# Cytonn H1'2019 Markets Review

## Real Estate

In H1'2019, the real estate sector continued to record increased activity supported by; (i) the positioning of Nairobi as a regional hub, (ii) continued National Government support for the affordable housing initiative, (ii) expansion by multinational corporations and retailers into the country, and (iii) the improving macroeconomic environment, with the country's GDP growing by 6.3% in 2018, 1.4% points higher than the 4.9% recorded in 2017. The key challenges that continue to face developers and end users include (i) oversupply the commercial office and retail sectors with a surplus of 5.2mn SQFT and 2.0mn SQFT, respectively, as at 2018, and (ii) lack of access to financing and high financing cost for both developers and off-takers following the capping of interest rates.

In this report, we have reviewed notable activities and the performance of the residential, commercial, hospitality, land, infrastructure, and listed real estate sectors during the quarter.

I. **Residential Sector**

In H1'2019, we continued to witness an increase in investor interest in the residential sector in Kenya. The most notable projects launched during the period were; (i) the United Nations' Habitat Housing Cooperative Society Limited 8,888-units joint venture project with Singapore-based consortium Afra Holdings, to be located in Mavoko, (ii) Actis Garden City Apartments along Thika road, (iii) Cytonn's Applewood in Karen, and (iv) Deltar's project to be located in Batu Batu Gardens, Parklands.

On the affordable housing front, major highlights during the period were:

i. The 2019/2020 National Budget allocation towards affordable housing initiative was raised by 61.5% to Kshs 10.5 bn, from Kshs 6.5 bn in the previous 2018/2019 budget, indicating continued government support towards the actualization of the affordable housing initiative,
ii. The National Treasury launched the Kenya Mortgage Refinancing Company (KMRC) after a successful mobilization of capital from key shareholders and international financial institutions. For more analysis, read our KMRC Topical,
iii. Leading mortgage financier in Kenya, Housing Finance (HF) announced plans to reduce its current average mortgage size by 50.0% in a bid to tap into the growing demand for home loans from the lower mid-income class,
iv. The Government of Kenya announced the relaxation of affordable housing regulations to include high income-earners of Kshs 100,000 and above, and
v. The Kenyan Government launched the bomayangu.go.ke portal to allow citizens to register and apply for affordable housing units online.

**Market Performance**

Overall, apartments performed better in H1'2019 with average total returns of 5.5%, 5.5%, and 6.3% for the upper mid-end, lower mid-end suburbs, and satellite towns, respectively, in comparison to detached units at 3.8%, 4.5%, and 4.1%, for high-end, upper mid-end, and satellite towns, respectively. Apartments also recorded higher annual uptake of 22.4%, compared to 19.7% for detached units. This is as apartments have a wider market due to their relative affordability to homebuyers, which also sustains their price growth.

## A. **Detached Units**

### High-End

The high-end market recorded a marginal price appreciation of 0.1%, from an average of Kshs 199,625 per SQM in H1’2018 to Kshs 201,275 per SQM in H1’2019, with select markets namely, Rosslyn and Kitisuru, recording depreciation of 2.6% and 0.4%, respectively. This is mainly as a result of the decline in asking prices, as areas like Kitisuru and Rosslyn reach their price ceilings, amidst a tough financial environment, which has led to a decline in effective demand.

(All Returns Are Annualized)

*(All Values in Kshs Unless Stated Otherwise)*

**Detached Units Performance H1'2019 – Top 5: High-End**

| Area | Price per SQM H1'2019 | Rent per SQM H1'2019 | Annual Uptake H1'2019 | Occupancy H1'2019 | Rental Yield H1'2019 | Annual Price Appreciation H1'2019 | Total Returns H1'2019 |
|---|---|---|---|---|---|---|---|
| Runda | 234,697 | 888 | 17.8% | 83.8% | 4.0% | 1.8% | 5.8% |
| Karen | 205,087 | 659 | 20.0% | 76.6% | 3.0% | 1.8% | 4.8% |
| Kitisuru | 223,310 | 903 | 19.4% | 83.3% | 3.7% | (0.4%) | 3.3% |
| Lower Kabete | 165,043 | 467 | 16.3% | 89.5% | 3.3% | 0.0% | 3.3% |
| Rosslyn | 178,237 | 757 | 19.1% | 84.3% | 4.3% | (2.6%) | 1.7% |
| **Average** | **201,275** | **735** | **18.5%** | **83.5%** | **3.7%** | **0.1%** | **3.8%** |

*• Karen and Runda recorded the highest price appreciation in the high-end market. The two areas continue to exhibit relatively high demand from the high-income earning class owing to the presence of amenities such as shopping malls and relatively good infrastructure such as the Northern and Southern Bypasses, which enhance their accessibility*
*• Rosslyn recorded the lowest returns to investors mainly attributable to the decline in asking prices, as developers seek to attract clients due to competition from other surrounding neighborhoods such as Gigiri, Runda, and Muthaiga*

*Source: Cytonn Research 2019*

### Upper Mid-End

The upper mid-end segment recorded the highest total annual uptake and returns in the detached units sector at 20.3% and 4.5%, respectively. This is due to areas such as Runda Mumwe and Loresho, which posted the highest average returns in the upper mid-market of 6.2% and 5.8%, respectively, attributable to their proximity to neighborhoods such as Runda for Runda Mumwe, and Lower Kabete and Kitisuru for Loresho, which make them appealing to the mid-income earners seeking exclusivity but in relatively affordable areas.

