projects under development include Infinity Industrial Park, Nairobi Gate Industrial Park along the Eastern Bypass, and Tilisi Industrial Park in Rironi -Limuru,
- Embakasi, Athi River, and Syokimau accounted for 72.0% of the total industrial space supply, attributable to proximity to the Inland Container Depot, the JKIA, as well as the Standard Gauge Railway station which are key ports into East Africa,
- Occupancy rates in the industrial sector increased by 4.0% between 2017 and 2018 attributable to improving business environment and infrastructure, with Grade A warehouses registering the highest increase to 77% on average from 67% in 2017 owing to continued demand for high grade logistics space that continues to be in low supply. As per the report, Grade A warehouses account for the lowest supply at 5.0%, in comparison to Grade B and C at 75.3% and 19.7%, respectively. Generally, Grade A logistic space offer better services and structures such as wide roads, corporate offices, and other amenities such as better-quality loading facilities as well as high security, and,
- However, average rental rates remained flat with the average monthly rent per SQFT for Grade A, B and C spaces at Kshs 65, Kshs 37 and Kshs 21, respectively in line with the general real estate sector performance.

We expect the industrial and logistics sector to continue expanding owing to (i) improved business environment, which is bound to attract foreign investors, (ii) government's focus on growing the manufacturing sector under its Big 4 Agenda, and, (iii) continued improvement of infrastructure, for instance, with the expected dualling of Mombasa Road, the Western Bypass, and SGR Phase II.

II. **Residential**

During the week, the Housing Ministry kick started the Housing Fund Levy with a directive for employees and employers to remit by 9th May. The fund is structured similar to a pension scheme such that, employees will contribute a percentage of their income- 1.5% of their gross earnings each month, to a maximum of Kshs 5,000, and employers will match the amounts contributed. According to the Principal Secretary in the Ministry of Housing, Mr. Charles Mwaura, the fund will be structured and operated as follows:

i. The funds contributed by both the employer and the employee will go to a common pool at the National Housing Development Fund, which will be under the control of the National Housing Corporation,
ii. There will be two categories of access and use for the funds, a) individuals in the affordable housing bracket will use the funds to purchase houses through tenant purchase schemes, while b) individuals with a stronger financial muscle, will use the funds as deposits for mortgages,
iii. The contributors, who are registered through the Boma Yangu Portal, will then be pre-qualified and given an automated score as to whether they fall under the low cost housing category (Individuals earning up to Kshs 14,999), social housing category (Individuals earning between Kshs 15,000 and Kshs 49,999), or mortgage category (Individuals earning above Kshs 50,000),

iv. The private sector will then start building houses in line with the PPP agreements signed, and it is expected that 2,000 houses will be delivered in each county every year,
v. The registered contributors, will then book the houses, and as the 3.0% contributed is not sufficient to cater for the cost of the houses, they will start paying for the houses off plan,
vi. Each year, the state will then run a lottery to allocate the houses available among the contributors paying for the houses. This is to allow for equal distribution and prevent the contributors with a stronger financial muscle from acquiring all the houses available and subsequently renting them out.

However, following the directive, the announcement has faced huge opposition attracting a court injunction to halt taking effect until final decisions by the labour court are made. Currently, approximately 211,000 Kenyans are registered on the affordable housing portal and in our view; the fund will help potential homebuyers in the lower mid-end class to save towards home ownership, boosting offtake for the 500,000 units to be delivered by the government. However, the key challenge is acceptance by Kenyans largely due to information gaps about the Housing Fund structure and lack of transparency by the government coupled by current high cost of living with an ongoing drought. The government should harmonize the process by sensitizing Kenyans and provide a clear and reliable framework of how the fund will benefit contributors.

We expect the real estate sector to continue recording a modest performance in sectors such as residential especially with the ongoing drought season and declined levels of expats residing in the country. However, niche markets and concepts should be able to do well, and we expect the logistics sector to continue on a positive performance owing to focus on industrializing the country, improved business environment especially with regards to tax rebates in special economic zones, and improved infrastructure.