Nairobi Metropolitan Area Residential Report 2017/2018

July 2018

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I. Introduction to Cytonn Investments

What We Stand For

Our Mission

We deliver innovative & differentiated financial solutions that speak to our clients' needs

Our Vision

To be Africa's leading investment manager by consistently exceeding clients' expectations

Our Values

People
Passionate and self-driven people who thrive in a team context

Excellence
Delivering the best at all times

Client Focus
Putting clients' interest first at all times

Entrepreneurship
Using innovation and creativity to deliver differentiated financial solutions

Accountability
We take both corporate and personal responsibility for our actions

Integrity
Doing the right things

Strategy is straightforward – just pick a general direction and implement like hell

— Jack Welch

About Us

Cytonn Investments Management Plc is an alternative investment manager with presence in East Africa, Finland and the US. We provide investors with exposure to the high growth East Africa region. Our investors include global and local institutional investors, individual high net-worth investors and the diaspora. We also service retail investors through our Cytonn Co-operative

82 bn Over Kshs. 82 billion worth of projects under mandate

7 Seven offices across 2 continents

400 Over 400 staff members

10 10 investment ready projects

A unique franchise differentiated by:

Independence & Investor Focus

Focused on serving the interest of clients, which is best done on an independent platform to minimize conflicts of interest

Alternative Investments

Specialized focus on alternative assets - Real Estate, Private Equity, and Structured Solutions

Strong Alignment

Every staff member is an owner in the firm. When clients do well, the firm does well; and when the firm does well, staff do well

Committed Partners

Strong global and local partnerships in financing, land and development affiliate

Why We Exist

Africa presents an attractive investment opportunity for investors seeking attractive and long-term returns. Despite the alternative markets in Africa having high and stable returns, only a few institutional players serve the market. Cytonn is focused on delivering higher returns in the alternative markets, while providing the best client service and always protecting our clients' interests.

WE SERVE FOUR MAIN CLIENTS SEGMENTS:

- Retail segment through Cytonn Co-operative membership
- High Net-worth Individuals through Cytonn Private Wealth
- East Africans in the Diaspora through Cytonn Diaspora
- Global and Local Institutional clients

WE INVEST OUR CLIENT FUNDS IN:

- Real Estate
- Private Equity
- Fixed Income Structured Solutions
- Equities Structured Solutions

We collect funds from our clients

We invest them in high growth opportunities

We deliver the best possible returns

Our Business

Where We Operate

Our Business Lines

Investments

Alternative investment manager focused on private equity and real estate

Real Estate

We develop institutional grade real estate projects for investors

Diaspora

We connect East Africans in the diaspora to attractive investment opportunities in the region

Technology

We deliver world-class financial technology solutions

Co-operative

Provides access to attractive alternative investment opportunities for members

Our Solutions

To unearth the attractive opportunity that exists in alternative markets in Africa, we offer differentiated investment solutions in four main areas:

HIGH YIELD SOLUTIONS

Our expertise in the alternative markets enables us to offer investors high yielding investments. Our robust credit analysis coupled with our quick dealing capabilities, our extensive research coverage and our innovative structuring helps to ensure consistent and above market returns to investors.

REAL ESTATE INVESTMENT SOLUTIONS

Our comprehensive real estate capabilities enable us to find, evaluate, structure and deliver world-class real estate investment products to our investors in the East African region. Our capabilities include fundraising, market research and acquisition, concept design, project management and agency and facility management.

PRIVATE REGULAR INVESTMENT SOLUTIONS

Attractive returns in the alternative segments have typically been accessible to institutional and high net-worth investors. Our regular investment solutions provide access to the alternative investments to members of the Cytonn Co-operative.

PRIVATE EQUITY

We seek to unearth value by identifying potential companies and growing them through capital provision, partnering with management to drive strategy and institutionalizing their processes. Our areas of focus are Financial Services, Education, Renewable Energy and Technology Sectors.

Our Products

We serve three main types of clients namely, high net-worth individuals, institutions and retail, each with diverse needs. Below are the suitability criteria for the various products.

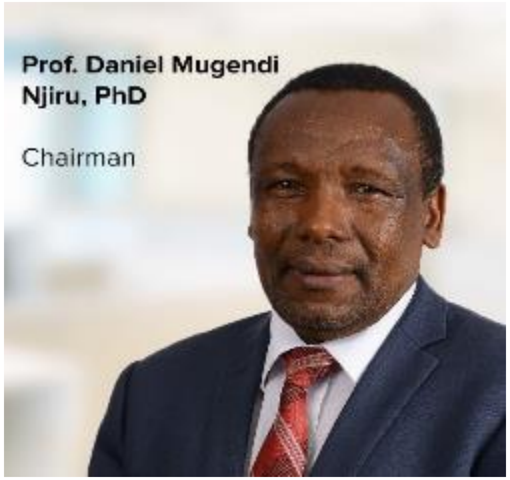
	INSTITUTIONAL CLIENTS	HIGH NET WORTH INDIVIDUALS (HNWI)	RETAIL CLIENTS
Cash Management Solutions	●	●	
Regular Investment Plan • Education Investment Plan • Regular Investment Solution • Co-op Premier Investment Plan • Land Investment Plan	●	●	●
Real Estate Development • Real Estate Developments • Sharpland	●	●	●

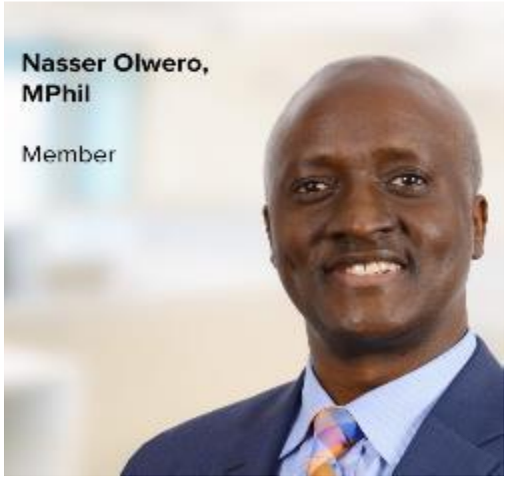
Our People

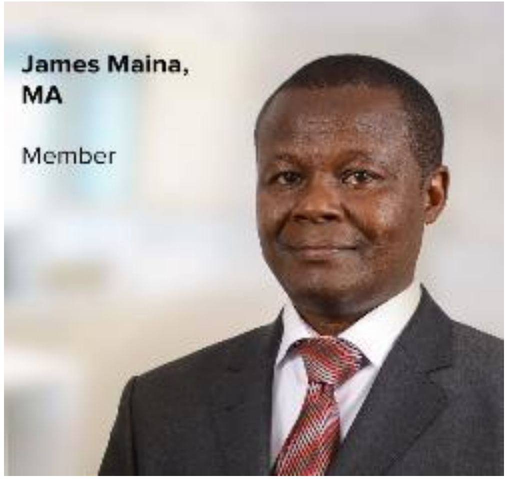
> If you could get all the people in an organization rowing the same direction, you could dominate any industry, in any market, against any competition, at any time.
>
> **— Patrick Lencioni**

Board of Directors

To ensure that we remain focused on the clients' interests, we have put in place proper governance structures. We have a board of directors consisting of 11 members from diverse backgrounds, each bringing in unique skill-sets to the firm.