*All Values in Kshs Unless Stated Otherwise)*

**Detached Units Performance H1'2019 – Top 5: Upper Mid-End**

| Area | Price per SQM H1'2019 | Rent per SQM H1'2019 | Annual Uptake H1'2019 | Occupancy H1’ 2019 | Rental Yield H1'2019 | Annual Price Appreciation H1'2019 | Total Returns H1’2019 |
|---|---|---|---|---|---|---|---|
| Loresho | 146,540 | 575 | 17.5% | 94.6% | 4.5% | 1.7% | 6.2% |
| Runda Mumwe | 158,932 | 662 | 26.1% | 83.6% | 4.3% | 1.5% | 5.8% |
| South C | 120,928 | 494 | 23.8% | 92.5% | 4.6% | (0.7%) | 3.8% |
| Redhill | 105,218 | 367 | 21.1% | 77.5% | 3.3% | 0.3% | 3.6% |
| Langata | 142,183 | 556 | 13.0% | 97.2% | 4.7% | (1.7%) | 3.0% |
| **Average** | **134,760** | **531** | **20.3%** | **89.1%** | **4.3%** | **0.2%** | **4.5%** |

*• Runda Mumwe and Loresho posted the highest average returns of 6.2% and 5.8%, respectively. This is attributable to their proximity to neighborhoods such as Runda for Runda Mumwe, and Lower Kabete and Kitisuru for Loresho, which makes them appealing to the mid-income earners seeking exclusivity but in relatively affordable areas*
*• Langáta posted the lowest returns owing to declining prices attributable to increasing relaxation of regulations and thus the proliferation of high-rise developments making the area lose its appeal to low-rise home buyers*

*Source: Cytonn Research 2019*

### Satellite Towns

Ruiru and Athi River Towns were the best performing satellite towns in H1'2019 with average returns to investors of 6.0% and 5.0%, respectively. This is attributable to the presence of good infrastructure such as the Eastern Bypass and Thika Superhighway for Ruiru, with relatively low land prices *(see below our land sector performance summary)* for development enabling their affordability to the majority of home seekers.

*(All Values in Kshs Unless Stated Otherwise)*

**Detached Units Performance H1'2019 – Top 5: Satellite Towns**

| Area | Price per SQM H1'2019 | Rent per SQM H1'2019 | Annual Uptake H1'2019 | Occupancy H1'2019 | Rental Yield H1'2019 | Annual Price Appreciation H1'2019 | Total Returns H1'2019 |
|---|---|---|---|---|---|---|---|
| Ruiru | 99,064 | 353 | 17.1% | 79.6% | 5.1% | 0.9% | 6.0% |
| Athi River | 92,054 | 406 | 19.3% | 79.6% | 4.5% | 0.6% | 5.0% |
| Ngong | 64,843 | 238 | 19.4% | 72.8% | 3.2% | 1.6% | 4.8% |
| Kitengela | 73,919 | 446 | 17.7% | 66.1% | 3.1% | 1.2% | 4.3% |
| Juja | 73,182 | 260 | 16.6% | 61.9% | 2.7% | (2.1%) | 0.7% |
| **Average** | **80,612** | **341** | **18.0%** | **72.0%** | **3.7%** | **0.4%** | **4.1%** |

*• Ruiru and Athi River Towns were the best performing satellite towns during the period with average returns to investors of 6.0% and 5.0%, respectively. This is attributable to the presence of good infrastructure such as the Eastern bypass and Thika Superhighway for Ruiru, and the Eastern Bypass for Athi River. Upcoming master-planned cities, such as Tatu City and Konza City also create speculative demand, thus driving prices up*
*• Juja posted a notable decline in price, with a price depreciation rate of 2.1%, attributable to softening demand due to competition from other satellite towns such as Ruiru and Ruaka which are closer to Nairobi's key commercial nodes*

*Source: Cytonn Research 2019*

B. **Apartments**

### Upper Mid-End

The upper mid-end sector posted relatively high annual uptake of 25.1% on average, owing to demand from real estate investors seeking to tap into the upper mid-end rental sector to support demand from long-stay foreigners seeking highly accessible areas with plenty of amenities. This is evidenced by the growing trend of serviced and furnished apartments in areas like Kilimani and Riverside, which attract relatively high rental rates.

*(All Values in Kshs Unless Stated Otherwise)*

**Apartments Performance H1'2019 – Top 5: Upper Mid-End**

| Area | Price per SQM H1'2019 | Rent per SQM H1'2019 | Annual Uptake H1'2019 | Occupancy H1'2019 | Annual Price Appreciation H1'2019 | Rental Yield H1'2019 | Total Returns H1'2019 |
|---|---|---|---|---|---|---|---|
| Riverside | 135,813 | 737 | 22.9% | 76.2% | 0.9% | 5.1% | 5.9% |
| Loresho | 113,122 | 479 | 20.9% | 95.4% | 1.4% | 4.3% | 5.7% |
| Kilimani | 121,845 | 852 | 30.4% | 76.8% | 0.0% | 5.6% | 5.5% |
| Westlands | 145,744 | 665 | 28.0% | 80.4% | 0.2% | 5.3% | 5.4% |
| Parklands | 123,146 | 744 | 23.3% | 85.7% | -0.3% | 5.1% | 4.8% |

**Apartments Performance H1'2019 – Top 5: Upper Mid-End**

| Area | Price per SQM H1'2019 | Rent per SQM H1'2019 | Annual Uptake H1'2019 | Occupancy H1'2019 | Annual Price Appreciation H1'2019 | Rental Yield H1'2019 | Total Returns H1’2019 |
|---|---|---|---|---|---|---|---|
| **Average** | **127,934** | **695** | **25.1%** | **82.9%** | **0.4%** | **5.0%** | **5.5%** |

*• Riverside recorded the best average returns to investors in the upper mid-end sector with 5.9%, compared to the upper mid-market average of 5.5%, due to the area’s proximity to key nodes, namely Westlands, CBD and Lavington, with further support by demand for luxury apartments especially from foreign nationals*

*Source: Cytonn Research 2019*

### Lower Mid End

The lower mid-end suburbs posted average returns of 5.5% with a positive marginal price appreciation rate of 0.6%. The performance has been sustained by demand for affordable units particularly from the constant urbanization and the growing middle class.

