Cytonn 2024 Markets Outlook

Cytonn

Date: Monday, January 28th 2024

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I. Global Markets Outlook

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Global Market Summary

India is projected to record the highest growth rate in 2024 at 6.4%, with Kenya's projected growth rate coming in at 5.2%

	Cytonn Report: World GDP Growth Rates						
	Region	2019	2020	2021	2022	2023e	2024f
1.	India	4.0%	(6.6%)	9.1%	7.2%	6.3%	6.4%
2.	Kenya	5.0%	(0.3%)	7.6%	4.8%	5.0%	5.2%
3.	China	6.0%	2.2%	8.4%	3.0%	5.2%	4.5%
4.	Sub-Saharan Africa*	2.5%	(2.0%)	4.4%	3.7%	2.9%	3.8%
5.	Middle East, North Africa	0.9%	(3.6%)	3.8%	5.8%	1.9%	3.5%
6.	United States	2.3%	(2.8%)	5.9%	1.9%	2.5%	1.6%
7.	Brazil	1.2%	(3.3%)	5.0%	2.9%	3.1%	1.5%
8.	South Africa	0.1%	(6.3%)	4.7%	1.9%	0.7%	1.3%
9.	Japan	(0.2%)	(4.3%)	2.6%	1.0%	1.8%	0.9%
10.	Euro Area	1.6%	(6.1%)	5.9%	3.4%	0.4%	0.7%
	Global Growth Rate	3.1%	(3.2%)	6.2%	2.9%	2.6%	2.4%

****Including South Africa***

Source: World Bank

Factors Shaping Global Markets in 2024

A subdued Global trade, tightened monetary policy declining commodity prices and high debt levels are the factors that will likely shape Global Markets in 2024

Global Trade	• Global trade growth is expected to improve to 2.3% in 2024 as compared to a growth of 0.2% in 2023 and is expected to be driven by increased goods trade and growth in global output. However, the growth still remains subdued due to the persistent supply chain constraints worsened by the Russian-Ukraine conflict, and the tight monetary policies adopted by economies especially developed economies leading to massive capital outflows from emerging and developing economies (EMDEs)
Monetary Policy Stance	• We expect most of the central banks to continue raising their interest rates as they monitor inflation levels given the persistent high food and fuel prices especially in developing economies. Additionally, the interest hikes will be adopted driven by the need to anchor local currencies from aggressive currency depreciations following rates hikes in developed economies. Key to note, the US Fed maintained its tightened policy rate at 5.25%-5.50% noting that the policy was transmitting in the economy as inflation had slightly eased by 3.1% points to 3.4% in December 2023 from the 6.5% inflation recorded in December 2022.
Declining Commodity Prices	• Most of the commodity prices were on a downward trajectory in 2023 and are projected to ease further in 2024. Oil prices declined by 29.9% in 2023, a reversal from the 60.0% increase in 2022. Food prices fell by 10.1% in 2023 and are expected to decline by 1.0% amid the ample supplies with prices of oils & meals and grains declining by 22.1% and 13.0% in 2023 respectively an indication of better agricultural productions globally. However, Key upside risks to food prices include increases in energy costs, adverse weather events, further trade restrictions, and geopolitical uncertainty, as this will further constrain the supply chain and hence exert pressure on prices.

Factors Shaping Global Markets in 2024

A subdued Global trade, tightened monetary policy declining commodity prices and high debt levels are the factors that will likely shape Global Markets in 2024

High Public debt	• High debt levels especially in Emerging Markets and developing economies (EMDEs) are expected to persist in 2024 mainly on the back of widened current account deficits and surging debt service costs due to declining global trade and currency depreciation in most economies, coupled with tighter financial conditions undermining economic growth. Additionally, given the perceived interest hikes in 2024, especially in developed economies such as the US that have strengthened the dollar, global public debt is expected to increase significantly due to increase of debt servicing costs with a huge chunk of the external debt in most economies being dollar denominated.

Source: International Monetary Fund

Global Market Outlook

The global economy in 2024 is expected to be shaped by continued tightening of monetary policies in advanced economies on the back of elevated inflationary pressures

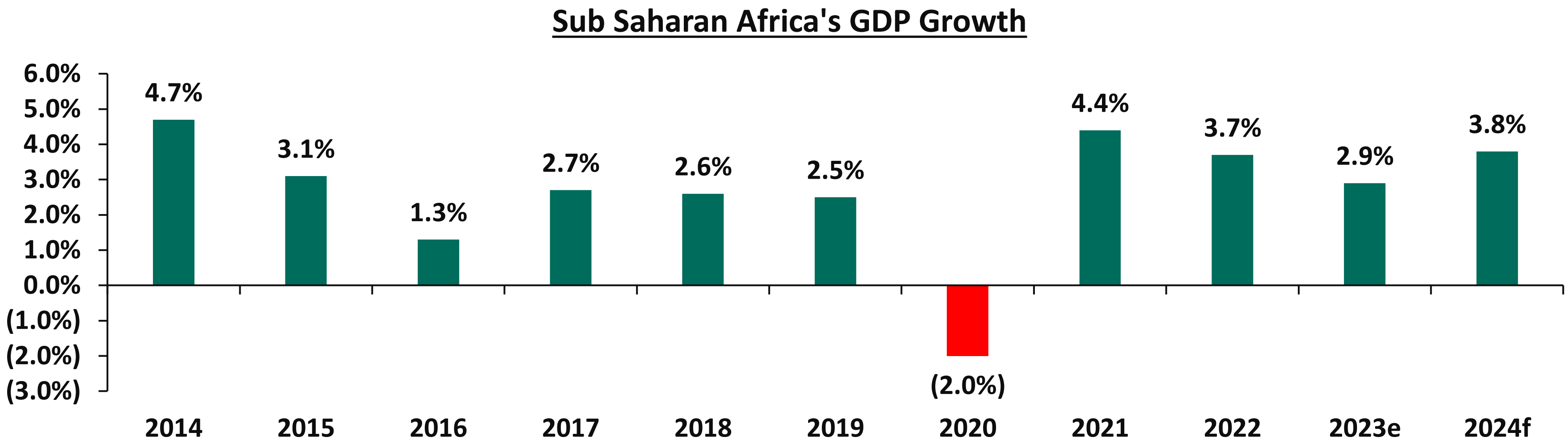
United States	• The US economy is expected to deteriorate to a 1.6% growth from the estimated 2.5% growth in 2023 due to the high food and energy prices that are still above the pre-pandemic levels, and worsened by the supply chain disruptions. Tightening of the monetary policy is expected to continue to anchor inflation to a range of 2.0% and this will weigh down on US activity in 2024
Eurozone	• The Eurozone growth is expected to record an economic growth of 0.7% in 2024, from the estimated growth of 0.4% in 2023. The slow growth in the are is attributable to the persistent high energy prices on the back of supply chain constraints especially for Natural gas. In addition, the lagged effects of past monetary tightening are expected to strain domestic demand, especially business investment, partly by reducing credit growth. However, Growth is projected to pick up to 1.6% in 2025, supported by a recovery in investment growth, especially as the European Union's NextGenerationEU (NGEU) funds lift public investment and help offset modest consolidation of national fiscal balances.
China	• The Chinese economy is expected to decline to 4.5% in 2024, from the 5.2% expected growth in 2023. The expected slowed growth in China is attributable to the Subdued investor sentiments which is expected to weigh on consumption as well as the persistent strains in the property sector due the decline in property prices and sales in the country. Further, the extreme weather conditions and prolonged effects of the real estate sector underperformance will be the key inhibitors of the 2024 economic growth

