Investing in Unit Trust Funds, & Cytonn Weekly #20/2019

Real Estate

i. **Residential Sector**

During the week, the Ministry of Housing, under the Civil Servants Housing Scheme Fund (CSHSF), proposed:

a. The reduction of mortgage deposits by public servants from 10.0% to 5.0% of the property value, and,
b. An allowance to pay mortgage loans up to 5-years after the retirement age of 60-years.

The Civil Servants Housing Scheme Fund (CSHSF) was established in 2004, with the aim of providing housing loan facilities to civil servants for the purpose of either purchasing or constructing a residential house and developing housing units for sale or rental by civil servants. Since inception, the scheme has facilitated more than 3,000 civil servants to access housing, through housing finance loans or purchase of houses constructed through the scheme. The scheme has partnered with two mortgage finance institutions, Home and Loan of KCB and Housing Finance with the aim of granting housing loans to civil servants. One of the major challenges that has faced the scheme is the high interest rates and short-term repayment periods, which have put off potential home-buyers. The incentives tabled before parliament aim at making home loans more accessible to low income state workers. This follows the continued government focus on enhancing home ownership in Kenya, through the affordable housing initiative under the Kenyan Government's Big 4 Agenda. Some of the other government initiatives in line with the same include;

i. The formation of the Kenya Mortgage Refinancing Company (KMRC) whose main function is enhancing mortgage affordability by enabling long-term loans; see Cytonn's KMRC Note for more details on the same, and,
ii. The establishment of the National Housing Development Fund (NHDF), which includes a 1.5% housing levy on employee's basic salaries towards a fund with the contribution expected to act as a saving for employees.

The above Kenyan Government initiatives are aimed at meeting the huge existing housing deficit, which stands at 2.0 mn units and growing by 200,000 units p.a., according to National Housing Corporation, Kenya. This has been fueled by:

i. Inaccessibility and unaffordability of off-take financing/mortgages in Kenya mainly due to low income levels that cannot service a mortgage, as according to data from the Kenya National Bureau of Statistics, 74.5% of employees in the formal sector earn less than Kshs 50,000 per month, in addition to 83.4% of total employment being in the informal sector with relatively unpredictable incomes and limited job security and thus they are unable to afford a house,
ii. Escalating property prices attributed to increased demand for housing and limited supply,
iii. Inadequate and high costs of funds, evidenced by reduced credit advancement to the private

sector due to tightened underwriting standards, in addition to the high actual cost of credit averaging at 18.0%, which then raises the cost of development, thus making development expensive, and,

iv. Inadequate infrastructural development.

In our view, if successfully endorsed, the incentives will enhance housing uptake, through encouraging more public servants to take up housing units, given the reduced burden of the deposit amount and the increased period of repayment, which means the borrower is able to pay smaller installments thus making the mortgage more affordable.

The UN-Habitat, a United Nations agency, announced that it had finalized on plans to build approximately 8,000 units in Mavoko Sub-County, in support of the affordable housing project under the Big 4 Agenda. The project, which will sit on a 55-acre parcel of land, will be launched in five-months' time and is aimed at resettling slum dwellers from the Nairobi Metropolitan Area. Other project details among them unit sizes are yet to be disclosed, but social housing units within the project are set to cost between Kshs 0.5 mn and 0.7 mn. Delivering of the units will be done at the lowest possible price that will be achieved through the use of various building technologies while maintaining high quality. The project is a step towards the achievement of the affordable housing initiative and adds to the count of other affordable housing projects set to be constructed in Mavoko area such as the 30,000 housing units project by National Social Security Fund (NSSF). Another project undertaken by the UN agency under their slum prevention programme is the relocation of 1,200 households from Soweto East to a decanting site in Lang'ata in 2010. Some of the key challenges that have continued to cripple the implementation of such projects include;

i. Resistance where families refuse to be relocated because they do not want to pay higher rent than they pay in areas such as Kibera and fear of projects failure to deliver promised units,
ii. Unit allocation issues where some of the households are not included in the lists of beneficiaries thus fail to acquire units,
iii. Purchase of the units by high income earners and letting at higher rental charges hence locking out the target tenants, and
iv. Lack of proper analysis and consideration of the residents' economic activities as well as the needs of the vulnerable (physically challenged) resulting in resistance.

For such a project to be successful, we recommend that adoption of participatory processes in slum upgrading so that the community can embrace and support it, in addition to implementation of a strategic unit allocation plan to ensure targeted beneficiaries acquire the units. For the Mavoko housing project, we expect the above factors will be considered and hence provide the much-needed affordable housing units for the low and middle-income earners, in addition to encouraging more organizations and private developers to take part in the provision of affordable housing.

During the week, Housing Finance handed over 248 housing units to owners under its Shika Nyumba Campaign. The fully sold out development, called Richland Pointe is located along Kamiti Road and is a joint venture with Richland Development Limited, a local real estate consultant firm. The houses valued at Kshs 1.9 bn, comprise of 2-bedroom units of 95 SQM and 3-bedroom apartments of 125 SQM, selling at approximately Kshs 82,737 per SQM, for Kshs 8.5 mn and Kshs 9.5 mn, respectively. The project, which started construction in 2016, is an example of a successful joint venture arrangement, where Richland Dam Estate Limited provided land where the project sits on, whilst Housing Finance provided equity equivalent to the land. The benefits of such a partnership include;

i. **An increased capital base** as the partners make contributions (land and/or equity) into the project,
ii. **Development expertise** as the developer in a joint venture provides development expertise in terms of concept development, design, project management and oversees the project to completion,

iii. **Access to market distribution channels** especially while partnering with a reputable brand as it ensures the real estate product reaches its suited market and thus faster exit, and,
iv. **Shared risks and gains** as a partnership enables spreading of economic and other market risks that might result from undertaking any worthy real estate investment, and that would otherwise be borne alone.

The Richland Pointe project signifies the continued involvement of strategic partners in the provision of housing in Kenya, fuelled by;

i. Huge demand for housing, particularly decent, affordable housing for the middle-income segment of the market,
ii. Relatively high returns attracting developers, and,
iii. Availability of development land in the satellite towns such as Ruiru in Kiambu County.

We therefore expect the above factors to continue resulting in increased development activities in the residential sector, with the market recording partnerships among both the public and private sector players.

Other highlights during the week;

i. Vitafoam Products, a factory-cum retailer, opened a showroom at the Two Rivers Mall, along Kiambu Road. The company, which makes mattresses and cushions, has taken up 2,200 square feet on the first floor of the mall. This will mark the company’s third showroom in Kenya, with others being situated along Mombasa Road and Muthithi Road in Westlands. The expansion of the retailer, signifies the continued expansion of local retailers, resulting in a growing demand for retail space. This is evidenced by growing occupancy rates in some submarkets such as Kiambu Road, which recorded 0.3% points increase from 69.5% in 2018 to 69.8% in Q1’2019.

We expect the real estate sector to continue recording increased activities especially in the residential sector, fueled by the continued focus on provision of affordable housing for the middle-income segment of the market, by both the government and other strategic partners such as United Nations agency, UN- Habitat.