*All Values in Kshs Unless Stated Otherwise)*

**Apartments Performance H1'2019 – Top 5: Lower Mid-End**

| Row Labels | Price per SQM H1'2019 | Rent per SQM H1'2019 | Annual Uptake H1'2019 | Occupancy H1'2019 | Annual Price Appreciation H1'2019 | Rental Yield H1'2019 | Total Returns H1'2019 |
|---|---|---|---|---|---|---|---|
| Lang’ata | 97,012 | 544 | 15.0% | 83.4% | 1.3% | 5.5% | 6.8% |
| South C | 99,059 | 555 | 20.6% | 88.1% | 0.8% | 4.8% | 5.7% |
| Imara Daima | 63,203 | 354 | 22.3% | 90.0% | (0.2%) | 5.6% | 5.4% |
| Dagoretti | 89,807 | 627 | 16.5% | 88.7% | 0.0% | 5.1% | 5.1% |
| Ngong Road | 99,800 | 508 | 20.7% | 87.2% | 0.9% | 3.8% | 4.7% |
| **Average** | **89,776** | **518** | **19.0%** | **87.5%** | **0.6%** | **5.0%** | **5.5%** |

*• Langáta had the highest total returns in the lower mid-end apartment category, at 6.8% owing to its appeal among the young working population due to its proximity to key commercial nodes such as Mombasa Road, the CBD, Kilimani as well as Upperhill*

*Source: Cytonn Research 2019*

### Satellite Towns

Apartments in satellite towns were the best performing category with average total returns of 6.3% (a price appreciation of 1.5% and a rental yield of 4.8%), attributable to relatively low land prices, with majority of the towns currently experiencing major infrastructural improvements enabling developers to develop and sell homes at relatively affordable prices, thus boosting uptake.

*(All Values in Kshs Unless Stated Otherwise)*

**Apartments Performance H1'2019 – Top 5: Satellite Towns**

| Row Labels | Price per SQM H1'2019 | Rent per SQM H1'2019 | Annual Uptake H1'2019 | Occupancy H1'2019 | Annual Price Appreciation H1'2019 | Rental Yield H1'2019 | Total Returns H1’2019 |
|---|---|---|---|---|---|---|---|
| Ruaka | 98,098 | 454 | 20.6% | 91.9% | 2.4% | 5.6% | 8.0% |
| Thindigua | 99,270 | 499 | 21.1% | 88.4% | 1.8% | 4.2% | 6.1% |
| Rongai | 63,064 | 350 | 19.1% | 68.5% | 1.1% | 4.6% | 5.7% |
| Kitengela | 60,124 | 341 | 16.5% | 76.3% | 2.2% | 4.5% | 6.6% |
| Syokimau | 59,242 | 289 | 15.6% | 88.2% | 0.0% | 4.9% | 4.9% |
| **Average** | **75,960** | **386** | **18.6%** | **82.6%** | **1.5%** | **4.8%** | **6.3%** |

*• Ruaka and Thindigua were the best performing nodes recording an average total returns to investors of 8.0% and 6.1% attributable to increase in infrastructure improvements such as the incoming Western Bypass and Westlands Link Road for Ruaka which is a boost for speculative demand, and proximity to shopping amenities such as Two Rivers, Ridgeways Shopping Mall and Rosslyn Riviera. Both areas also attract expatriates demand due to their proximity to foreign organizations such as the UN and foreign embassies*

*Source: Cytonn Research 2019*

***Overall, we expect the residential sector to continue experiencing minimal demand in the high-end and upper mid-end sectors mainly driven by incoming expatriates. However, the lower mid-end sectors will continue to exhibit fast growing demand from the majority of Kenyans seeking to buy affordable homes amidst a tough financial environment.***

## II. Commercial Sector

### A. Commercial Office

In H1'2019, the commercial office sector recorded a decline in performance recording 0.3% and 2.3% points decline in average rental yields and occupancy rates, to 7.8% and 81.0% in H1'2019, from 8.1% and 83.3%, respectively in FY'2018. Asking rents decreased by 5.3% to an average of Kshs 96.6 per SQFT in H1'2019, from Kshs 102 per SQFT in FY'2018, while asking prices increased marginally by 0.5% to Kshs 12,637 in H1'2019 from Kshs 12,573 in FY'2018. The negative performance was largely attributed to:

i. A surplus of office space that stood at 5.2 mn SQFT as at 2018, which has created a bargaining chip for tenants forcing developers to reduce or maintain prices and rents in order to remain competitive and attract occupants to their office spaces, and,
ii. Slow growth in private sector credit following the capping of interest rates on loans offered by banks creating a tough operating environment for small and medium-sized enterprises (SMEs), leading to layoffs, downsizing or business closures.

The table below highlights the performance of the commercial office sector in Nairobi over time:

*All values in Kshs unless stated otherwise*

**Summary of Commercial Office Returns in Nairobi Over Time**

| Year | Q1'2018 | H1'2018 | Q3'2018 | FY'2018 | Q1'2019 | H1'2019 | Δ Y/Y Q4'2018/H1'2019 |
|---|---|---|---|---|---|---|---|
| Occupancy (%) | 80.5% | 84.6% | 87.3% | 83.3% | 82.4% | **81.0%** | **(2.3%) points** |
| Asking Rents (Kshs/SQFT) | 98.0 | 102.0 | 102.0 | 102.0 | 100.3 | **96.6** | **(5.3%)** |
| Average Prices (Kshs/SQFT) | 12,718 | 12,527 | 12,202 | 12,573 | 12,574 | **12,637** | **0.5%** |
| Average Rental Yields (%) | 9.2% | 9.3% | 9.5% | 8.1% | 8.0% | **7.8%** | **(0.3%) points** |

*• Rental yields and occupancy rates declined by 0.3% and 2.3% points, respectively to 7.8% and 81.0% in H1'2019 from 8.1% and 83.3% in FY'2018 attributed to the surplus of 5.2 mn SQFT office space as at 2018*
*• Rental rates dropped by 5.3% to Kshs 96.6/SQFT/Month from Kshs 102/SQFT/Month as developers reduce rents in order to remain competitive and attract tenants*

*Source: Cytonn Research 2019*

In terms of submarket analysis, Gigiri, Kilimani and Karen were the best performing nodes in H1'2019, recording rental yields of 9.2%, 9.2%, and 9.0%, respectively, attributed to increased demand by businesses and multinational companies, as a result of their superior locations, offering quality Grade A offices, which enable them to charge a premium on rental charges.