Source: World Bank

II. Sub Saharan Africa Regional Market Outlook

Regional GDP Growth

Sub Saharan Africa Region is expected to grow by 3.8% in 2024, according to the World Bank

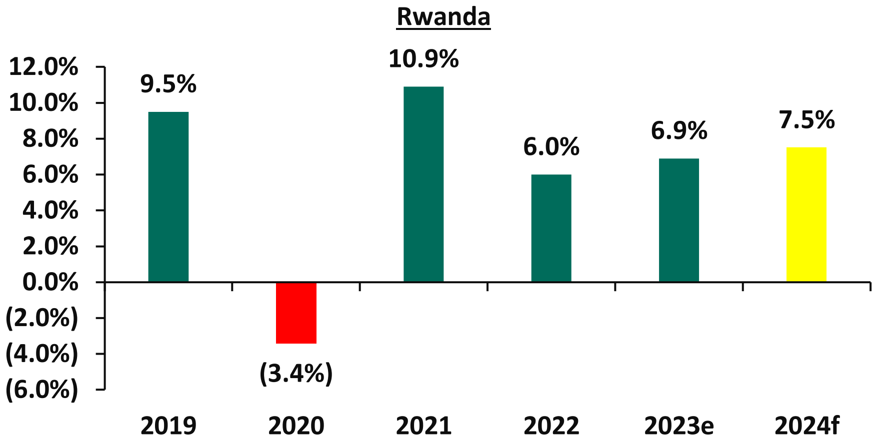


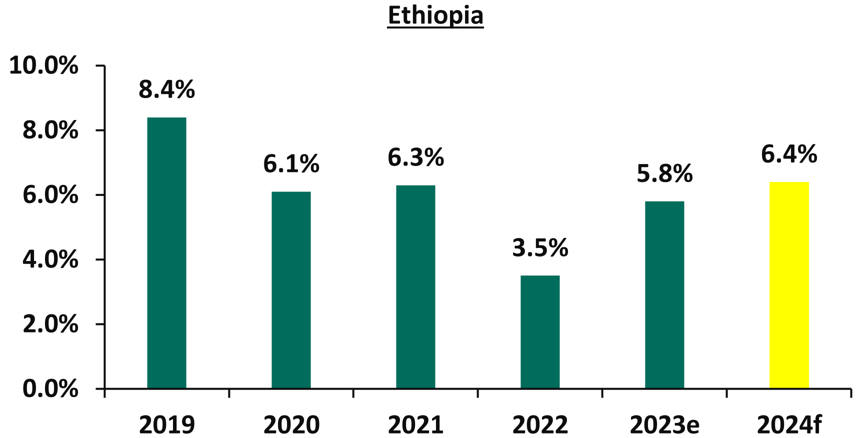
- The SSA region is expected to grow by 3.8% in 2024, 0.9% points higher than the estimated 2.9% in 2023. The slightly higher growth in 2024 is attributable to the easing inflationary pressures, reduction in prices of key imports such as fertilizers, metal and fuel, improved fiscal support and the expected increase in domestic demand
- The countries expected to drive growth in 2024 are Rwanda, Ethiopia, Kenya and Nigeria, with expected economic growth rates of 7.5%, 6.4%, 5.2% and 3.3%, respectively
- However, growth in the region is expected to be hampered by the high debt levels, stifled demand, persistent depreciation of local currencies as well as the increased cases of corruption in the region as indicated by the Corruption perceptions Index.

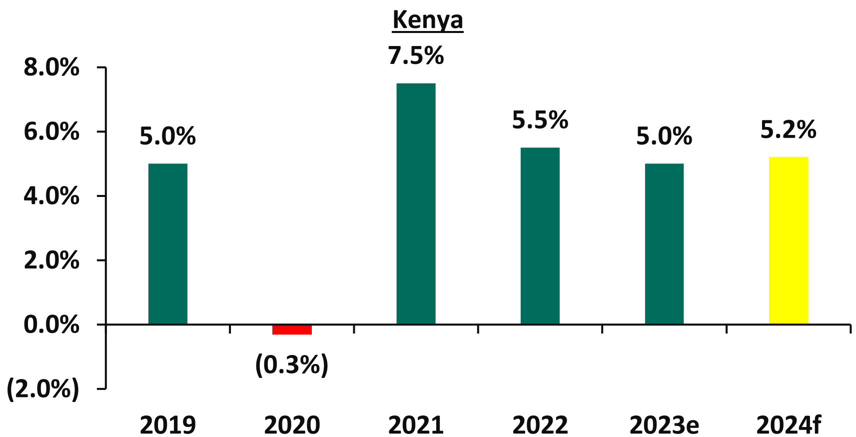
Source: World Bank

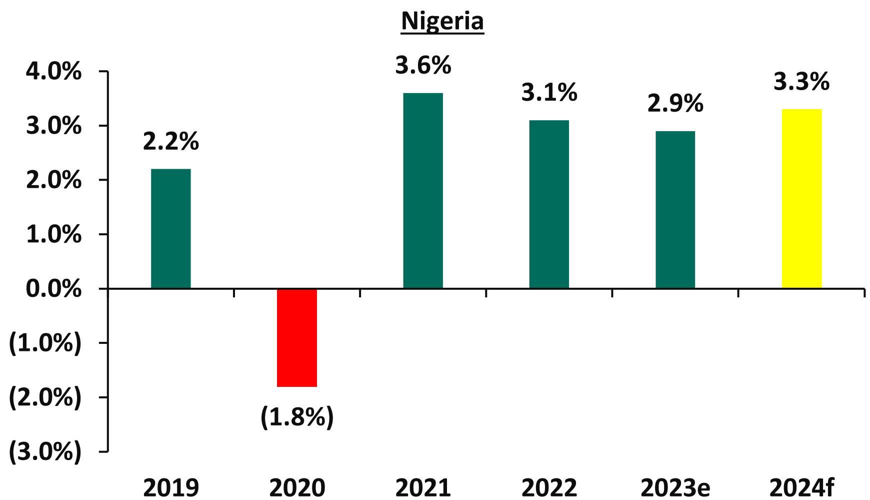
GDP Growth – Selected SSA Countries

Sub Saharan Africa Region is expected to grow by 3.8% in 2023, with the main countries driving growth being Rwanda, Ethiopia, Kenya and Nigeria









