RESEARCH

KENYA

MARKET UPDATE - 2ND HALF 2015

The Westgate Shopping Mall on Mwanzi Road, Westlands

HIGHLIGHTS

- Estimated 2015 GDP growth revised downwards
- Kenya shilling stabilises
- Developers paint positive outlook for the future
- Standard Gauge Railway on track for completion
- Income REIT debuts in market
- Retail yields rise
- Westgate reopened for business
- Office absorption levels dip
- Commercial rents stagnate as headline rents creep up
- Slight dip in prime residential rents
- Prime residential prices up
- Hotel occupancy levels improve
- Radisson Blu opens in Nairobi

The Economy

Kenya's economic performance remained solid, underpinned by strong infrastructure spending and consumer demand, which drove growth. The World Bank estimated that economic growth will be at 5.4% in 2015, a downward revision of 0.6 percentage points on its estimate in December 2014. This revision reflects the strong headwinds the economy was facing in the foreign exchange market, the monetary policy response to calm fears, and the fact that the effect of lower global oil prices on the wider economy was muted because of the depreciation of the shilling in 2015 and weak transmission into the wider economy. It should, however, be noted that the revised figure is still higher than the average for both lower-middle-income countries and Sub-Saharan Africa.

The construction and real estate sectors cumulatively contributed approximately 13.5% to the country's GDP in the 3rd quarter of 2015. Construction grew by 14.1% in the 3rd quarter compared to 8.8% in a similar period in 2014. The accelerated growth was mirrored in the increased credit advanced to the sector and cement consumption. Similarly, the real estate sector grew by 5.4% in 2015 compared to 6.1% in a comparable period in 2014.

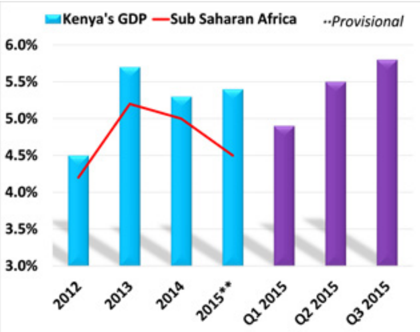
Consumption of cement increased from 2.7 million MT recorded in the 1st half of 2015 to 2.9 million MT in the 2nd half. Developers' positive outlook for the future continued into the 2nd half of 2015, as the value of approved building plans increased by circa 39% from Sh101 billion in the 1st half of 2015 to approximately Sh140 billion in the latter. Though significant, it only represented a 7% increase from a similar period in 2014.

The Monetary Policy Committee (MPC) maintained the Central Bank Rate at 11.5% and the Kenya Banks' Reference Rate at 9.87% throughout the 2nd half of 2015. The retention was informed by the monetary measures put in place by the Central Bank and the fiscal measures undertaken by the National Treasury. Commercial banks' lending rates were observed to increase marginally in the 4th quarter of 2015 but are expected to stabilise with the steadying Kenya shilling. Month-on-month overall inflation was 8% in December 2015, up from 7.3% in November. The increase was driven largely by food prices, mainly Irish potatoes, tomatoes, kales, carrots, cabbages, onions, beef with bones, and avocadoes. These items contributed 2.3 percentage points to overall inflation and 6.3 percentage points to food inflation in December 2015. Commercial lending rates ended the 2nd half of 2015 at a year's high of 17.41%.

The Kenya shilling continued its trend from the 1st half to hit a 3-year low in August and early September, largely reflecting international developments, in particular the impact of the devaluation of the Chinese Yuan and continued strengthening of the US dollar against most currencies. However, the tight liquidity conditions and direct interventions by CBK helped stabilise the market towards the end of the 2nd half.

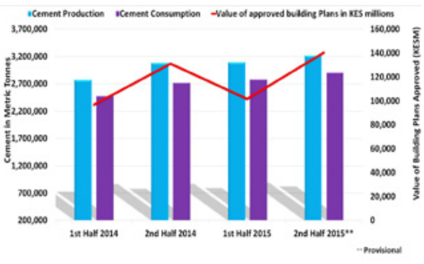
Diaspora remittances increased to circa US$401 million in Q4 of 2015 compared to US$365 million in a similar period in 2014.