Thika Road and Mombasa Road continue to record the lowest returns with average rental yields of 5.9% and 5.4% in H1'2019, respectively, which represents a 0.8% and 0.4% points decline from 6.7% and 5.8%, in FY'2018, respectively. This is attributed to low-quality office space and traffic snarl-ups that have made the nodes generally unattractive to firms.

The most improved nodes were Karen and Parklands which recorded rental yields of 9.0%and 8.9%, respectively, driven by increased occupancy rates of 2.6% each, as a result of its serene working environment away from the key commercial nodes such as the Nairobi CBD, thus attracting high-end clientele and premium rental rates.

The table below highlights Nairobi Commercial Office Submarket Performance in H1'2019:

*All values in Kshs unless stated otherwise*

**Nairobi Commercial Office Submarket Performance 2018- H1'2019**

| Location/Node | Price Kshs/ SQFT H1'2019 | Rent Kshs/SQFT H1'2019 | Occupancy H1'2019(%) | Rental Yield (%) H1'2019 | Price Kshs/ SQFT FY 2018 | Rent Kshs/SQFT FY 2018 | Occupancy FY 2018(%) | Rental Yield (%) FY 2018 | Δ in Rent | Δ in Occupancy (% points) | Δ in Rental Yields (% points) |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Gigiri | 13,833 | 116.0 | 77.0% | 9.2% | 13,833 | 141.0 | 88.3% | 10.5% | (17.7%) | (11.3%) | **(1.3%)** |
| Kilimani | 12,680 | 91.0 | 82.9% | 9.2% | 13,525 | 98.9 | 88.3% | 8.0% | (8.0%) | (5.3%) | **1.1%** |
| Karen | 13,665 | 112.2 | 91.1% | 9.0% | 13,666 | 118.0 | 88.6% | 9.2% | (4.9%) | 2.6% | **(0.3%)** |
| Parklands | 12,369 | 100.9 | 88.6% | 8.9% | 12,494 | 102.1 | 86.0% | 8.4% | (1.2%) | 2.6% | **0.5%** |
| Westlands | 12,334 | 106.9 | 79.5% | 8.4% | 12,050 | 109.7 | 82.1% | 9.0% | (2.6%) | (2.6%) | **(0.6%)** |
| Nairobi CBD | 12,425 | 88.8 | 88.4% | 7.6% | 10,875 | 88.8 | 88.3% | 7.6% | 0.0% | 0.1% | **0.0%** |
| UpperHill | 12,431 | 97.6 | 82.9% | 7.3% | 12,560 | 99.8 | 80.7% | 7.9% | (2.2%) | 2.2% | **(0.6%)** |
| Thika Road | 12,600 | 83.3 | 74.7% | 5.8% | 12,517 | 86.3 | 81.5% | 6.7% | (3.5%) | (6.8%) | **(0.9%)** |
| Msa Road | 11,400 | 72.8 | 64.0% | 5.3% | 11,400 | 78.8 | 65.6% | 5.8% | (7.6%) | (1.6%) | **(0.5%)** |
| **Average** | **12,637** | **96.6** | **81.0%** | **7.8%** | **12,547** | **102.6** | **83.3%** | **8.1%** | **(5.3%)** | **(2.3%)** | **(0.3%)** |

**Gigiri area covers Gigiri and Limuru Road*
*• Nairobi Metropolitan area recorded a 0.2% points decrease in rental yields to 7.8% in H1'2019 from 8.1% in 2018, attributable to reduced rental rates driven by a 2.3% decrease in office occupancy rates due to an oversupply of office space and a slowdown in private sector credit growth*
*• Gigiri, Kilimani and Karen were the best performing nodes within the Nairobi Metropolitan Area recording average rental yields of 9.4%, 9.2% and 9.0% respectively, and occupancy rates of 77.0%, 82.9% and 91.1%, respectively. The high returns are attributed to prime rental charges as a result of the high-quality office spaces in these areas*
*• Thika Road and Mombasa Road were the worst performing markets recording average rental yields of 5.9% and 5.4%, respectively, due to poor quality offices and also affected by high traffic snarl-ups that have made them generally unattractive to firms*

*Source: Cytonn Research 2019*

The key highlights in the commercial office sector in H1’2019 include; (i) launch of corporate serviced offices at Sanlam Tower, Waiyaki Way, Westlands by Workable Nairobi, a commercial serviced office provider, (ii) the opening of Park Medical Centre along 3rd Parklands Avenue in Parklands, and (iii) Opening of business offices by multinational corporations: Cigna, a global health service company, MAC Mobile, a FMCG technology solutions company, and Mauritius Commercial Bank (MCB) Group at the UNON Complex in Gigiri, 3 Mzima Springs Road in Kileleshwa and Pramukh towers in Westlands, respectively.

***We retain a negative outlook on the performance of the commercial office sector attributable to an oversupply of 5.2mn SQFT of office space thereby reducing occupancy rates translating to decline in rental yields. Pockets of value in the sector are in differentiated concepts such as serviced offices and offices in mixed-use developments (MUDs) that attract yields of 13.4% and 8.2%, respectively.***

B. **Retail**

The retail sector performance softened, recording a 0.8% points decline in rental yield to 8.2% in H1’ 2019 from 9.0% in FY’ 2018. This is due to the retail space surplus, recording an oversupply of 2.0 mn SQFT, which saw average occupancies drop by 3.5% points from 79.1% in FY’ 2018 to 75.6% in H1’ 2019 and average rents declined by 4.9% to Kshs 170.0/ SQFT/month from Kshs 178.2/ SQFT/month in FY’2018. The decline in rent is attributable to property managers’ adoption of innovative pricing models such as reducing rental charges and rent-free grace periods of up to 6 months in order to attract tenants.