Source: World Bank

III. Kenya Macro Economic Outlook

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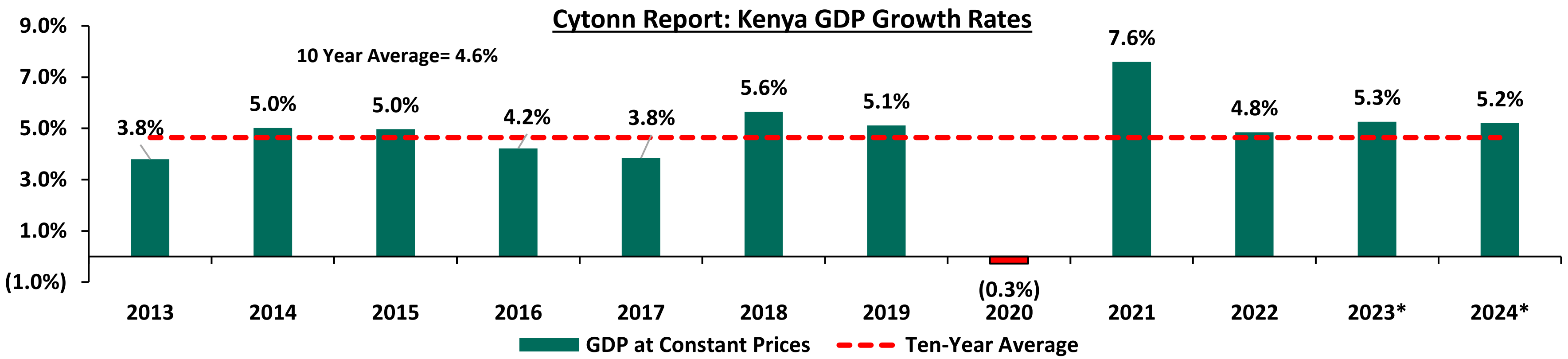
Kenya GDP Growth

Kenya's economy is projected to grow by 5.2% in 2024



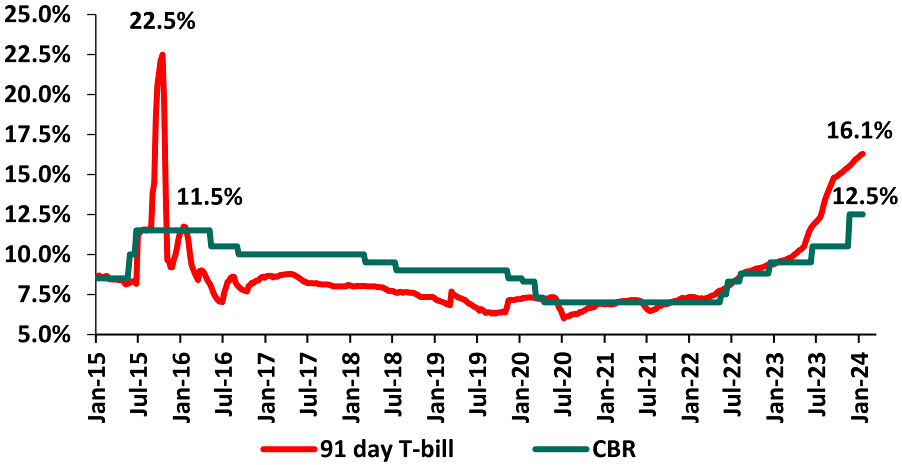
**Average estimate from IMF, World Bank, National Treasury, Cytonn estimate and S&P Global*

- We expect Kenya's 2024 GDP growth to range between 5.0% and 5.4%, driven by:
  i. Expected rebound in the agricultural sector, and robust performance in the services sector driven by growth in information and technology as well as accommodation and food services as a result of increased tourism
  ii. Continued recovery of the private sector with the renewed focus on Public-private Partnerships (PPP) to finance commercially viable projects expected to spur business growth. We also expect access to credit with the credit to the private sector to remain strong as banks embrace the risk-based lending model
- Key risks to the economic growth however include:
  i. Debt sustainability which continues to be a key concern, with the public debt to GDP ratio coming in at 72.6% as of September 2023,
  ii. Elevated inflation averaging 7.7% in 2023 and the sustained depreciation of the shilling prompting the aggressive monetary tightening currently at 12.5% stifling economic growth,

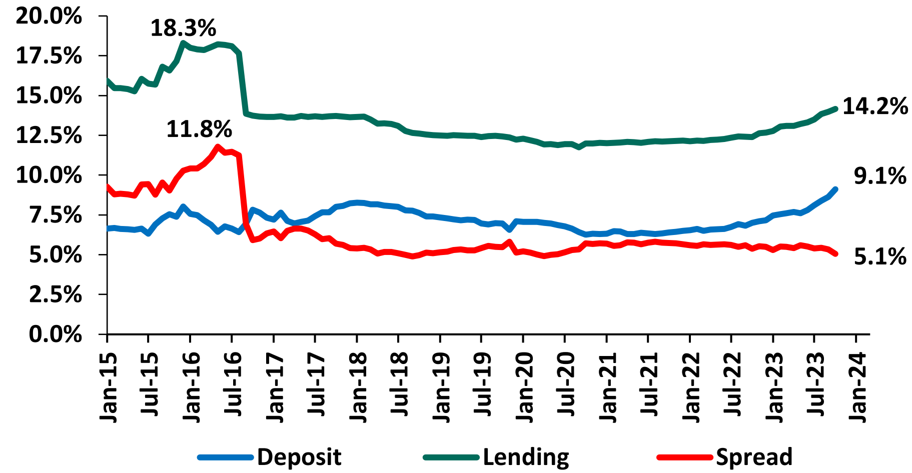
Interest Rates and Monetary Policy

We expect the interest rate environment to ease slightly in the Medium Term of 2024

Kenya
Central Bank Rate vs 91-day T-bill



Interest Rates:
Deposit, Savings and Lending Rates



- In 2023, the Monetary Policy Committee (MPC) raised the Central Bank Rate (CBR) by 375.0 bps from 8.75% in January to 12.5% in December, in a bid to anchor the inflation rate within the CBK's target range of 2.5%-7.5% from the 7.7% average registered in 2023 and also to support the Kenyan shilling which lost 26.8% of its value against the US Dollar during the year
- Going forward we expect the MPC to maintain its restrictive fiscal policy in the short term as it monitors the performance of the local currency and the country's inflation rate. However, we could see a downward revision of the CBR in the medium term if the performance of the Kenyan shilling stabilizes

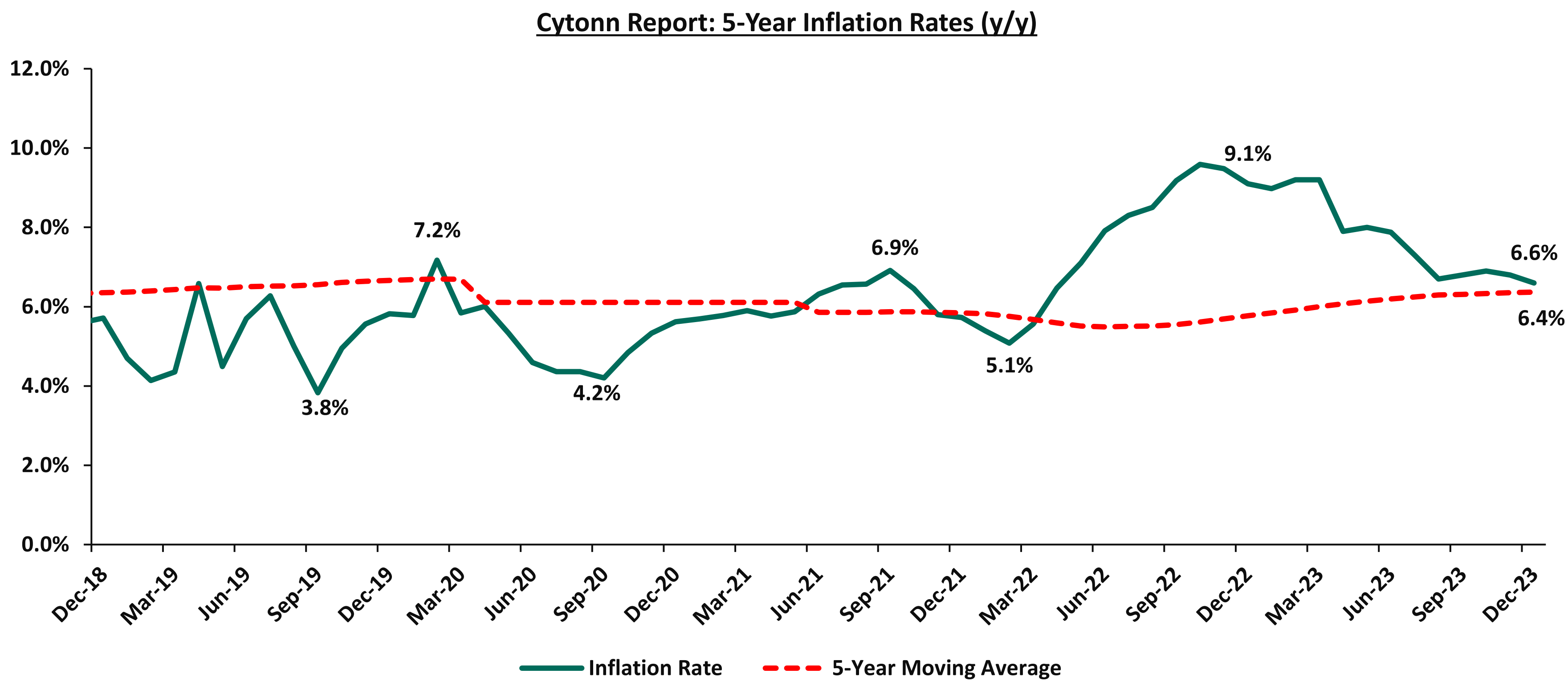
We expect monetary policy to EASE SLIGHTLY in the Medium Term in 2024