Board of Directors, continued …

Governance Committees

We have four main board committees to ensure all of Cytonn's functions are done in a fair and transparent manner:

Investments and Strategy Committee

The committee oversees and provides strategic investment direction, including the implementation and monitoring process. The members are:-

- James Maina (Chair)
- Antti-Jussi Ahveninen, MSc
- Madhav Bhalla, LLB
- Edwin H. Dande, MBA
- Elizabeth Nkukuu,CFA

Audit, Risk and Compliance Committee

The committee establishes and oversees risk and compliance, including the implementation and monitoring process. The members are:-

- Madhav Bhalla, LLB (Chair)
- Nasser Olwero, Mphil
- Madhav Bhandari, MBA
- Patricia N. Wanjama, CPS

Governance, Human Resources and Compensation Committee

The committee establishes, oversees and implements governance structure, human resource policies and firm wide compensations. The members are:-

- Antti-Jussi Ahveninen, MSc (Chair)
- Prof. Daniel Mugendi Njiru, PhD
- Michael Bristow, MSc (Chair)
- Edwin H. Dande, MBA

Technology and Innovation Committee

The committee establishes, oversees and implements technical expertise and innovative processes as a driver towards competitiveness. The members are:-

- Nasser Olwero, Mphil (Chair)
- Michael Bristow, MSc
- Patricia N. Wanjama, CPS

II. Overview of Real Estate in Kenya

Introduction to Real Estate in Kenya

Real estate sector expected to continue growing on the back of improved macroeconomic conditions, sustainable high returns, and a changing operational landscape as developers strive to tap into the huge housing deficit

Macro-Economic Contribution

- A relatively stable political environment, as well as favourable macroeconomic conditions have led to sustained GDP Growth which has averaged at 5.3% over the last 5 years, and a stable exchange rate have led to positive development in the sector
- As a result, the real estate sector expanded by 6.8% in Q1'2018, 0.7% points higher than Q1'2017 which recorded a 6.1% growth (KNBS), attributable to a recovery of the macroeconomic environment

High Returns

- Real estate has consistently out performed other asset classes in the last 5 years, generating returns of on average 24.3% p.a, compared to an average of 13.2% p.a for overall asset classes
- Land prices have grown with a 6 year CAGR of 17.4%, with real estate recording an average rental yield of 7.6% in 2017 that is 9.6% in retail, 9.2% in commercial office, 5.8% in industrial sector and 5.6% in residential

Recent Developments

- The real estate sector has witnessed the entry of institutional as well as international players. For instance, in Q1'2018, UK based Mace acquired YMR and Turner and Townsend acquired a majority stake in MML Kenya
- Government initiatives such as: the digitization of the land ministry, the scrapping off of the land search fees and inclusion of affordable housing as part of the Big Four Pillars of focus for the next 5-years are likely to boost real estate development

Market Outlook

- We expect continued growth of the sector boosted by improved macroeconomic conditions, sustainable high returns, and a changing operational landscape as developers strive to address the huge housing deficit
- Key challenges include: high land and infrastructure development costs, high finance costs and inadequate sources of funding

Introduction to Real Estate in Kenya – RE Contribution to GDP

Real Estate and construction sectors contribution to GDP has been on a rising trend from 10.5% in 2000 to 12.6% in 2010 to 14.1% as at 2017

	2000	2010	2017
Agriculture	31.3%	23.7%	31.5%
Manufacturing	17.0%	11.5%	8.4%
Wholesale & Retail Trade	16.5%	7.1%	7.6%
Hospitality & Tourism	16.5%	1.7%	1.2%
Real Estate & Construction	**10.5%**	**12.6%**	**14.1%**

Source: KNBS

III. Nairobi Metropolitan Residential Report

Executive Summary

The residential sector recorded average y/y price appreciation of 2.8% and average rental yields of 5.4%, resulting in 8.2% returns p.a on average, while selected markets had returns of up to 13.9%

- We carried out a research on 35 sub-markets in Nairobi Metropolis. The report aims to inform on the performance and the investment opportunity in the residential sector in Nairobi Metropolis in 2017/2018

- According to Cytonn Research, prices for the period under review, 2017/2018, have appreciated by 2.8% which is 1.0% points lower than the 3.8% recorded in 2017. The slow pace of capital gains could be attributed to a change in the financial landscape in Kenya, with access to home buyer financing getting stricter as an impact of the interest rates cap law, while also increased supply of residential units in some markets has dragged down the rate of price appreciation

- Rental yields during this period have, however, only declined by a marginal 0.2% points, coming in at 5.4% from 5.6% in 2017. We attribute this to increased supply stock, especially in satellite towns and thus investors have had to keep rents stable

- Thus, on the overall performance, with an average price appreciation of 2.8% and rental yields averaging at 5.4%, the total return in the market averaged at 8.2%. In some sub-markets such as Kilimani, however, we recorded returns of up to 13.9%

- On housing demand and supply, Nairobi had an estimated supply of 25,819 units in 2017, bringing the total number of dwelling units available to 1.9 mn; with an estimated population growth of 3.3%, the required number of units in Nairobi in 2018 is 3.9 mn, resulting in a cumulative housing deficit of approximately 2.0 mn units in 2018, having grown from 1.9 mn in 2017 according to Cytonn Research

- On the best areas to invest, Kilimani continue to offer the best investment opportunity for apartments driven by high returns and annual uptake of 13.9% and 25.6% respectively, while Karen and Runda Mumwe are the best for investment in detached units due to (i) uptake of 27.7%, 24.3%, respectively, (ii) relatively high returns at 8.8% and 8.7%, respectively compared to the market average of 8.2%, and (iii) the areas' prime locations

- We expect price stagnation in selected markets with surplus supply. Investors therefore need to invest in proper market research and trend analysis to identify specific market niches

Nairobi Metropolitan Residential Report – "Question of Where Amidst Sluggish Growth"

Y/Y price appreciation came in at 2.8% whereas average total returns came in at 8.2%, an indicator of the sector's sluggish growth