The performance of the retail sector in Nairobi over time is as shown below;

*All values in Kshs unless stated otherwise*

**Retail Sector Performance H1' 2019**

| Item | H1' 2018 | FY' 2018 | H1' 2019 | Δ Y/Y | Δ H1'2019 |
|---|---|---|---|---|---|
| Average Asking Rents (Kshs/SQFT) | 190.4 | 178.2 | 170.0 | (10.7%) | **(4.9%)** |
| Average Occupancy (%) | 82.7% | 79.1% | 75.6% | (7.4%) | **(3.5%) points** |
| Average Rental Yields | 9.7% | 9.0% | 8.2% | (1.8%) | **(0.8%) points** |

*• The retail sector performance softened, recording an average rental yield of 8.2%, a 0.8%-point decline from 9.0% in FY' 2018. Occupancy rates as well declined by 3.5% points, while the rental charges decreased by 4.9% over the first half of the year.*
*• The decline in performance is attributable to the oversupply of mall space in Nairobi, currently at 2.0mn SQFT, with the opening of malls such as Waterfront, The Well and Coholo*

*Source: Cytonn Research 2019*

In terms of submarket analysis in Nairobi, Westlands and Kilimani were the best performing retail nodes with average rental yields of 12.0% and 10.5% respectively, as the areas are affluent neighborhoods hosting middle – high-end income earners with high consumer purchasing power and thus tenants are willing to pay higher rents for retail space in the area. Mombasa Road and Satellite towns were the worst performing nodes recording a rental yield of 6.3% and 5.7%, respectively. The poor performance is attributable to low rental charges as a result of traffic congestion along Mombasa road and competition from informal retail space in Satellite towns.

Karen recorded the largest declines in the rental yield in H1' 2019 of 2.2%, attributable to a 17.0% decline in average occupancy rates as a result of the opening of Waterfront and The Well malls.

*All values in Kshs unless stated otherwise*

**Summary of Nairobi's Retail Market Performance H1' 2019**

| Location | Rent Kshs/SQFT H1' 2019 | Occupancy H1' 2019 | Rental Yield H1' 2019 | Rent Kshs/SQFT FY' 2018 | Occupancy FY' 2018 | Rental Yield FY' 2018 | H1' 2019 Δ in Rental Rates | H1' 2019 Δ in Occupancy (% points) | H1' 2019 Δ in Rental Yield (% points) |
|---|---|---|---|---|---|---|---|---|---|
| Westlands | 209 | 89.0% | 12.0% | 219 | 82.2% | 12.2% | (4.7%) | 6.8% | (0.2%) |
| Kilimani | 173 | 91.4% | 10.5% | 167 | 97.0% | 10.7% | 3.6% | (5.6%) | (0.2%) |
| Ngong Road | 171 | 87.5% | 9.3% | 175 | 88.8% | 9.7% | (2.3%) | (1.3%) | (0.4%) |
| Karen | 219 | 71.8% | 8.8% | 225 | 88.8% | 11.0% | (2.5%) | (17.0%) | (2.2%) |
| Eastlands | 145 | 74.2% | 7.5% | 153 | 64.8% | 6.8% | (5.6%) | 9.4% | 0.7% |
| Kiambu Road | 169 | 65.3% | 7.3% | 183 | 69.5% | 8.1% | (7.6%) | (4.2%) | (0.8%) |
| Thika road | 168 | 66.5% | 6.8% | 177 | 75.0% | 8.3% | (5.4%) | (8.5%) | (1.5%) |
| Mombasa road | 144 | 65.5% | 6.3% | 162 | 72.4% | 7.9% | (10.7%) | (6.9%) | (1.6%) |
| Satellite Towns | 129 | 69.2% | 5.7% | 142 | 73.7% | 6.7% | (9.2%) | (4.5%) | (1.0%) |
| Average | 170 | 75.6% | 8.2% | 178 | 79.1% | 9.0% | (4.9%) | (3.5%) | (0.8%) |

**Summary of Nairobi’s Retail Market Performance H1’ 2019**

| Location | Rent Kshs/SQFT H1’ 2019 | Occupancy H1’ 2019 | Rental Yield H1’ 2019 | Rent Kshs/SQFT FY’ 2018 | Occupancy FY’ 2018 | Rental Yield FY’ 2018 | H1’ 2019 Δ in Rental Rates | H1’ 2019 Δ in Occupancy (% points) | H1’ 2019 Δ in Rental Yield (% points) |
|---|---|---|---|---|---|---|---|---|---|

*• Performance softened, with yields declining by 0.8% points in H1’ 2019, as a result of an oversupply of retail space, currently at 2.0mn SQFT leading to a 3.5% points decline in occupancy levels and a 4.9 % decline in rental charges in H1’ 2019,*
*• Westlands and Kilimani were the best performing submarkets, with a yield of 12.0% and 10.5% respectively, driven by relatively higher rental rates as the areas are affluent neighbourhoods hosting middle – high-end income earners with high consumer purchasing power and thus investors are willing to pay higher rents for retail space in the area*
*• Karen recorded the highest change in rental yields in H1’ 2019, a reduction of 2.2% points, attributed to a 17.0% decrease in average occupancy from 88.8% in FY’ 2018 to 71.8% in H1’ 2019 as a result of an increase in retail space supply in the area with the opening of Waterfront and The Well malls*
*• Eastlands recorded an increase in rental yields of 0.7% points as a result of a 9.4% points increase in occupancy levels, attributable to the adoption of the formal retail sector by low middle-income earners hence attracting tenants*

*Source: Cytonn Research 2019*

***We expect reduced development activity of malls supply in 2019 due to the current oversupply of 2.0mn SQFT. However, our outlook for the sector is neutral as the sector continues to attract both local and international retailers to cushion the retail real estate sector performance through increased occupancy rates.***