Source – Central Bank of Kenya

Inflation Forecast

Kenya's inflation rate is expected to average 6.9% in 2024, within the Government's target of 2.5%-7.5%

Kenya's Inflation Rate 2023

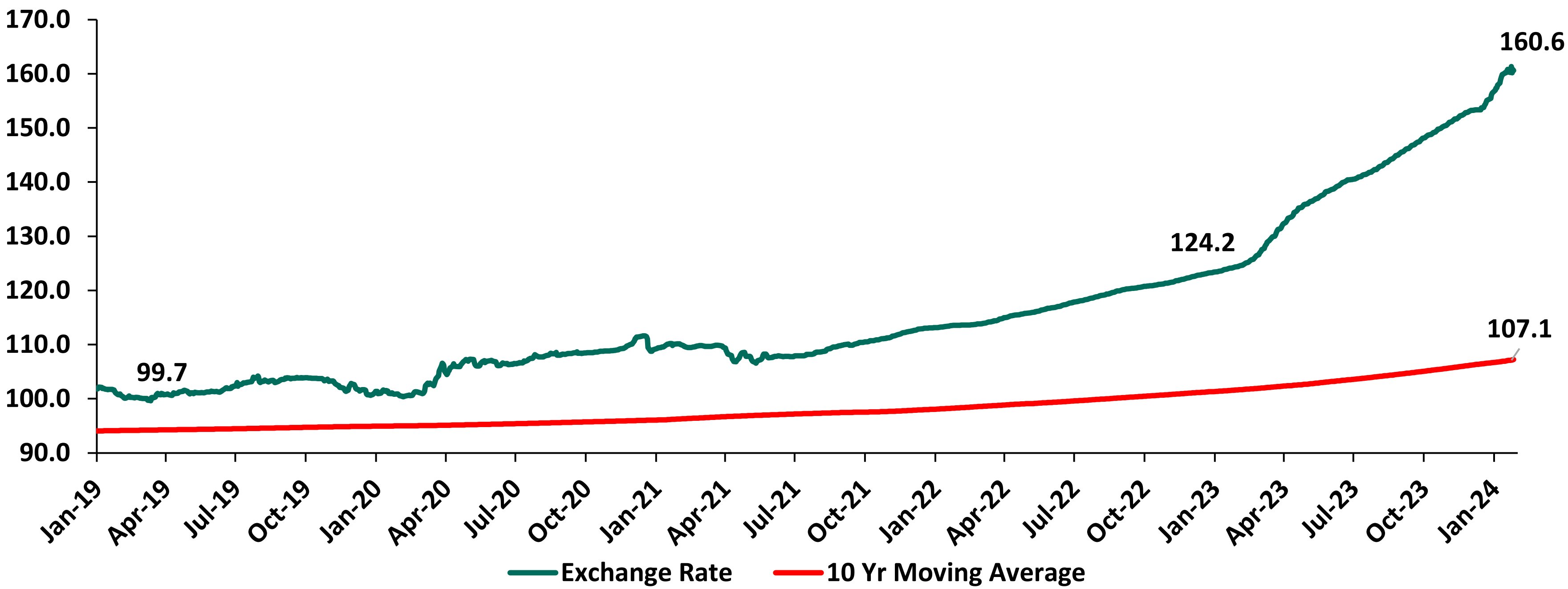


In 2024 we expect inflation to average 6.9%, within the Government target range of 2.5% - 7.5%

Exchange Rate

We expect the Shilling to trade within a range of Kshs 183.2 and Kshs 189.6 against the USD

Kshs. Vs USD



In 2024, <u>the shilling is likely to depreciate</u> due to:

i. ***Persistent current account deficit resulting in increased demand for foreign currency hence putting more strain on the local currency, and***

ii. ***The increasing debt servicing costs which continue to put pressure on forex reserves given the Eurobond coupons which are falling due ahead of the maturity of the 2014 issue in June 2024, and***

iii. ***Elevated risk of increase in global crude oil prices as a result of supply chain disruptions following the rising geopolitical tension in the Middle East,***

2024 Macroeconomic Outlook - Summary

2 indicators are negative, 4 are neutral and 1 is positive. Overall effect is Neutral

Macro-Economic & Business Environment Outlook		
Indicators	**2024 Outlook**	**Effect**
Government borrowing	• On the domestic front, we expect the government to borrow aggressively from the domestic market as it aims to plug in the fiscal deficit, which is projected to come in at Kshs 704.0 bn in the FY'2024/25 budget, 3.9% of the GDP. The government intends to plug this fiscal deficit through Kshs 326.2 bn in external financing and Kshs 377.7 bn in domestic borrowing. • In our view, the level of foreign borrowing will also increase in 2024 due to the following reasons; i) Need to service the upcoming maturities such as the 10-year USD 2.0 bn (Kshs 226.0 bn) Eurobond maturing in June 2024 (ii) Disbursement of concessional loans from the IMF under the EFF/ECF arrangement and the RSF programme, coupled with funding from the World Bank under the Development Policy Operation, and (iii) Disbursement of commercial loans from lenders such as the Trade & Development Bank and the African Development Bank.	**Negative**
Exchange Rate	• We expect the Shilling to range between Kshs 183.2 and Kshs 189.6 against the US dollar with a bias to a 16.4% depreciation by the end of the year	**Negative**
Interest Rates	• We expect the CBK to be maintain the tight monetary stance taken in 2023 through the short term of 2024 with the intention of anchoring the elevated inflation and supporting the depreciating shilling. . However, we expect the interest rate environment to stabilize in the medium term as the government meets the coupon payments and the eventual redemption of the 10-year Eurobond due in June 2024 with the support of concessional loans and commercial financing.	**Neutral**
Inflation	• We expect inflation to average 6.9% in 2024, falling within the government target range of 2.5% - 7.5%	**Neutral**
GDP	• We anticipate the economic growth to continue on its recovery trajectory in 2024, with the GDP growth rate ranging between 5.0% - 5.4% mainly supported by the continued recovery of the agricultural sector and a robust performance in the services sector driven by growth in information & technology as well as accommodation and food services. However, risks abound include the high risk of debt distress, elevated inflationary pressures, currency depreciation, and a restrictive monetary policy stance.	**Neutral**
Investor Sentiment	• We expect the low investor sentiments witnessed in 2023 to persist through the short term of 2024, mainly due to; i) Elevated inflationary pressures driven by high electricity costs and high fuel costs, and ii) Continued depreciation of the Kenyan currency as a result of increased dollar demand from importers. However, we expect investor sentiments to improve in the medium term as the country meets its coupon payments and the eventual maturity of the USD 2.0 bn Eurobond due in June 2024. Additionally, we expect the renewed focus on Public-private Partnerships (PPP) to finance commercially viable projects to spur growth in the private sector.	**Neutral**
Security	• We expect security to be maintained in 2024 with a stable political environment following the peaceful dispute resolution mechanisms adopted by the current regime and the opposition.	**Positive**