Value Area	Summary	Effect
Demand	• Nairobi Metropolis has a deficit of 2.0 mn units as at 2018, according to Cytonn Research • 70.7% of housing demand is in the lower middle income segment of persons whose average monthly rent is Kshs 18,112 • 26.4% of the housing demand is in the low end income segment of persons whose average monthly rent is Kshs 6,734	• The government continues to offer incentives such as 15% tax for firms that build 100 affordable units annually to boost development of housing for lower income segments, as well as land to developers in a PPP model • This has resulted to growth of satellite towns, with bantamweight developers opting to provide infrastructure where land is cheap
Returns	• Prices appreciated by 2.8% compared to a 3.8% appreciation in 2017 whereas rental yield declined marginally to 5.4% compared to 5.6% in 2017, indicating a sluggish growth of the sector • The best performing markets such as Kilimani have returns of up to 13.9% and Upper Kabete with 11.9%,	• High returns in specific pockets of the market continue to attract investors in areas such as Upper Kabete, and Kilimani • Investors have shied away from low performing areas mostly those experiencing decline in selling prices such as Parklands, Roselyn among others
Opportunity & Outlook	• The opportunity in detached units lies in areas such as Karen and Runda Mumwe which have high annual uptake of 27.7% and 24.3%, respectively • The opportunity in apartments lies is areas such as Kilimani and Upper Kabete, also driven by high uptake of 25.6% and 27.4%, respectively	• We expect increased investment in the best returning areas such as Kilimani and Upper Kabete • Affordability and continued infrastructural improvements in satellite towns is also set to enhance rate of uptake in these areas

While there exists huge demand in the lower middle and low end income segments, there still is opportunity for investment in the upper and high income segment in specific sub-markets that have high uptake and relatively high returns such as Kilimani, Karen and Upper Kabete

A. Introduction

Introduction: Factors Affecting Residential Demand

Increasing incomes, population growth and access to housing finance are affecting the demand for houses

Household Incomes

- With a relatively stable economy whose growth has averaged at 5.3% over the last 5 years, household incomes have increased driven by the fact that most household especially within the middle income class have both partners working and earning a steady income.
- As per the KNBS Economic Survey 2018, the average wages salary came in at Kshs 57,008 in 2017, a 6.1% increase from Kshs 53,733 reported in 2016
- This has resulted in increased demand for formal housing, thus pushing prices up

Demographics

- Kenya’s population has been rapidly growing at an average of 2.6% for the last 5 years compared to a global average of 1.2%, creating demand for more dwelling units
- Additionally, the urbanization rate in Kenya is relatively high at 4.4% compared to the global average of 2.1%, necessitating the need for adequate housing in the urban areas

Access to Credit

- Before the Bank Amendment Act of 2015, the average interest rate on a mortgage in 2015 stood at 18.7%, ranging between 11.9%-23.0%. This however dropped to an average of 13.5%, as at 2016 (CBK) with a range of 10.5%-18.0%, due to the interest rates cap law. Despite this, the number of active mortgages dropped by 1.5% in December 2016 to 24,085 from 24,458, attributed to tight credit standards employed by banks as they would prefer the less risky government securities following the capping of bank interest rates, currently at 13.5%

Affordability

- With the intensified focus on affordable housing, developers are continuously shifting to affordable dwellings, given the affordable land prices in satellite towns and alternative building technologies gaining traction. This has created an avenue for units that are affordable to the middle income earner with areas like Athi River, Ngong and Thika, having prices as low as Kshs 3.0 mn compared to an overall market average of Kshs 6.9 mn

Introduction: Factors Affecting Residential Supply

Difficulty in access to funding and high construction costs negatively affects the supply of houses, but government support creates an enabling environment for developers

Government Initiatives & Incentives

- Following the huge demand for decent housing the government has put in place initiatives aimed at prompting the private sector to aid in addressing the shortage, with initiatives such as the urban regeneration plan for various parts of Nairobi, and tenant purchase schemes in other counties
- Incentives include the 50.0% corporate tax cuts for developers of 100 cost housing units; and provision of public land

Access to Credit

- Lack of proper funding for real estate developments has resulted in excessive debt financing, resulting in increased financing costs owing to the extended project time frames
- The Banking Amendment Act 2015 continues to impact on development activity as financial institutions deprive the private sector of credit which stood at 2.1% as at April 2018, compared to a 5-year average of 14.0% (2013-2018)

Availability and Cost of Development Class Land

- Land prices in Nairobi are relatively high with an average price per acre of Kshs 222.6 mn, that is for high rise, low rise and commercial areas,
- In satellite towns where land is relatively affordable, with an average price per acre of Kshs 17.0 mn, there is inadequate trunk infrastructure, and the developer has to provide, this ultimately leads to increased construction costs for developers amidst waning private sector credit growth

Infrastructure Support

- Improved infrastructural developments such as road repairs, the SGR, bypasses, electrification, and the planned construction of industrial parks in every county, have opened up new development areas in areas such as Kikuyu, Ruiru, Ruaka, and metropolitan areas such as Machakos
- Challenges such as insufficient sewer systems, water supply and access roads in some areas, especially in satellite towns, still persist hampering supply of housing and thus necessitating the need for local government support in the real estate industry

Introduction: Factors Affecting Residential Supply

Land regimes create opacity around land processes with developers facing constant statutory challenges in terms of levies and long approval processes

Land Regimes

- The multiple land tenure land system in Kenya, and the fact that 64.0% of the land in Kenya is estimated to be communal has led to opacity in land registrations and transfers, which affects development processes

Statutory Challenges

- The statutory requirements and approval procedures have been a key challenge for most developers especially due to the elongated processes and also the many fees required which ultimately add onto developer costs. However, even though inadequate, the Kenyan Government has introduced a number of measures aimed at reforming the industry such as the recently launched Sessional Paper No. 1 of 2017 National Land Use Policy (NLUP), digitization of the lands ministry and the scrapping of land title search fees, all aimed at curbing the lack of transparency and efficiency, as well as curbing poor land management

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Recent Developments in Residential Sector