### III. Hospitality Sector

In H1’ 2019, 2 industry reports related to the hospitality sector were released. The take-outs were as stated below:

| Report | Key Take-outs |
|---|---|
| Leading Economic Indicators 2018 | • The number of tourist arrivals at the Jomo Kenyatta International Airport (JKIA) and the Moi International Airport Mombasa grew by 13.0%, from 0.86 mn during the period between January and November 2017 to 0.97mn during the same period in 2018. This we attribute to the improved security and political stability, which have continued to boost tourists’ confidence in the country thus making it a preferred travel destination for both business and holiday travelers<br>• According to Cytonn Market Outlook 2019, we expect the number of arrivals to increase to 1.5 mn during the same period in 2019, supported by the above factors, in addition to the improving air transport operations. See the analysis of the same here |
| Hotel Chain Development Pipelines in Africa 2019 Report | • Kenya was ranked #5 among African countries with the highest hotel room pipeline with a deal pipeline of 27 hotels and 4,232 keys in total, as at 2019, ranking it behind Egypt, Nigeria, Morocco and Ethiopia, with Kenya’s deal pipeline notably increasing by 22.9% from the 3,444 rooms pipeline recorded in 2018,<br>• The upward growth trajectory in Kenya’s hospitality sector was attributed to;<br>•<br>- Enhanced security in spite of setbacks such as the DusitD2 Terrorist attack earlier in the year,<br>- A vibrant tourism sector with the number of international visitors reported in 2018 increasing by 14.0% to 2.0 mn from 1.8 mn in 2017, and<br>- Meeting, Incentives, Conferences and Exhibitions (MICE) initiative, leading to the growth of business tourism.<br>•<br>• For further analysis, see here |

The above reports indicate an upward growth trajectory in the hospitality sector over the last year. This is reaffirmed by the recent hospitality sector activities recorded in the sector during the first half of the year. They include;

?. In January, Superior Hotels Limited, a hospitality chain, opened its third hotel in Naivasha town, in an expansion move that has seen its portfolio grow to 6 hotels. The resort, which is located along Naivasha Moi South Road, brought to the market 96 rooms organized in cottages, 16 conference rooms, a business center and an amphitheater with a capacity of 1,200 people. In our view, the hotel will be a destination for meetings, incentives, conferencing and exhibitions tourism, as Naivasha town is preferred by corporates and government institutions for out-of-office meetings. Please see Cytonn Q1'2019 Market Review,

i. In February, local airlines, Kenya Airways and Silverstone Air, introduced daily direct flights from Nairobi to Seychelles, and from Nairobi to Lodwar, respectively. In our view, the improving air transport operations, political stability and continued marketing of Kenya as an experience destination, will result in increased tourist arrivals. For more analysis, please see our Cytonn Weekly #03/2019,
ii. In February, Ministry of Tourism Cabinet Secretary Hon. Najib Balala announced plans to rehabilitate Kisumu's Sunset Hotel into a conference center. The center, set to be complete by 2021, will have a 10,000-pax capacity with an estimated cost of Kshs 300.0 mn. In our view, the move will buck the growth of both local and international conferencing with demand being driven by national and county government officials, corporates, political parties and international delegates looking to hold meetings in the county. Please see our Cytonn Weekly #08/2019 for more analysis,
iii. In March, Concord Hotels, a local hotel group, announced that it was set to open Shelly Beach Hotel in Mombasa after a US 10.0 mn makeover. The phase 1 of the refurbishment will include restaurants, swimming pools, bar and 36 rooms and is set for completion by the end of 2019. We expect that the refurbishment will result in the improvement of hospitality services and thus give the hotel a competitive advantage in the wake of competition from other international brands such as the Hilton Hotel and Radisson *Hotel Group.* Please see Cytonn Q1'2019 Market Review, and
iv. In May, one of Marriott International's brand of luxury hotels, Autograph Collection Hotels, took over Nairobi's Sankara Hotel located in Westlands, as a franchise. Sankara Hotel, which had 168 keys, underwent renovation to suit the Autograph Collection's brand gaining an additional 11 suites, bringing its total number of keys to 179. For analysis, see Cytonn Weekly #19.

***We expect the hospitality sector to continue recording increased activities supported by; i) the improving air transport operations, ii) continued marketing of Kenya as an experience destination, iii) improved security, and iv) political stability, which have continued to boost tourists' confidence in the country and thus making it a preferred travel destination for both business and holiday travelers.***

## IV**. Land Sector**

The land sector in the NMA recorded a 0.5% y/y decline in the asking prices, 4.3% points decline compared to the 3.8% growth rate in H1'2017, attributed to an overall slowdown in real estate investment activities. Despite the rest of the zones recording a decline in asking prices, un-serviced land in satellite towns such as Ruiru and Limuru registered a 4.1% annual capital appreciation on average, attributed to the relatively high demand for land in these areas fueled by the affordable housing initiative in addition to satellite towns acting as Nairobi's dormitory with majority of the population moving away from the congested Central Business District.

The table below shows the performance of the sector:

*All values in Kshs unless stated otherwise*

***Summary of the Land Price Performance by Zones – Nairobi Metropolitan Area 2018/19***

| **Location** | ***Price in 2011** | ***Price in 2015** | ***Price in H1'2017** | ***Price in H1' 2018** | ***Price in H1' 2019** | **7-year CAGR** | **H1' 2018 Annual Capital Appreciation** | **H1' 2019 Annual Capital Appreciation** | **Y/Y Δ in capital appreciation** |
|---|---|---|---|---|---|---|---|---|---|
| Satellite Towns - Unserviced Land | 9m | 17m | 22m | 23m | 23.7m | 17.8% | 5.1% | 4.1% | (1.0%) |