IV. Fixed Income Market Outlook

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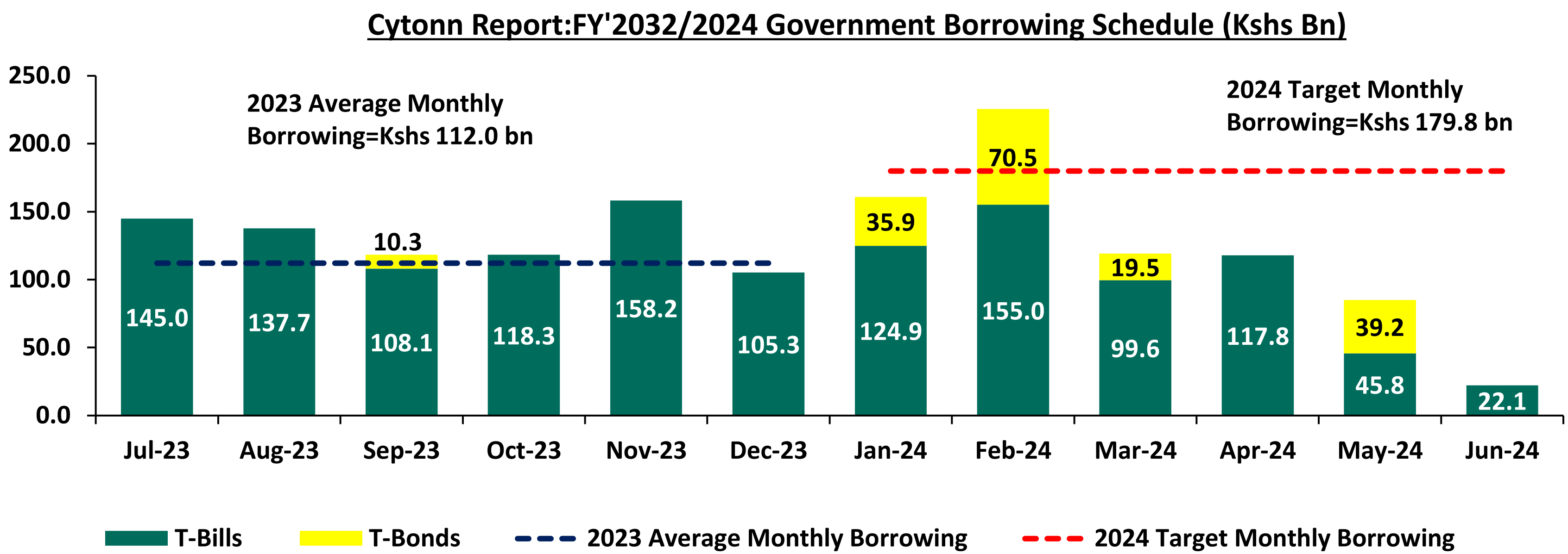
Government Domestic Debt

The government will have to borrow an average of Kshs 179.8 bn locally on a monthly basis to meet both its domestic borrowing target in the current fiscal year and maturity obligations

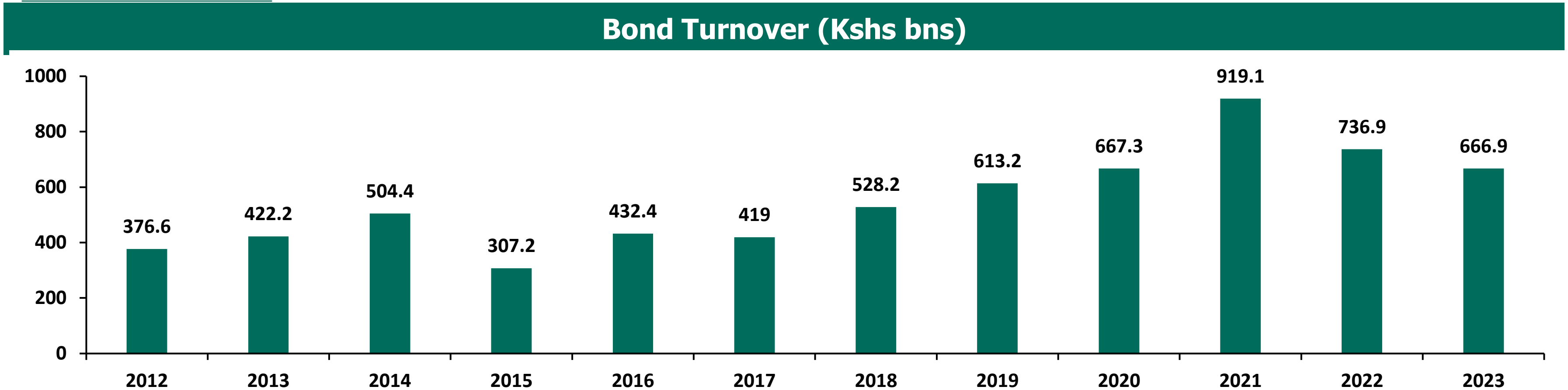


- The government is 34.0% behind of its prorated domestic borrowing target, having borrowed Kshs 181.2 bn domestically, against the pro-rated target of Kshs 274.5 bn
- Current Maturities = Kshs 634.6 bn
- Total Domestic borrowing target = Kshs 471.4 bn

Target Monthly Borrowing = Kshs 179.8 bn

Fixed Income Market Outlook

We expect secondary bond market activity and turnover to slightly increase in 2024 due to attractive interest rates and security offered by Government papers



- The secondary bond market recorded reduced activity with the turnover having declined by 9.5% to Kshs 666.9 bn, from Kshs 736.9 bn in 2022. This is partly attributable to local institutional investors shifting from the secondary market attributable to hiked interest rates in the primary market, coupled with higher interest rates in developed countries leading to capital flight by foreign investors and tightened liquidity in the market.
- We expect slightly increased activity in the secondary bond market boosted by the high yields offered to the government's papers

Source- Central Bank of Kenya (CBK)

Fixed Income Market Outlook, continued

Of the 7 indicators we track, 2 are positive, 3 are negative and, 2 are neutral. It is due to this that we find it prudent for investors to be biased towards short-term papers