Relaxation of zoning regulations and Affordable Housing Initiatives are changing the residential sector landscape in 2018

i. **Proposed Review of Zoning Regulations:** The relaxation of zoning regulations in areas such as Kyuna, Loresho and Spring Valley, will lead to a densification of the areas which have otherwise been some of the key exclusive neighbourhoods in Nairobi. This is expected to create more demand for low rise properties in areas such as Runda and Karen;

ii. **Government Incentives:** The Government of Kenya has introduced a raft of measures that are key in the performance of the real estate sector. For instance, (i) the digitization of the lands ministry which is aimed at getting rid off the opacity that has laden the ministry for many years, and therefore interfering with the real estate development process, (ii) 50.0% corporate tax cuts for developers of 100 affordable units p.a, and (iii) Innovative financing solutions aimed at aiding in development as well a uptake. For instance, the plans of setting up a Mortgage Liquidity Facility (MLF) i.e. The Kenyan Mortgage Refinancing Company (KMRC), as well as the National Housing Development Fund (NHDF);

iii. **Purpose Built Student Accommodation/Young People's Housing:** As a result of Kenyan universities being ill equipped to accommodate the huge numbers of newly enrolling students, it has necessitated the need for purpose built student accommodation which as per Cytonn Research 2017, has potentially high yields of 7.2% - 9.6%, compared to conventional residential properties whose yield stands at 5.6%. Notable partnerships in this segment include locally-based Acorn and UK-based Helios; NY-based Africa Integra-Kenyatta University; NY-based Consonance Kuramo and locally based Century Developers Ltd

Recent Developments: Affordable Housing Initiative

The Kenya Mortgage Refinancing Company and National Housing Development Fund are expected to increase mortgage uptake and fast tracking affordable homes' off take, respectively

iv. Affordable Housing Initiative/Big 4 Agenda:

As part of the Big 4 Agenda, the government plans to develop 1.0 mn units over the next 5 years out of which, 20.0% will be social housing with price points of Kshs 0.6 mn – 0.8 mn while 80.0% will be affordable housing costing between Kshs 0.6 mn and Kshs 3.0 mn, to be delivered through public-private partnerships

Toward this goal, the government has proposed various strategies some of which include;

i. Provision of public land and undertaking land swaps to avail suitable land for development
ii. Public-private partnerships with the private sector to obtain 60% of the required funding
iii. Legislative reviews such as the RBA Act to allow the NSSF to invest more than 30% of its AUM in real estate, thus obtain more funding
iv. Amendment of the Employment Act of 2012 to increase minimum contributions from employees to allow for creation of a National Housing Development Fund (NHDF)
v. Setting up of the NHDF whose role is to provide funding for development as well as a home-savings plan for employees and thus facilitate offtake of affordable homes
vi. Provision of a waiver on stamp duty for first time buyers, tenant-purchasing schemes and extension of background checks to include the informal sector so as to increase home-ownership
vii. Setting up of the Kenya Mortgage Refinancing Company (KMRC) whose role is to enable longer-term loans at attractive rates by creating liquidity for primary lenders

- We therefore expect to see redirection of developer efforts towards provision of more housing for the lower middle to low income market segments

Affordable Housing Initiative: Kenya Mortgage Refinancing Company

The Kenya Mortgage Refinancing Company will enable provision of mortgages for longer tenors through increased liquidity for the primary lenders

What it is

- This is a non-bank financial institution restricted to providing long-term funding and capital market access to mortgage lenders through issuance of bonds to investors
- It will be under the Central Bank of Kenya's supervision, while its bond issuance operations will be overseen by the Capital Markets Authority of Kenya

How it works

- Borrowers cede their property as security for a long-term mortgage loan while the KMRC will lend its funds to the Primary Mortgage Lenders with the mortgages as collateral
- KMRC will then issue a bond to investors with the mortgages as collateral
- Investors including institutions with medium to long-term investment horizons buy the bonds at a margin above government securities

Expected Impact

- Boosted supply of long-term capital and thus expansion of mortgage lending
- Fostering healthy competition in the mortgage market by promoting the entry of new primary lenders
- Mortgage home-buyers will access mortgages for longer tenors, pay lower instalments and thus it will reduce the financial burden for buyers thus scaling up the rate of uptake for housing

Limitations

- Investors are likely to buy into the long-term mortgage backed bond for approximately 13.0%-14.0%, assuming a 1.0% margin above the minimum of the risk free rate for a 10-15 year bond which currently ranges from 12.0%-13.1%
- With a risk premium that the primary lenders are likely to charge, currently at 4.0%, the cost of debt is likely to be at least 17.0% which is still high and may lock out lower income earners

Affordable Housing Initiative: National Housing Development Fund

The role of the National Housing Development Fund will be management of funds for provision of affordable housing, and also to act as a savings plan for potential home-buyers

What it is

- This is a fund tasked with management of funds set aside for planning and provision of low cost housing
- It will also act as a savings plan for potential home-buyers through monthly contributions towards the fund and consequently offer offtake for housing developments

How it works

- Employees will contribute a percentage of their income-0.5% of their gross earnings each month, to a maximum of Kshs 5,000, and employers will match the amounts contributed to the fund
- Individuals in the affordable housing bracket will use the funds to purchase houses through tenant purchase schemes, while individuals with stronger financial muscle, will use the funds as deposits for mortgages or other forms of securitization
- The funds will be used for construction of houses. Contributors will book houses and start paying for the houses off-plan in addition to their monthly contributions

Expected Impact

- The fund will raise part of the required capital for construction and provision of social infrastructure
- It will provide offtake for the houses as registered contributors will be allocated houses, whose payments will be made during the construction period

Limitations

- The fund will not be sufficient to provide the off-take and financing needed given the relatively low incomes of Kenyans
- It is likely to face opposition due to the possibility of primary contributors not benefiting as allocation will be structured in a lottery form and also given that employers and employees are already subjected to a number of statutory deductions

B. Residential Market Performance

Cytonn
REAL ESTATE

Market Performance Summary

We conducted research in 35 sub-markets and categorized them into High End, Upper Middle and Lower Middle segments

- We conducted market research in 35 sub-markets in Nairobi Metropolitan area to determine returns measured by rental yields and price appreciation
- In our submarket analysis, we classified the various suburbs in the Nairobi Metropolitan Area into three segments

  i. **High End Segment** – Consists of prime suburbs in Nairobi, such as Karen, Runda and Kitisuru. Most of these zones have been zones for low rise residential developments only and are characterized by palatial villas and bungalows on half acre parcels

  ii. **Upper Middle Income Segment** – Consists of suburbs such as Kilimani, Lavington, Kileleshwa, Loresho and Ridgeways among others. The population in these zones are middle class but with higher incomes than the average characterization of middle class. They are zones for both high rise and low density houses.

  iii. **Lower Middle Income Segment** – Consists of suburbs in Nairobi habited by middle class such as Donholm, Komarock and Imara Daima as well as Satellite Towns such as Ngong, Rongai and Juja

- We analysed detached units and apartments separately;

  i. **Detached units** refers to stand-alone houses such as townhouses, maisonettes and bungalows

  ii. **Apartments** refers to a self-contained housing units occupying part of a building, also called flats