FIGURE 1:
GDP Rates



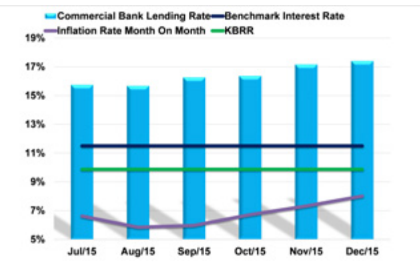
Source: KNBS & World Bank

FIGURE 2:
Value of Building Plans Vs Cement Consumption



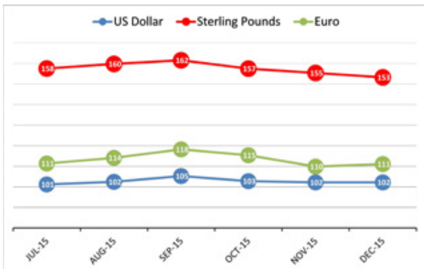
Source: KNBS

FIGURE 3:
Benchmark Economic Rates



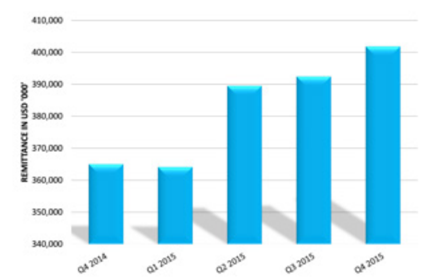
Source: Central Bank of Kenya

FIGURE 4:
Foreign Currency Exchange Rates



Source: KNBS

FIGURE 5:
Quarterly Diaspora Remittances



Source: Central Bank of Kenya

The share of diaspora remittances to Kenya from North America increased from US$187.7 million in Q3 2015 to US$196.4 million in Q4 of 2015. This constituted a 48% and 49% of the total cash inflows for the respective quarters.

Financial Market

Stanlib's Fahari Income Real Estate Investment Trust (I-REIT), the first of its kind in East Africa, started trading at the Nairobi Securities Exchange on November 27, 2015.

Stanlib offered 625 million units priced at Sh20 each during the Initial Public Offering, targeting a maximum of Sh12.5 billion.

The company, however, said it raised Sh3.6 billion from the IPO, 38.5% above the minimum target of Sh2.6 billion.

Data from the Nairobi Securities Exchange shows that the I-REIT has been trading at the Sh20 IPO price or slightly above.

The highest gain seen on the unit so far was Sh23.75, which was reached on the first day of trading. The unit also gained another high trading value averaging Sh22.25 towards the onset of the New Year.

Major investors in the I-REIT included the International Finance Corporation and the Government of Kenya.

Infrastructure

In the 2nd half of 2015, the Government announced that the Sh327 billion Standard Gauge Railway was 60% complete.

The freight trains will have a capacity of 216 TEUs and will travel at an average speed of 80km/h while multiple unit passenger trains will have a capacity of 960 passengers and will travel at an average speed of 120km/h on the line.

A total of 40 stations are planned to be built along the line, 33 out of which will be ready when the railway becomes operational. Proposed designs indicate that it will pass through places with less human settlement in Nairobi thus minimising on compensation claims whilst maintaining a straight line.

In Nairobi, the construction of Outer Ring Road risked further delay as variations to the project more than doubled the initial cost.

The Government needs to raise an additional Sh7.9 billion for the 13-km road after the contractor factored in new costs, including variation of the contract. This pushed the cost up to approximately Sh14 billion. The project, financed by the African Development Bank (80%) and the Government of Kenya, will be ready by September 2017, bringing to an end the traffic woes in Nairobi's most populated suburb.

The road stretches from the Ruaraka/ Thika Road Junction to Taj Mall in Embakasi and involves construction of two lanes in each direction, service roads, 10 footbridges, non-motorised transport facilities and six interchanges. The design also makes provision for a nine-metre raised central median that will be later developed into a bus rapid transit (BRT) corridor. Other features include walkways and cycle tracks over the entire length of the road, planting of 4,500 trees, and a children's traffic safety park.

At the Coast, the first phase of the estimated Sh11 billion Mombasa Port Area Development Project (MPARD), popularly known as the Dongo Kundu by-pass, kicked off.