Indicators	2024 Outlook	Our View
Domestic Borrowing	• We expect the government to borrow aggressively from the domestic market given that the external markets remain a challenging source of financing due to high interest rates, as it aims to plug in the fiscal deficit, which is projected to come in at Kshs 886.6 bn in the revised FY2023/24 representing 5.5% of the GDP, and decline further to an estimate of Kshs 692.5 bn, for the FY'2026/2027, translating to 3.1% of GDP. Domestic debt provides the government with a cheaper source of debt compared to foreign currency-denominated debts with higher interest rates and have currency risk attached to them. Owing to this, we expect the interest rate environment in the country to remain under an upwards pressure on the back of aggressive borrowing by the government and increased investor uncertainty, with the upcoming USD 2.0 bn Eurobond maturity in June, 2024.	Negative
Revenue Collection	• Revenues for the current financial year are projected at Kshs 3.0 tn with ordinary revenues at Kshs 2.6 tn. On the other hand, expenditures are projected at Kshs 4.0 tn with recurrent expenditures projected at Kshs 2.8 tn while development expenditures are projected at Kshs 762.6 bn. The fiscal deficit is therefore projected at Kshs 934.0 bn, excluding grants. According to KRA, Total revenue collected in for the last fiscal year amounted to Kshs 2.03 tn against a revised target of Ksh 1.98 tn, an outperformance of 102.8%. As of December 2023, total revenue collected amounted to Kshs 1,092.1 bn, equivalent to 84.8% of the prorated estimates of Kshs 1,288.4 bn. Total expenditure amounted to Kshs 1.4 tn, equivalent to 33.7% of the revised estimates of Kshs 4.3 tn, and is 67.3% of the prorated expenditure estimates of Kshs 2.1 tn • We expect revenue collection for FY'2023/2024 to improve given the current administration's focus on expanding the tax base to include the informal sector, increasing the exercise duty tax, and the roll-out of the e-TIMS system to improve VAT collection margins. However, the risks lie on the downside given that business environment remains subdued, underpinned by the aggressive depreciation of the Kenyan shilling that has suppressed business production levels, as well as inflationary pressures. As such, the low production performance will weigh down on the projected revenue performance	Positive
Monetary Policy	• The Central Bank is expected to maintain a tight monetary policy stance in the medium term with the intention of anchoring inflation which is currently on the upper bound of the preferred target range; as well as to help stabilize the Shilling exchange rate amid high global interest rates. Hence, we expect to see more upwards pressure on the interest rates as the government compensates investors for the increased risks posed by currency depreciation and inflationary pressures	Negative
Inflation	• We expect the annual average inflation rate to fall back into the middle within the government's target of 2.5%-7.5% coming in at an average of 6.0% as compared to 7.7% in 2023. We expect the decline in inflation to be driven by an expected stabilization in inflation both globally and locally, with most major economies like the U.S and UK almost achieving the 2.0% target rate, as the tightened monetary policy continues to take effect. Additionally, the ongoing reduction in global fuel prices is expected to aid in the ease in inflation globally. However, there remains threat of global inflation increasing in 2024 due to the ongoing unrest in the Middle East which could disrupt supply chains.	Neutral

Fixed Income Market Outlook, continued…

Our view is that investors, should be biased towards Short-term Fixed Income Instruments

Macro-Economic Indicators	2023 Outlook	Current View
Exchange Rate	• We project the Kenya Shilling to trade within the range of between Kshs 183.2 and Kshs 189.6 with a bias towards 16.4% depreciation against the USD in 2024, driven by the high global crude oil prices that will lead to increased dollar demand from oil and energy importers who will have to increase the amounts they pay for oil imports and hence depleting dollar supply in the market, high Fed rates and high debt servicing	Negative
Investor Sentiments	• Foreign investors remained net sellers in 2023, with a net outflow of USD 296.3 mn, compared to net outflows of USD 204.3 mn recorded in FY'2022. The foreign-investor outflows during the year can be largely attributed to investors fleeing emerging markets such as Kenya, to advanced economies such as United States and United Kingdom following interest rate hikes as well as increased concerns on macroeconomic deterioration. In 2023, the market valuation closed the year at a price to earnings ratio (P/E) of 5.1x, 23.9% lower than the 6.7x recorded at the end of 2022 and 57.7% below the 12-year historical average of 12.61 due to poor performance in the equities, with NASI, NSE20 and NSE 25 declining by 27.7%, 10.4% and 24.2%, respectively. The corporate earnings growth is expected to grow slightly due to an improved business environment, • We expect 2024 to register lower investor sentiments in the short term mainly due to continued depreciation of the Kenyan currency as a result of increased dollar demand from importers, especially for oil and energy sectors against a lower supply of hard currency and high debt servicing, owing to high Fed rate • Notably, yields on all Kenyan Eurobonds generally decreased in 2023, save for the USD 2.0 bn June maturity which increased by 0.6% points to 13.5%, pointing towards improved investor perception on Kenya partly attributable to the government's deliberate actions towards repaying the June maturity. Given the close maturity, the June maturity remains very sensitive to market speculation hence the increase in its yield.	Neutral
Security	• We expect security to be maintained in 2024 with a stable political environment, following the peaceful conclusion of general elections in 2022	Positive

Our view is that investors, should be biased towards:
SHORT-TERM FIXED INCOME INSTRUMENTS
Investors need to reduce duration risks associated with the long-term debt coupled with the relatively flat yield curve on the long-end due to saturation of long-term bonds

V. Kenya Equities Market Outlook

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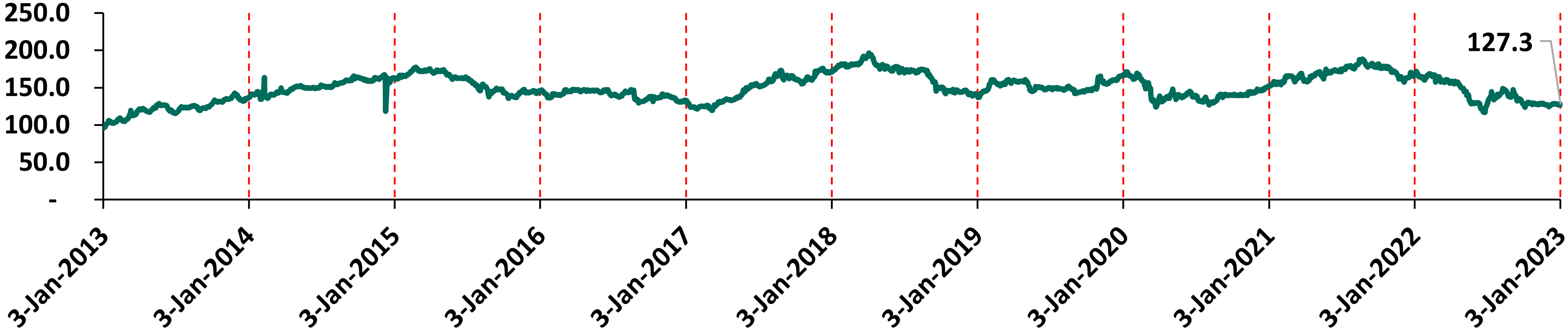
Kenya Equities Performance