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Market Performance Summary

Prices appreciation came in at 2.8%, 1.0% points lower than 2017 which came in at 3.8%. Total returns declined by 1.2% points to 8.2% compared to last year' 9.4%

Segment	Average Rental Yield 2017/2018	Average Y/Y Price Appreciation 2017/2018	Total Returns 2017/2018	Average Rental Yield 2017	Average Price Appreciation 2017	Total Returns 2017	Y/Y Change in Appreciation	Y/Y Change in Rental Yield	Y/Y Change in Total Returns
High-End	4.7%	3.5%	8.3%	5.6%	3.9%	9.5%	-0.4%	(0.9%)	(1.2%)
Upper Middle	5.1%	2.4%	7.5%	4.9%	2.6%	7.5%	(0.2%)	0.2%	0.0%
Lower Middle	5.0%	2.0%	7.0%	5.0%	6.1%	11.1%	(4.1%)	0.0%	(4.1%)
Detached	4.9%	2.7%	7.6%	5.0%	3.9%	8.9%	(1.5%)	(0.2%)	(1.8%)
Upper Middle	6.0%	2.9%	8.9%	6.2%	4.3%	10.5%	(1.4%)	(0.2%)	(1.6%)
Lower Middle Suburbs	5.6%	3.2%	8.8%	5.3%	3.5%	9.2%	(0.3%)	0.3%	(0.4%)
Lower Middle Satellites	5.9%	2.7%	8.6%	6.5%	2.6%	9.1%	0.1%	(0.6%)	(0.5%)
Apartments	5.8%	2.9%	8.7%	6.0%	3.5%	9.5%	(0.6%)	(0.2%)	(0.8%)
Average	**5.4%**	**2.8%**	**8.2%**	**5.6%**	**3.8%**	**9.4%**	**(1.0%)**	**(0.2%)**	**(1.2%)**

- Average prices increased by 2.8% on average, 1.2% points slower compared to 3.8% in 2017
- Capital appreciation had the deepest decline of 4.1% in the lower middle end sector for detached; which we attribute to increased supply in the lower mid income segment and thus owners have had to reduce prices to attract buyers
- Rental yields declined marginally y/y by 0.2% points to 5.4%. This is attributable to increased housing stock in the market and thus developers have had to stabilize rents in order to preserve clientele
- Overall, the sector's performance dropped marginally, driven by a decline in the rate of price appreciation which we attribute to the effect of last year's electioneering period and financing challenges following the waning private sector credit growth owing to the interest rates cap law

Source: Cytonn Research

Cytonn REAL ESTATE

i. Detached Units Performance

Market Performance: Detached Units, High-End

Lower Kabete had the highest returns at 10.8% while Rosslyn has the lowest at (1.9%) per annum

Location	Average Price Per SQM	Average Rent Per SQM	Average Annual Sales	Average Rental Yield	Average Price Appreciation	Average Total Returns
Lower Kabete	174,963	491	21.4%	3.4%	7.5%	10.8%
Kitisuru	250,983	1,007	22.6%	4.7%	5.4%	10.1%
Karen	194,341	799	27.7%	4.7%	4.0%	8.8%
Runda	188,098	772	23.2%	5.0%	2.7%	7.7%
Roselyn	164,125	808	20.8%	5.9%	(1.9%)	3.9%
Average	**194,502**	**776**	**23.1%**	**4.7%**	**3.5%**	**8.3%**

- Lower Kabete and Kitisuru areas continued to perform well, registering the highest returns in the high-end market. This is attributable to the exclusivity both areas offer, and high land prices that lead to developers increasing unit prices to recoup returns
- Rosslyn recorded the least returns, owing to a depreciation of asking prices by 1.9%. This is attributable to the market's limitation in terms of what it offers investors

Source: Cytonn Research

Market Performance: Detached Units, Upper Mid-End

Langata and Runda Mumwe performed best in the upper mid end sector indicating investor demand

Location	Average Price Per SQM	Average Rent Per SQM	Average Annual Sales	Average Rental Yield	Average Price Appreciation	Average Total Returns
Langata	129,107	448	21.6%	4.3%	4.7%	9.1%
Runda Mumwe	144,346	687	24.3%	5.8%	2.8%	8.7%
South B/C	131,394	582	22.3%	4.5%	3.5%	8.0%
Spring Valley	167,940	504	21.2%	4.3%	3.5%	7.7%
Lavington	180,498	658	16.7%	4.4%	3.1%	7.5%
Loresho	150,499	827	25.0%	6.6%	(0.6%)	6.0%
Ridgeways	150,422	822	20.8%	5.5%	(0.3%)	5.2%
Average	**150,601**	**647**	**21.7%**	**5.1%**	**2.4%**	**7.5%**

- Langata had the highest returns in the upper mid end sector, recording the highest price appreciation in the category of 4.7%
- Langata's performance is on account of its proximity to key business districts such as Upperhill, and CBD against low supply to match the demand
- Ridgeways and Loresho registered a slight decline in prices by 0.3% and 0.6%, respectively
- This is attributable to encroachment of apartments in and round these areas, leading to decline in value for low rise houses as the areas lose their appeal to high end buyers

Source: Cytonn Research

Cytonn REAL ESTATE

Market Performance: Detached Units, Lower Mid-End

Ruiru had the highest returns to investors at 11.7% while Imara Daima had the lowest with 4.2%

Location	Average Price Per SQM	Average Rent Per SQM	Average Annual Sales	Average Rental Yield	Average Price Appreciation	Average Total Returns
Ruiru	91,591	332	23.6%	5.1%	6.6%	11.7%
Kitengela	70,558	309	22.6%	4.8%	6.2%	11.0%
Ruai	49,407	265	18.8%	6.6%	0.0%	6.6%
Donholm & Komarock	86,198	367	22.8%	5.2%	1.1%	6.3%
Rongai	80,145	305	23.8%	4.6%	4.1%	8.7%
Juja	81,844	277	23.3%	5.1%	1.1%	6.1%
Redhill	89,979	327	19.2%	4.2%	1.6%	5.8%
Syokimau/Mlolongo	73,333	340	25.0%	5.7%	0.0%	5.7%
Athi River	91,948	295	22.6%	3.7%	2.4%	6.2%
Thika	67,875	326	22.3%	4.7%	0.3%	5.1%
Ngong	65,125	247	23.4%	4.5%	2.1%	6.6%
Imara Daima	72,417	318	26.9%	5.1%	(1.0%)	4.2%
Average	**76,702**	**309**	**22.9%**	**5.0%**	**2.0%**	**7.0%**