The project is aimed at decongesting the port of Mombasa. Phase One of the project entails construction works of a 10.1-km dual carriageway from Miritini junction to Kipevu, which also comprises an interchange at Miritini and at the entry of Kipevu, rail-over-road bridge at Miritini, a weigh bridge along the Kipevu link road and a 1.3km access road to the Moi International Airport.

The project is 80% financed by the Japan International Cooperation Agency (JICA), with the Government providing 20%.

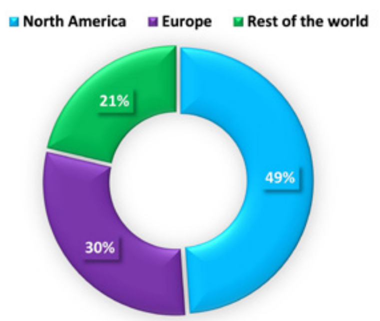
Retail

- Rents stabilise
- Westgate reopens for business
- Retail absorption slows
- Retail yields rise

Westgate Shopping Mall reopened in the 2nd half of 2015, with Nakumatt as the anchor tenant and an overall uptake of over 80%, and only a few shops were yet to open. This is not only a positive indicator for the retail sector, but also a demonstration of the determination and resilience of the Kenyan people.

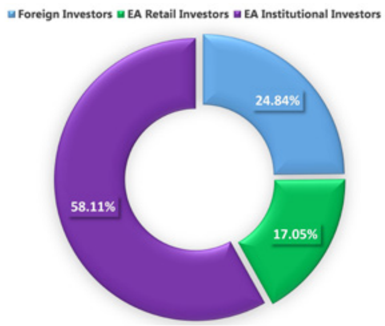
The existing mall comprises of approximately 17,300 square metres of retail space and contributes circa 27% of the formal retail space that was released into the market in 2015.

FIGURE 6:
Remittance Inflow Share by Source, Q4 2015



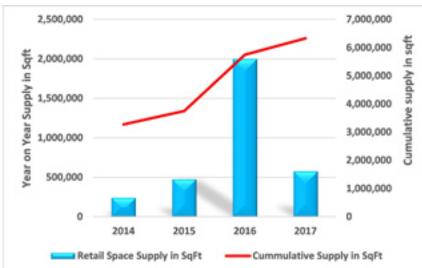
Source: Central Bank of Kenya

FIGURE 7:
Investor Profile, Fahari I-REIT



Source: Stanlib

FIGURE 8:
Retail Space Supply in Nairobi



Source: Knight Frank Kenya

Prime retail rents remained unchanged in the 2nd half of 2015 at US$48/sqm/month. The period experienced a 45% decline in absorption of formal retail space compared to the 1st half.

The decline in absorption of space is mainly attributed to the fact that major retailers had already secured space in the upcoming developments. This was as retailers developed a wait-and-see approach to gauge the performance of their new premises before securing space in the developments in the pipeline.

Southfield Mall in Embakasi broke ground, while major launches expected in the 1st half of 2016 include the 30,000 sqm Diamond Plaza 2 in Parklands that will incorporate a revolving restaurant and Two Rivers on Limuru Road. The Hub in Karen opened on February 4, 2016.

Prime retail yields in 2015 closed at 11.5%, up 150 basis points from 10% in 2014. The most notable transaction was the acquisition of Greenspan Mall by Stanlib for the Fahari I-REIT at approximately US$20 million.

Office

- Absorption levels dip
- Headline rents overtake asking rents
- Supply of office space steady

The 2nd half of 2015 experienced a 5% decline in the absorption of Grade A office space compared to the 1st half of 2015 and a 40% decline compared to a similar period in 2014.

The decline in absorption of office space is still attributed to the decline is supply of prime Grade A offices, coupled by the fact that some multinationals are downsizing their operations in Kenya, particularly in the oil sector. In addition, Government agencies, which were major takers of space are devolving their functions to county levels.

External economic shocks in the international markets begun taking their toll on the commercial office market, specifically on the energy-related companies as some of the key players announced intentions to downsize their operations in Kenya due to the fall of crude oil prices by at least 30% in 2015.