NASI declined by 27.7% in 2023, compared to the 23.7% decline recorded in 2022

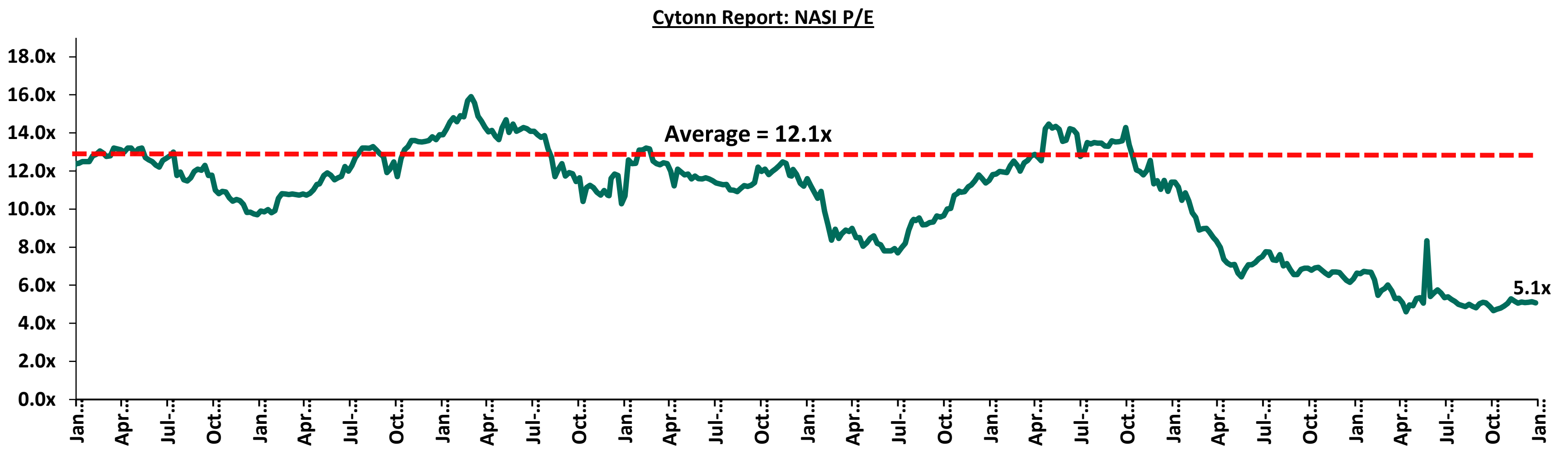
Annual NASI Performance									
2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
19.3%	(10.7%)	(8.4%)	29.1%	(18.0%)	18.7%	(8.4%)	9.5%	(23.7%)	(27.7%)

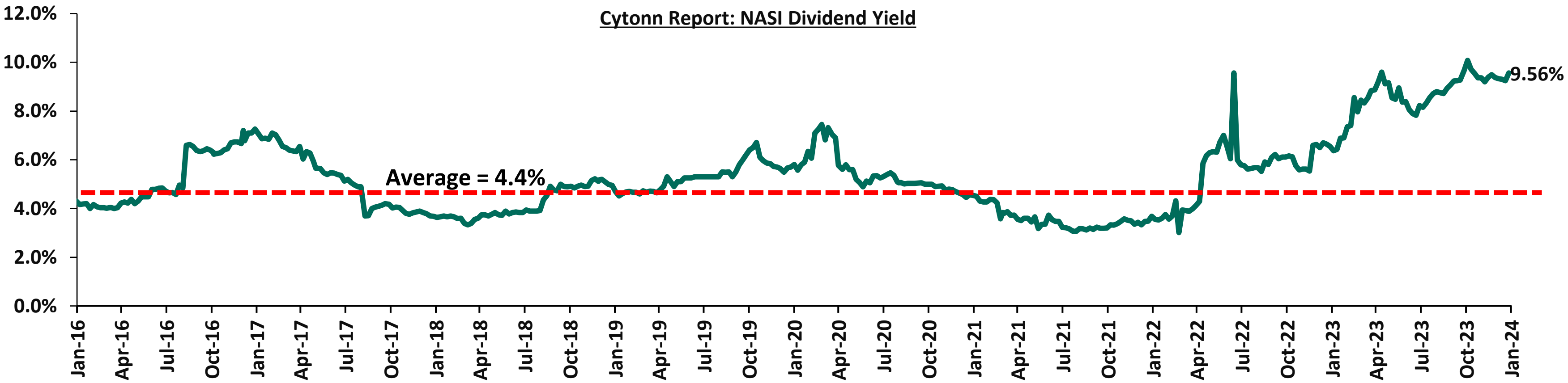


- The negative performance of NASI in 2023 was driven by losses recorded by large cap stocks such KCB Group, Safaricom, EABL, Equity Group, Diamond Trust Bank Kenya, Absa Bank, and Co-operative Bank Kenya of 42.9%, 42.2%, 32.9%, 25.3%, 9.6%, 6.1%, and 5.8% respectively, during the year, mainly due to uncertainty in the Kenyan equities markets, which resulted in massive capital outflows as investors sought less riskier investments such as government papers and other investment alternatives
- The losses were however mitigated by gains recorded by other banking stocks such as Bamburi Cement, Standard Chartered Bank, and Stanbic Bank of 14.0%, 11.7%, and 6.6%, respectively

NASI P/E and Dividend Yield

NASI is currently trading at a P/E of 5.1x, 58.0% below the historical average of 12.1x





Equities Outlook - Neutral for 2024

Of the 4 indicators we track for Equities market performance, 1 presents a positive outlook

Indicators	Outlook for 2024	Current View
Macro-Economic Environment	• We are projecting the economy to register a growth within the range of 5.0%-5.4% in 2024 supported by continued recovery of business activity, expected rebound in the agricultural sector, and robust performance in the services sector driven by growth in information and technology as well as accommodation and food services as a result of increased tourism. Additionally, the Central Bank of Kenya's Monetary Policy Committee decision to hike the Central Bank Rate (CBR) in a bid to curb inflation and maintain price stability is expected to curtail economic growth • The key downside to this growth shall be restrictive monetary policy stance, high risk of debt distress, elevated inflation, and local currency depreciation. However, we expect the agricultural sector to be supported by the long rains witnessed across the country at the end of the year, coupled with recent fiscal policies such as subsidizing costs of crucial farm inputs such as fertilizers that will enhance growth in the sector	Neutral
Corporate Earnings Growth	• We expect a slight improvement the listed sector's earnings growth in 2024, largely driven by the expected 5.0%-5.4% GDP growth and the improvement of the country's business environment. Corporate earnings growth is projected to come in at 12.5% for 2024 compared to the projected 10.6% growth in 2023, • Additionally, the growth in Corporate Earnings is expected to be boosted by the successful expansion of operations into Ethiopian telecommunication industry by Safaricom, which currently boasts of over 4.1 million customers as of September 2023 and continues to control the largest bourse in the Nairobi Stock Exchange, • Further, we anticipate growth in the banking sector's earnings as a result of expected increase in lending with the continued adoption of risk-based lending as well as revenue diversification strategies by banks	Neutral
Valuations	• With the market closing the year 2023 at a P/E of 5.1x, 57.7% below the 12-year historical average of 12.1x, and a dividend yield of 9.4%, 5.0% points above the historical average of 4.4%. This represents a potential upside of 32.2% compared to historical levels	Positive
Investor Sentiment and Security	• We expect the equities market to register muted foreign interest in 2024, attributable to the uncertainties in the Kenyan macro-economic conditions occasioned by the runaway currency depreciation. This caused high capital flights in 2023 as investors sought less risky investments such as government papers and other investment alternatives • On the flipside, we believe pockets of value still exist in the equities market due to the attractive valuations, with NASI trading below its historical average	Negative