- Ruiru had the highest returns at 11.7%
- Ruiru has been performing well on account of good infrastructure, for instance, the Thika Superhighway and the Eastern bypass respectively. It is also driven by its affordability compared to other suburbs while offering easy access to CBD
- Imara Daima registered the least returns attributable to the quality of detached properties in the area which is predominantly a high rise area

Source: Cytonn Research

Cytonn REAL ESTATE

ii. Apartments Performance

Market Performance: Apartments, Upper Mid-End

Kilimani has high returns at 13.9% due to its prime location and sustained demand from the middle class income population

Location	Average Price Per SQM	Average Rent Per SQM	Average Annual Sales	Average Rental Yield	Average Price Appreciation	Average Total Returns
Kilimani	131,594	621	25.6%	6.1%	7.8%	13.9%
Riverside	121,295	508	21.7%	5.4%	3.8%	9.3%
Spring Valley	144,169	647	24.1%	5.9%	3.1%	9.0%
Loresho	109,426	558	23.2%	6.0%	2.7%	8.7%
Upperhill	141,905	593	23.7%	5.2%	3.4%	8.6%
Westlands	132,128	636	26.1%	6.0%	2.3%	8.3%
Kileleshwa	124,549	629	23.6%	6.0%	1.0%	7.0%
Parklands	113,908	641	25.8%	7.3%	(1.3%)	5.9%
Average	**127,372**	**604**	**24.2%**	**6.0%**	**2.9%**	**8.9%**

- Kilimani area has the highest returns at 13.9% owing to its proximity to key business districts and nodes such as CBD, Upperhill and Westlands, and also its vast supply of social amenities such as neighborhood malls and good infrastructure and incoming infrastructure such as the upgrade of Ngong Road,
- Parklands had the lowest returns averaging at 5.9% compared to a market average of 8.8%, due to a decline in asking prices by 1.3%. This is attributable to an increase in supply of apartments as investors move out of Westlands which is increasingly being commercialized

Source: Cytonn Research

Cytonn REAL ESTATE

Market Performance: Apartments, Lower Mid-End Suburbs

Upper Kabete has the highest uptake in the suburb area of 27.4% with the highest returns of 11.9%

Location	Average Price Per SQM	Average Rent Per SQM	Average Annual Sales	Average Rental Yield	Average Price Appreciation	Average Total Returns
Upper Kabete	86,344	429	27.4%	6.3%	5.6%	11.9%
South B & C	107,819	510	26.5%	5.7%	4.4%	10.1%
Donholm & Komarock	75,072	374	20.3%	6.0%	3.9%	9.9%
Ngong Road	99,630	453	25.6%	5.9%	4.0%	9.9%
Imara Daima	74,232	381	26.2%	6.3%	3.0%	9.4%
Kahawa West	82,166	416	22.9%	6.2%	1.8%	8.1%
Dagoretti	98,038	482	22.5%	6.2%	1.7%	7.8%
Thome	124,554	297	22.3%	2.8%	3.9%	6.7%
Langata	107,374	462	23.2%	5.3%	0.3%	5.6%
Average	**95,025**	**423**	**24.1%**	**5.6%**	**3.2%**	**8.8%**

- Upper Kabete recorded the best returns in the lower middle end sector for suburbs
- Upper Kabete benefits from its proximity to Waiyaki Way which offers good access to business nodes such as Westlands and the CBD, thus, attracting demand especially from the young and working population in general
- Langata recorded the lowest price appreciation of 0.3% compared to a market average of 3.2%, indicating low demand from investors attributable to competition from areas such as South B and C

Source: Cytonn Research

Market Performance: Apartments, Lower Mid-End Satellite Towns

The satellite towns with the highest returns are Thindigua and Ruaka with 11.2% and 11.1% against market average of 8.5%

Location	Average of Price Per SQM	Average of Rent per SQM	Average of Annual Sales (%)	Average of Rental Yield	Average of Price Appreciation	Average of Total Return
Thindigua	92,603	454	28.2%	5.9%	5.3%	11.2%
Ruaka	101,163	440	25.6%	5.3%	5.8%	11.1%
Ruiru	89,918	469	20.6%	6.3%	3.7%	9.9%
Athi River	63,395	351	25.4%	6.3%	2.4%	8.7%
Rongai	70,983	338	23.7%	5.9%	2.8%	8.7%
Lower Kabete	86,026	415	24.3%	5.8%	2.6%	8.4%
Kitengela	67,018	327	19.4%	6.4%	1.8%	8.2%
Kikuyu	76,046	336	22.3%	5.3%	2.7%	8.1%
Syokimau/Mlolongo	75,313	299	22.0%	5.0%	1.8%	6.8%
Thika	49,155	284	25.0%	6.1%	0.3%	6.4%
Juja	50,728	259	23.7%	6.1%	0.0%	6.1%
Average	**74,759**	**361**	**23.7%**	**5.9%**	**2.7%**	**8.6%**

- Thindigua and Ruaka recorded the best returns driven by relatively high y/y price appreciation at 5.3% and 5.8%, respectively, compared to the market average of 2.7%. Both areas benefit from proximity to high end neighborhoods such as Runda and Rosslyn, thus attracting investors
- Apartments in Juja stagnated in price appreciation, as apartments in the area mostly target, and also mostly occupied by, the student population and thus buyers in the sub-market prefer detached

Source: Cytonn Research

Cytonn REAL ESTATE

Market Performance: Summary

High end market for detached recorded the highest year-on-year price appreciation at 3.5% with upper middle market for apartments recording the highest average rental yields at 6.0%

Segment	Typology	Average Price Per SQM	Average Rent Per SQM	Average Annual Sales	Average Rental Yield 2017/2018	Average Y/Y Price Appreciation 2017/2018	Total Returns 2017/2018
High End	Detached	194,502	776	23.1%	4.7%	3.5%	8.3%
Upper Middle	Detached	150,601	647	21.7%	5.1%	2.4%	7.5%
Lower Middle	Detached	76,702	309	22.9%	5.0%	2.0%	7.0%
Upper Middle	Apartments	127,372	604	24.2%	6.0%	2.9%	8.9%
Lower Middle Suburbs	Apartments	95,025	423	24.1%	5.6%	3.2%	8.8%
Lower Middle Satellites	Apartments	74,759	361	23.5%	5.9%	2.7%	8.6%
Average					5.4%	2.8%	8.2%

- The residential market has an average return of 8.2% for the period 2017/2018
- For investment, Kilimani recorded the highest returns in the apartments segment with 13.9%, and Upper Kabete which recorded average returns of 11.9%,
- For detached units, returns to investors were highest in areas such as Lower Kabete, and Ruiru, which had the best annual returns to investors in this category with 10.8%, and 11.7%, respectively