***Summary of the Land Price Performance by Zones – Nairobi Metropolitan Area 2018/19***

| **Location** | ***Price in 2011** | ***Price in 2015** | ***Price in H1'2017** | ***Price in H1' 2018** | ***Price in H1' 2019** | **7-year CAGR** | **H1' 2018 Annual Capital Appreciation** | **H1' 2019 Annual Capital Appreciation** | **Y/Y Δ in capital appreciation** |
|---|---|---|---|---|---|---|---|---|---|
| Nairobi Suburbs - Low Rise Residential Areas | 36m | 68m | 79m | 82m | 81m | 12.4% | 5.5% | (0.9%) | (6.4%) |
| Nairobi Suburbs - High rise residential Areas | 52m | 92m | 111m | 117m | 117m | 12.7% | 4.2% | (1.6%) | (5.7%) |
| Nairobi Suburbs - Commercial Areas | 156m | 377m | 458m | 473m | 463m | 17.0% | 3.4% | (1.8%) | (5.2%) |
| Satellite Towns - Site and service schemes | 5m | 12m | 13m | 13m | 13m | 18.9% | 1.0% | (2.2%) | (3.2%) |
| **Average** | | | | | | **15.7%** | **3.8%** | **(0.5%)** | **(4.3%)** |

**Asking land price per acre*
*• Land in the NMA recorded a 0.5% y/y decline in the asking prices, a 4.3% points lower than the 3.8% growth rate recorded in H1' 2018, attributed to an overall slowdown in real estate activities thus a decline in effective demand for development land*

*Source: Cytonn Research*

- Land in satellite towns such as Ruiru recorded an annual capital appreciation of 4.1% in H1'2019, 1.0% points lower than the 5.1% growth recorded in H1'2018 attributed to the relatively high demand for land in these areas, fueled by the affordable housing initiative which has been a key focus sector by both the government and private sector players, in addition to satellite towns acting as Nairobi's dormitory with majority of the population moving away from the congested Central Business District,
- Low rise residential areas recorded a 0.9% asking price correction in H1'19, 6.4% points lower than the 5.5% price growth rate recorded in H1'2018. This is attributed to general decline in demand for development land in these areas attributed to (i) unaffordability given the relatively high asking land price per acre of Kshs 81 mn on average compared to satellite towns at approximately Kshs 24 mn per acre, and (ii) credit crunch that has led to a decline in housing units uptake and prices by 3.5% and 0.9% respectively, making these areas unattractive to investors,
- High rise residential areas recorded a 1.6% decline in asking prices in H1'2019 5.8% points decline compared to 4.2% growth rate in H1'2018, attributed to the decline in demand for development land due to reduced development activity, in the residential sector evidenced by the 12.0% decline in total value of residential building approved to Kshs 132 bn in 2018 from Kshs 150 bn in 2017 according to the Kenya National Bureau of Statistics (KNBS) Economic survey 2019,
- Commercial zones recorded a 1.8% decline in asking prices in H1'2019 5.2% points lower than 3.4% recorded in H1'2018. We attribute this to decreased development activities in commercial zones due to the existing oversupply of 5.3 mn SQFT of office space and 2.0 mn of retail space. Kilimani recorded the highest annual capital appreciation at 4.1%, attributed the continued demand for commercial land in the area by developers looking to venture into differentiated concepts such as serviced apartments and offices, which thrive in the area given that it hosts expatriates and the middle class with high purchasing power. On the other hand, Westlands recorded a 9.3% price correction given the high land prices at approximately Kshs 430 mn per acre, thus investors are not able to achieve a favourable return on investment in the area,
- Serviced land in satellite towns recorded a 2.2% annual decline in asking prices, due to decreased demand as buyers are not willing to pay a premium for the services provided, thus opt for un-serviced land and provide the services for themselves. Syokimau- Mlolongo recorded the highest annual capital appreciation of 3.5% driven by the speculative tendencies brought about by the

Standard Gauge Railway (SGR). Ruai recorded the highest decline in prices of 9.4%, attributable to decreased demand for development land in the area as a result of the ongoing land repossession in parts of the area in addition to title contestation thus causing investors to adopt a wait and see attitude, which means reduced activities,

- The investment opportunity in land is in Satellite towns, in markets with high returns such as Ruiru and Utawala which recorded annual capital appreciation rates of above 5.0% in H1’2019 and Syokimau- Mlolongo areas for site and service schemes recording an average 3.5% capital appreciation in the wake of a market decline of 2.2% during the same period, thus making these areas the most recommendable for both land and real estate development.

Other highlights during the first half of the year:

?. In March 2019, the Government of Kenya announced plans to incorporate blockchain technology into the land’s digitization process in a bid to end human interference in the Lands Ministry by helping track all land transactions in the country, thus leading to an efficient, transparent and fair system in a country where issues of land fraud have been rampant. See Cytonn Q1 2019 Market Review, and
i. The Lands Information Management System (LIMS) went live as from 1st April 2019, as announced prior by the Ministry of Lands. The system is expected to shorten the lands registration process by 61-days, to 12-days, from 73-days required by the manual system and this is likely to enhance time-saving, cost reduction and transparency in the registration of land and thus encourage property development. For more details, see our Cytonn Weekly 11/2019.

***Despite the reduced real estate activities in the NMA due to the existing oversupply in the commercial office, retail and upper- mid-end residential sectors, we expect growth in the land sector to be driven by the demand for development land especially with the affordable housing initiative, digitalization of the lands ministry thus simplifying the transaction processes, improving infrastructure and positive demographics.***

V**. Statutory Reviews**

In June, the National Treasury read the FY2019/2020 Budget statement themed *Creating Jobs, Transforming Lives - Harnessing the “Big Four” Plan*. The budget proposed an increase in the rate of Capital Gains Tax (CGT) from 5.0% to 12.5%, excluding the transfer of properties necessitated by restructuring. Despite this having a positive impact on the nation, we expect the same to negatively impact on the real estate sector by resulting in;

?. a “Lock-in effect” as the investors may result in holding properties that have appreciated to avoid paying the CGT on the same if the margins are low,
a. the increased burden to the already struggling real estate sector, and
b. increased property prices in the long run

For further details, see Cytonn Weekly 24/2019

VI**. Infrastructure Sector**

Infrastructure sector was characterised by the following highlights in H1’ 2019;