The prime headline rental levels remained stable in the 2nd half of 2015 at US$21/sqm/month, remaining above asking rentals as prospective tenants continue to enjoy a variety of options, owing to an oversupply of office space in the sub-market. This trend is expected to continue into 2016 where the year-on-year supply is set to double. This has resulted in more landlord concessions such as longer rent-free periods, reduced escalations and increased fit-out contributions

The sectional sales market remained quiet in the 2nd half of 2015, with The Mirage along Chiromo Road being the most notable completion in Westlands.

Ongoing construction of commercial office blocks continued in earnest. Most notably, the British American Investments Company Limited (Britam) marked the completion of structural works on its 33-storey Britam Towers in Upper Hill, Nairobi with a 'topping out' ceremony.

Major completions expected in 2016 include UAP Towers and 4th Ngong Avenue Towers, both in Upper Hill, and Two Rivers.

It is estimated that just over 3 million sqft of commercial office space will be released in Nairobi alone in 2016.

Proposed major commercial office developments in the pipeline include the proposed building in Upper Hill by the CPS Governance Centre. It is estimated to cost Sh720 million, with a lettable area of approximately 140,000 sqft. The Elegance, along General Mathenge Drive, is another development that is estimated to cost circa Sh800 million with a net lettable area of approximately 130,000 sqft.

Residential

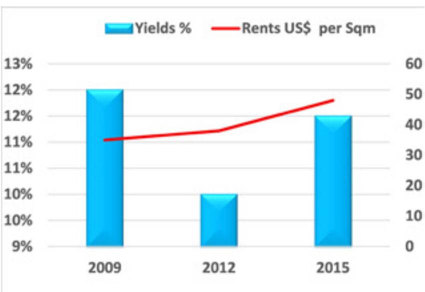
- Stabilised rents persist
- Marginal price increases
- Mega housing projects unveiled

The 2nd half year of 2015 continued the year's relatively stable trend for the high income and upper-middle residential rental market. The price stabilisation through Q3 and Q4 meant that rents remained more or less the same.

Accommodation uptake has been slow and there was a marked decline of rental price change of 5.11% from Q4 2014 to Q4 2015. Nairobi has enjoyed rental increments over the past years with annual escalations in the region of 10%, which built up rents for prime properties significantly. The result is low occupancy levels and longer letting periods.

FIGURE 9:

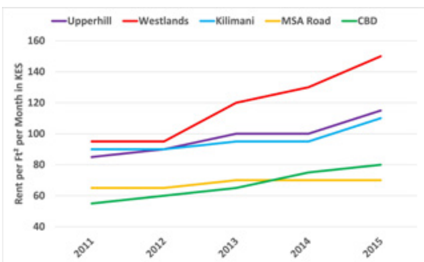
Prime Rental Rate per month per Sqm (2009-2015) & Yields.



Source: Knight Frank Kenya

FIGURE 10:

Prime Rental Rate per month per Sqm (2009-2015) & Yields.



Source: Knight Frank Kenya

FIGURE 11:

Year-on-Year Commercial Office Supply for Nairobi.

Source: Knight Frank Kenya

Contrary to this, the high-end residential sales market witnessed a 2.9% annual growth from Q4 2014 to Q4 2015, compared to a 1.5% increase in a similar period in the previous year, with a quarterly increase of circa 0.7%. This increase in property values was mainly attributed to the poor performance of other investment options, more specifically the bearish run on the stock market witnessed towards the end of the year. The trend is expected to continue into 2016.

Tatu City, Kenya's biggest privately funded real estate project, finally broke ground on the first phase of the project. The residential phase, known as Kijani Ridge, comprises of 150 acres subdivided to 145 half-acre and 156 quarter-acre serviced plots. The phase was 60% sold on ground breaking.

Housing Finance (HF), through its building subsidiary, the Kenya Building Society (KBS), commenced the construction of Komarock Phase 5C consisting of 1,272 apartments. The initial development will consist of 480 units at a cost estimated in the region of Sh1.7 billion.

Other HF developments in the pipeline include Precious Gardens Phase 2 consisting of 144 housing units, 240 apartments along Kamiti Road and 1,100 residential apartments on Thika Road. KBS also plans to develop site and service for 1,024 plots along the Ruiru-Kiganjo Road.