Source: Cytonn Research

Cytonn REAL ESTATE

C. Residential Market Opportunity

Residential Market Opportunity: Demand

The measure of adequate housing used is one person per habitable room

- We carried out an analysis to determine the housing requirement in Nairobi Metropolis based on the population, and the housing supply;

Assumptions Used

- The measure of adequate housing used is one person per habitable room
- Developments have a 2-year lag-period between getting approvals and completion
- Only 75% of planned developments actually go into market
- Owner-occupiers account for 28% of the housing market
- The population grows at a constant rate of 3.3%
- Only 30% of the buildings are compliant on obtaining approvals

Terms Used

- A **habitable room** is any room in a dwelling unit that is used mainly for living and excludes stores, granaries, offices, toilets and garages

Limitations of Methodology

- The methodology used assumes one person per habitable room as a measure of adequate housing whereas in reality families are comfortable sharing rooms eg couples, young children and same gender children

Source: Nairobi City County Building Audit, KNBS

Residential Market Opportunity: Demand

Nairobi Metropolis requires 2.0 Mn dwelling units in 2018; 70.7% of the demand is in the lower middle income segment

Year	2009	2014	2015	2016	2017	2018F	2019F	2020F
Nairobi Metropolis Urban Population	5.0m	5.8m	6.0m	6.2m	6.4m	6.6m	6.9m	7.1m
Nairobi Metropolis Urban Population Growth Rate		3.3%	3.3%	3.3%	3.3%	3.3%	3.3%	3.3%
Total Units Supplied		17,039	18,020	18,581	25,819	20,771	16,238	20,352
Nairobi Metropolis Habitable Rooms Supplied		28,540	30,184	31,123	43,247	34,791	27,199	34,090
Nairobi Metropolis Habitable Rooms Available	3.1m	3.2m	3.2m	3.2m	3.3m	3.3m	3.3m	3.4m
Nairobi Metropolis Habitable Rooms Required	5.0m	5.8m	6.0m	6.2m	6.4m	6.6m	6.9m	7.1m
Nairobi Metropolis Habitable Rooms Deficit	1.9m	2.6m	2.8m	3.0m	3.1m	3.3m	3.5m	3.7m
Nairobi Metropolis Dwelling Units Deficit	**1.3m**	**1.6m**	**1.7m**	**1.8m**	**1.9m**	**2.0m**	**2.1m**	**2.2m**
Owner-Occupied Developments	28%	28%	28%	28%	28%	28%	28%	28%
Developer Supplied Housing Requirement	**0.9m**	**1.1m**	**1.2m**	**1.3m**	**1.3m**	**1.4m**	**1.5m**	**1.6m**

Income Groups	Percentage	2014	2015	2016	2017	2018	2019	2020
Low Income (Avg Rent Kshs 6,734)	**26.4%**	299,153	317,373	336,197	354,386	374,288	395,830	417,402
Lower Middle Income (Avg Rent Kshs 18,112)	**70.7%**	801,480	850,295	900,728	949,460	1,002,780	1,060,495	1,118,290
Upper Income (Rent above Kshs 30,000)	**2.9%**	32,842	34,842	36,909	38,906	41,091	43,456	45,824

Source: KNBS, Kenya 2009 Census, Cytonn Research

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Residential Market Opportunity: Supply

Metrics such as uptake, returns, infrastructure and distance from key business nodes have been used to determine the best areas to invest

- Whereas the overall market performance has declined, there exists an opportunity in some sub-markets. To identify the investment opportunity in the sector and single out the specific suburbs that would be best to invest in, we used the following metrics;
   i. **Weighted Annual Uptake-** Derived from the difference between 2018 and 2017's absolute uptake, this refers to how fast developments sell on average per annum, the higher/ faster the sales rate, the higher the points allotted
   ii. **Average returns-** This is the sum of the rental yield and price appreciation for each suburb. The higher the return the more points allotted
   iii. **Amenities** – areas with good amenities and incoming mall space scored high with areas that lack current or future planned development scored low
   iv. **Distance from Main Business Nodes-** This is to establish the commute distance for majority of the working population, where we assumed Nairobi Central Business District as the common node
   v. **State of infrastructure -** Here we looked at bits of infrastructure that affect real estate heavily, that is, roads and sewer systems. For the purpose of the ranking, for detached properties, we used the status of the roads only, while the following factors were used to rank the incoming infrastructure and the state of the infrastructure for high rise areas;
      a. **Good**-Access mainly through tarmac Roads and sewered
      b. **Average**- Access mainly through tarmac roads but not sewered
      c. **Poor-** Access mainly through earth roads and not sewered

Residential Market Opportunity: Supply

Areas have been allocated points from 1 to 3, with 3 being the highest points

- The following shows the points allocated for each metric
- Areas have been allotted points from 1 to 3, with 3 being the highest points. The higher the points, the better an area is for investment

Residential Market Opportunity			
Weighted Annual Uptake (WAU)	**<0.2%**	**0.2%-0.4%**	**>0.4%**
Points	1	2	3
Average Returns	**<5%**	**5-10%**	**>10%**
Points	1	2	3
Availability of Amenities	**Low (supermarket)**	**Average (Neighbourhood Community + social amenities)**	**High (regional mall, social amenities)**
Points	1	2	3
Infrastructure	**Poor**	**Average**	**Good**
Points	1	2	3
Distance from Main Business Nodes	**>28 km**	**15km-28km**	**Within 14km radius of NRB CBD**
Points	1	2	3

Residential Market Opportunity: Apartments, Top 15

Kilimani, Westlands and Ruaka are the best for apartments development due to high annual uptake, investor returns and relatively good state of infrastructure

	5.0%	5.0%	15.0%	30.0%	35.0%	10.0%		
Location	**Distance from Main Business Node**	**Amenities (Incomng and current malls & Recreation)**	**Infrastructure**	**Weighted Annual Uptake**	**Returns**	**Availability of Development Class Land**	**Total Points**	**Rank**
Kilimani	3.0	3.5	3.5	2.0	3.0	2.0	2.7	1
Westlands	3.0	3.5	3.5	3.0	2.0	1.0	2.6	2
Thindigua	3.0	2.0	2.0	2.0	3.0	2.0	2.4	3
Ruaka	2.0	2.0	2.0	2.0	3.0	2.0	2.4	4
Waiyaki Way	3.0	2.0	2.0	2.0	3.0	1.0	2.3	5
South B & C	3.0	2.0	2.0	2.0	3.0	1.0	2.3	5
Spring Valley	3.0	3.5	3.5	2.0	2.0	1.0	2.3	7
Ruiru	1.0	1.5	1.5	3.0	2.0	3.0	2.3	8
Upperhill	3.0	3.0	3.0	2.0	2.0	2.0	2.3	8
Riverside	3.0	3.0	3.0	2.0	2.0	1.0	2.2	10
Loresho	3.0	2.5	2.5	2.0	2.0	2.0	2.2	10
Kikuyu	2.0	1.5	2.0	2.0	2.0	3.0	2.1	12
Race Course/Lenana	2.0	2.5	2.5	2.0	2.0	1.0	2.0	13
Athi River	1.0	1.5	1.5	2.0	2.0	3.0	2.0	14
Kitengela	1.0	1.5	1.5	2.0	2.0	3.0	2.0	14
Imara Daima	1.0	2.5	2.5	2.0	2.0	1.0	2.0	14