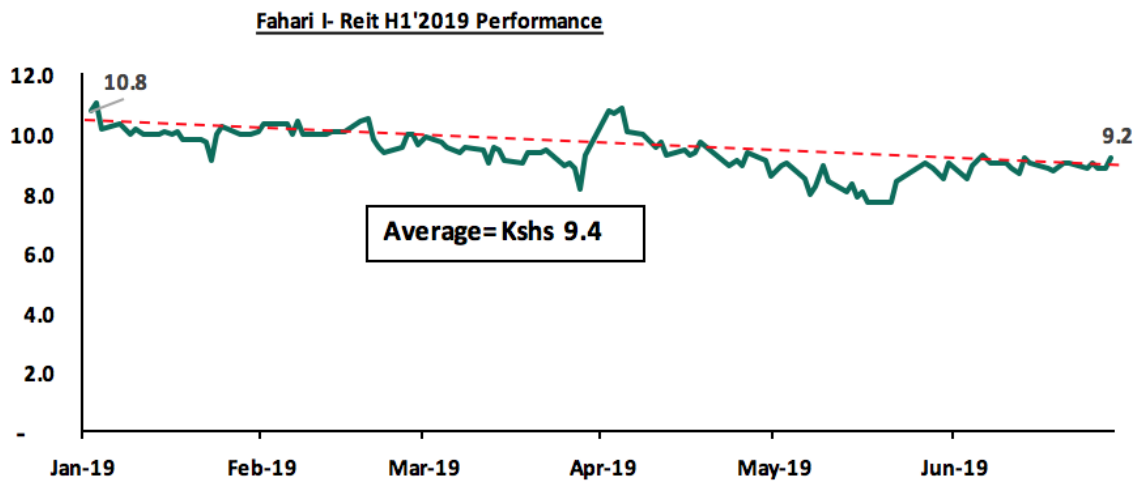
- Kenya National Bureau of Statistics released the Economic Survey 2019, which reported the government expenditure on roads decreased by 7.4%, to Kshs 104.8 bn in 2017/18, from Kshs 113.2 bn in 2016/17. The key notable construction activities in 2018 were the ongoing construction of Phase Two of the Standard Gauge Railway (SGR) and other public investments in transportation infrastructure, with a 9.8% increase in the total length of bitumen roads in Kenya to 18,655 km in 2018, from 16,827 km in 2017. For more information, see Cytonn Weekly #17/2019,

- The National Treasury read the FY2019/2020 budget on 13th June 2019. According to the budget, the infrastructure sector was allocated Kshs 324.7 bn, 22.5% lower than the 418.8 bn allocated in the 2018/2019 budget. The funds will be directed towards ongoing road construction projects as well as road rehabilitation and maintenance, completion of Phase 2A of the Standard Gauge Railway, the Lamu Port-South Sudan-Ethiopia-Transport (LAPSSET) Corridor project and the Mombasa Port Development Project. For more information, see Cytonn Weekly #24/2019,
- Construction of the 17.4 km Western Bypass by the China Road and Bridge Corporation commenced in April. The Kshs 17 bn project starts from Gitaru, linking to Southern Bypass and terminates at Ruaka, in Kiambu County. The increased provision of infrastructure is expected to increase accessibility and reduce traffic congestion, resulting in increased demand for property in satellite towns such as Ruaka.

***Despite the slowdown in infrastructure expenditure, infrastructural development still remains a top priority and we expect the Kenyan government to remain committed in infrastructure improvements and completing ongoing projects.***

VII**. Listed Real Estate**

The Stanlib Fahari Income-REIT closed the first half of the year at Kshs 9.2 per share, 14.4% lower than the year's opening price of Kshs 10.8, and 54.0% from its issue price of Kshs 20. The REIT has been performing poorly mainly due to minimal acceptance by real estate investors and a general poor institutional framework inhibiting its growth.




Other highlights in the sector:

?. In March, Stanlib Fahari I-REIT released their FY'2018 earnings, registering a 13.1% growth in earnings to Kshs 1.07 per unit from Kshs 0.95 per unit in FY'2017, attributable to a 10.9% growth in rental income to Kshs 309.8 mn from Kshs 279.4 mn in FY'2017. The net profit in 2018 grew by 13.1% to Kshs 193.5 mn, from Kshs 171.1 mn in FY'2017. The REIT recorded 1.6% points increase in dividend yield to 8.1% in 2018 from 6.5 % in 2017, attributable to its declining stock price closing at Kshs 9.2 per unit as at 29th March 2019 in comparison to Kshs 11.6 as at 29th March 2018, representing a 20.3% loss of value. To date, that is as at 28th June 2019, the value of the REIT has declined by 54.0%, closing at Kshs 9.2 per share, compared to its initial listing price of Kshs 20.0 in November 2015. For a more comprehensive analysis on the REIT FY'2018 performance, see our Stanlib Fahari I-REIT Earnings Note - 2019,

i. In April, Stanlib Fahari I-REIT announced plans to acquire more properties from pension firms and insurers who will be compensated in the form of units in the REIT. The proposed structure eliminates the need for the firm to raise large sums of new capital to buy more buildings, in addition to expanding the pool of income-generating buildings owned by the REIT and raising earnings for the expanded investor base. For more information and analysis, see our Cytonn Weekly #17/2019,

ii. Nairobi Securities Exchange (NSE) admitted property development company, 'My Space Properties', under the Ibuka Incubator Programme, following successful vetting of the subject company. My Space Properties plans to officially list after the incubation, which will make it the second property developer to be listed in Kenya, after Home Afrika Limited, which went public on 15th July 2013. For more information and analysis, see our Cytonn Weekly #14/2019,

iii. In June, the 2019 Finance Bill was published, and it proposes an amendment of the Income Tax Act to include the exemption of REIT investee companies from income tax. If successful, the amendment which is subject to Parliament's approval will have a positive impact on the performance of the REIT market through resulting in higher returns to the investors, thus attracting them and this will deepen the capital markets. The move signifies the growing institutional support of the REIT by institutions such as the Capital Markets Authority (CMA).

***Our outlook for Stanlib's listed real estate is neutral supported by the improved dividend yield, in line with the real estate performance.***



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