Knight Frank continued to receive interest in high-rise luxury residential in developments such as The Signature in Kileleshwa, which comprises 110 apartments, and The Residences along General Mathenge Drive, comprising 41 apartments. Both developments were over 45% sold as at the end of 2015, with completion dates scheduled for the 1st half of 2016.

On this backdrop, the most notable proposed residential developments in the pipeline include Rumaisa on Riverside Drive and Esquire Investments on General Mathenge Drive, both of which are estimated to cost over Sh0.9 billion.

Major proposed mixed-use developments in the pipeline include Muthithi Heights in Westlands and a development in Kasarani with an estimated construction cost of approximately Sh1.5 billion.

Hotel & Tourism

- Radisson Blu opens
- Travel advisories lifted
- Holiday festivities and conferencing boost occupancy levels

The 2nd half of 2015 witnessed a number of travel advisories against Kenya lifted. These included the United States and France, which lifted their restrictions on travel to the Coast. These followed the United Kingdom which had lifted a travel warning to the same areas in June 2015.

The hospitality sector also got a boost from the conferencing sub-sector, which continued to host major conferences. The most notable ones were the Global Entrepreneurship Summit attended by US President Barack Obama and the 10th World Trade Organisation Ministerial Conference, both hosted at the Kenyatta International Conference Centre in Nairobi.

Carlson Rezidor Hotel Group opened its flagship brand Radisson Blu, in Upper Hill in the 4th quarter of 2015. The hotel offers 271 guest rooms and suites, 2 bars, 2 restaurants, meeting facilities and a 590 sqm ballroom. This represents approximately 9% of the high-end hotel market in Nairobi currently. Park Inn, another brand of Carlson Rezidor, is set to open in 2016 in Westlands.

One of the major hotel developments in the pipeline is the Glee Hotel Limited, which is putting up a Sh1.8 billion hotel on Kiambu Road.

It was noted by industry stakeholders that during the conferences and the holiday seasons, occupancy levels were above 80%. This was substantiated by the number of visitor arrivals in the international airports that peaked in July to 78,243 when the Global Entrepreneurship Summit took place in Nairobi.

Industrial Market & Redevelopment Land

- More industrial parks in pipeline
- Demand for redevelopment land strong

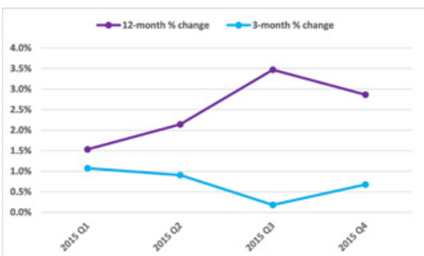
Demand for prime redevelopment and developed land remained strong, with major real estate agents closing major deals towards the end of 2015.

Former retail giant Uchumi Supermarkets announced intention to dispose of some of its prime properties, included a 20-acre plot in Kasarani, in a move aimed at turning around its financial fortunes.

Industrial parks in the pipeline around the capital include the 200-acre Infinity Industrial Park and the 695-acre site within the proposed Northlands City. These add to the already launched industrial parks such as Tatu City's and Tilisi – all within Kiambu County.

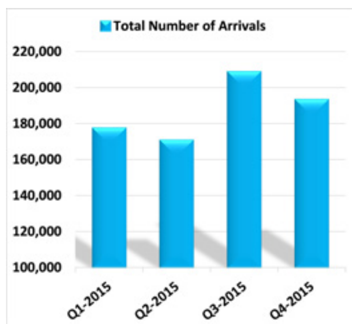
Knight Frank Kenya continued receiving significant interest in prime redevelopment land on its books, with the most notable transactions being 1.1 acres in Upper Hill, Nairobi, which transacted for over US$5 million.

FIGURE 12
Prime Nairobi



Source: Knight Frank

FIGURE 13
Quarterly Arrival Trends



Source: KNBS

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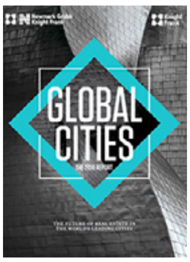

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