- For apartments we allotted the highest weighting to average returns and uptake at 35% and 30%, respectively. This is because for the investors and buyers, these are the most important factors to consider when investing
- We allotted the lowest weighting to distance from main business node and amenities at 5%. This is these factors are catered for in the pricing. However, existing incoming infrastructure was allocated 15% as it is one of the key factors which attracts both developers and buyers,
- Kilimani and Westlands therefore are the best opportunity for residential development driven by uptake, good infrastructure and market returns

Source: Cytonn Research

Residential Market Opportunity: Detached Units, Top 15

Karen and Runda Mumwe are the best for detached units development due to relatively higher uptake and returns

Location	Distance from main Business Node	Amenities	Infrastructure	Weighted Annual Uptake	Average Returns	Availability of Develoment Land	Total Points	Rank
	5.0%	5.0%	10.0%	30.0%	35.0%	15.0%		
Karen	3.0	3.0	2.0	3.0	2.0	3.0	2.6	1
Runda Mumwe	3.0	2.0	1.5	2.0	2.0	3.0	2.2	2
Ruiru	1.0	2.0	2.0	2.0	2.0	3.0	2.1	3
South B/C	3.0	1.0	1.0	3.0	2.0	1.0	2.1	4
Kitisuru	3.0	1.0	2.0	1.0	3.0	2.0	2.1	4
Lower Kabete	2.0	1.0	2.0	1.0	3.0	2.0	2.0	6
Ngong	1.0	2.0	1.0	3.0	1.0	3.0	2.0	7
Juja	2.0	2.0	1.0	2.0	1.0	3.0	1.7	8
Kitengela	2.0	1.0	1.0	2.0	1.0	3.0	1.7	9
Rongai	2.0	1.0	1.0	2.0	1.0	3.0	1.7	9
Langata	3.0	2.0	2.0	1.0	2.0	1.0	1.6	11
Athi River	1.0	1.0	1.0	2.0	1.0	3.0	1.6	11
Redhill & Sigona	1.0	1.0	1.0	1.0	2.0	2.0	1.5	13
Runda	3.0	3.0	2.0	1.0	1.0	2.0	1.5	14
Ridgeways	3.0	3.0	2.0	1.0	1.0	2.0	1.5	14

- For detached units, we allotted the highest points to returns and uptake at 35% and 30%, respectively. For an investor to recoup their investment in detached units, the most important factor would be how fast they can sell
- The lowest weighting was allotted to amenities, and distance from main business nodes at 5%, since investors prefer to buy cheaper land away from the CBD for development of low density units
- Karen and Runda Mumwe present the best opportunity for detached units development driven by relatively higher uptake and returns

Source: Cytonn Research

Cytonn REAL ESTATE

Residential Report Conclusion

Of the key metrics we use to measure performance, two are positive and two neutral, thus our outlook for the residential sector is positive

Residential Report 2017/2018 Conclusion				
Measure	**2017 Sentiment**	**2018 Sentiment**	**2017 Outlook**	**2018 Outlook**
Demand	• The housing deficit was estimated to be 1.9 mn units according to Cytonn Research with the demand is highest in the lower middle income segment of the market at 70.7%	• The Housing deficit in the Nairobi Metropolitan area continues to widen driven by rapid population growth at an average of 3.3%, compared to the national average of 2.6%, with 97.1% being lower middle-income and low end income earners, creating demand for affordable homes • Furthermore, the number of wealthy Kenyans has been on the rise and is expected to grow by 60.5% by 2022, creating demand for luxury homes	Positive	Positive
Credit	• There was a tough operating environment characterized by low credit supply, as a result of the implementation of the Banking Amendment Act 2015, which resulted in declining private sector credit growth from 25.8% in June 2014 to 2.1% as at May 2017	• The private sector credit growth has been on a continuous downward trend following the Bank Amendment Act of 2015, coming in at 2.1% as at April 2018 compared to a 5-year average of 14.0% between 2013 and 2018 • However, the introduction of innovative financial credit solutions such as the Kenya Mortgage Refinancing Company an National Housing Development Fund is expected to create a better credit financing environment for developers and end buyers	Negative	Neutral

Residential Report Conclusion

Of the key metrics we use to measure performance, two are positive and two neutral, thus our outlook for the residential sector is positive

Residential Report 2017/2018 Conclusion				
Measure	**2017 Sentiment**	**2018 Sentiment**	**2017 Outlook**	**2018 Outlook**
Infrastructure	• Improved infrastructural developments such as improved roads, the SGR, electrification, and ICT led to opening up of new development areas in areas such as Athi River, Mlolongo and Ruaka	• We have witnessed a continued provision of infrastructure in the recent years, as well as revamping of old roads. This has opened up new areas for investment and helped reduce development costs for developers	Positive	Positive
Performance	• The residential sector performance softened in 2017, with the total returns coming in 9.4% from 12.6% in 2016. The average rental yield was 5.6%, 0.4% points higher than the 5.2% recorded in 2016, however average price appreciation was 3.8%, 3.6% points lower than the 7.4% recorded in 2016 • We expected there to be price stagnation in selected markets with surplus supply	• The average return in the residential sector is 8.2%, a 1.2% decline from 2017 returns. The best-performing markets have returns of up to 13.9% which is high compared to returns from other asset classes such as the 10-Year Treasury Bond with a 13.2% yield	Neutral	Neutral

- **For the key metrics that have been used to determine the performance of the sector, two are positive, that is, demand and infrastructure; and two are neutral, that is, access to developer and end buyer credit, as well as the performance of the sector in terms of total returns, thus we have a positive outlook for the sector**
- **For apartments, the best opportunity is investment in areas such as Kilimani, Westlands and Ruaka driven by returns, and uptake as well as state of infrastructure and amenities; For detached units, the best opportunity is in areas such as Karen and Runda Mumwe, driven by uptake and the market returns to an investor**

Cytonn REAL ESTATE

Q&A