Top 10 Stock Picks: 2024

KCB Group presents the highest upside at 62.7%

No.	Stock	Current Price*	Fair Price	Dividend Yield**	Total Upside	Recommendation
1	KCB Group***	20.4	31.2	9.8%	62.7%	Buy
2	Jubilee Holdings	180.8	260.7	6.6%	50.8%	Buy
3	Kenya Reinsurance	1.8	2.5	11.0%	49.7%	Buy
4	Sanlam	7.0	10.3	0.0%	46.6%	Buy
5	Diamond Trust Bank***	44.8	58.5	11.2%	41.9%	Buy
6	NCBA***	37.2	48.3	11.4%	41.5%	Buy
7	I&M Group***	17.5	22.1	12.9%	39.1%	Buy
8	ABSA Bank***	11.7	14.6	11.6%	36.9%	Buy
9	Stanbic Holdings	110.0	132.8	11.5%	32.2%	Buy
10	CIC Group	2.0	2.5	6.5%	30.8%	Buy
11	Standard Chartered***	160.3	185.5	13.7%	29.5%	Buy
12	Co-op Bank***	12.0	13.8	12.5%	27.5%	Buy
13	Equity Group***	37.1	42.8	10.8%	26.1%	Buy
14	Britam	5.1	6.0	0.0%	17.1%	Accumulate
15	Liberty Holdings	5.1	5.9	0.0%	16.5%	Accumulate

** Prices as at 27th January 2024*

*** Estimated Dividend Yield*

Our top stock picks for 2024 are based on a risk-adjusted return basis. We took into account banking & insurance stocks with medium risk levels, are liquid and have strong fundamentals

Top Stock Pick: 2024

We recommend investors to take a BUY position on Safaricom

- In their H1'2024 results, Safaricom recording an increase in core earnings per share of 10.0% to Kshs 0.9, from Kshs 0.8 in H1'2023. The gain was largely attributable to a 9.9% increase in mobile service revenue to Kshs 151.7 bn from Kshs 138.1 bn recorded in H1'2023, which contributed to the 7.3% increase in total revenue to 164.6 bn from 153.4 bn in H1 2023. Its Ethiopian subsidiary generated Kshs 2.0 bn in mobile service revenue and 2.9 bn in total revenue. The Ethiopian subsidiary incurred operating expenses amounting to Kshs 10.4 bn, representing 27.7% of the Group's total operating expenditure of 37.7 bn
- We expect Safaricom to register muted earnings growth in 2024 attributable to the tough macroeconomic environment and the continued support to the relatively new Ethiopian subsidiary. On the flipside, revenue growth is expected to be supported by increased service revenue, which also recorded a 9.9% y/y gain to Kshs 159.1 bn, from Kshs 144.8 bn recorded in H1'2023 with MPESA revenue and mobile data revenue increasing by 16.4% and 17.7%, respectively
- In 2023, Safaricom share price registered a 42.2% decline, mainly attributable to increased sell off by foreign investors as they exited the market due to hiked interest rates in developed economies such as United States making dollar investments more appealing and thus lowering their appetite for risky investments in emerging markets such as Kenya. However, Safaricom continued to exert its dominance in the bourse, with its market cap closing the year at 39.0% of the entire bourse as at 30th December 2023, a decline from 49.6% recorded in 2022
- Given the firms strong fundamentals and expansion to Ethiopia, we remain positive on Safaricom. We recommend investors to take a **BUY** position on the stock based on sound fundamentals

Equities Market Outlook

We are "Neutral" on the Equities markets in the short term due to the current adverse operating environment and huge foreign investor outflows

- We are **Positive** for 1 indicator that we track which is;
    i. Valuations
- We are however **Neutral** for 2 indicators we track which include;
    i. Macro Economic Environment,
    ii. Corporate Earnings Growth, and
- We are also Negative for 1 indicator that we tract that is;
    i. Investor Sentiment and Security,
- We are "NEUTRAL" on equities for investors as the Neutral outlook on the macro-environment, corporate earnings growth and subdued investor confidence and security could inhibit the market's performance

We have a ''NEUTRAL" outlook on the Kenyan Equities market in the short term. However, we maintain our bias towards a "BULLISH" equities markets in the medium to long term, with the expectations of a slower growth in corporate earnings and the cheap valuations currently in the market..

VI. Real Estate Market Outlook

Cytonn

2024 Residential Sector Outlook (Demand)

Of the five factors we track on the residential demand, one positive, three are neutral and one is negative, thus our outlook for demand in 2024 is neutral with a bias on the positive

Cytonn Report: Residential Demand Outlook		
Metric	**2024 Outlook**	**Effect**
Demographics	• According to World Bank Kenya has relatively high urbanization and population growth rates averaging 3.7% and 1.9% respectively, compared to the global averages of 1.5% and 0.8%, respectively, as of 2022. This will continue to provide sustained demand for more housing units in the country	**Positive**
Infrastructure	• The government aims at completing various infrastructural projects in the country including Riruta – Lenana – Ngong Railway Line, phase I of Nairobi Railway City, the Meter Gauge Railway (MGR) Link from Mombasa SGR Terminus to Mombasa MGR Station, and the Railway Bridge across Makupa Causeway • Going by the Draft 2024 Budget Policy Statement the government's Infrastructure, Energy, and ICT allocation for the FY'2024/2025 is forecasted to be Kshs 505.7 bn, representing a 8.0% increase from Kshs 468.2 bn FY'2023/2024 . With the ongoing construction projects such as Kenol-Marua Highway, Lamu-Garissa Highway, the sector is set to witness increased investments. However, recent budgetary cuts to the state department for housing, and a general reduction in the country’s development expenditure will potentially hinder optimal performance of the sector	**Neutral**
Investor Returns	• Residential sector in 2023 recorded a slight decrease in average total returns to 6.1%, from 6.0% in 2022. This is linked to the decrease in price appreciation at 0.5% in FY’2023, 0.6%-points lower than the 1.1% appreciation recorded in FY’2022. Investors also increased their asking rents in order to hedge themselves against the tough economic times • We expect more investments in the lower mid-end Suburbs towns with average total returns of 6.1% performing better than detached units average of 5.8%. Apartments in Waiyaki Way, South C, and Imara Daima recorded the highest returns at 7.5%, 7.2%, and 7.0% respectively, higher than the market average of 6.3%	**Neutral**

2024 Residential Sector Outlook (Demand), cont'd…

Of the five factors we track on the residential demand, one positive, three are neutral and one is negative, thus our outlook for demand in 2024 is neutral with a bias on the positive

Purchasing Power	• As the tough macro-economic environment persists evidenced by the continuous depreciation of the Kenyan Shilling against the United States dollar as well as select currencies, and inflation rises, buyer's purchasing power will continue to be weakened. This will weigh down the performance in the residential sector by hindering uptake	**Negative**
Access to Credit	• The government has continued to promote access to affordable credit through the Kenya Mortgage Refinance Company (KMRC) which has been crucial in providing Kenyans with low-cost loans increasing home ownership • However, lenders continue to ask for more collateral against loans advanced to the real estate sector due to the increase of Non-performing loans. In Q3'2023 the Non-Performing loans advanced to the real estate sector stood at Kshs 97.9 bn compared to Kshs 96.0.0 bn in Q2'2022, which is a 2.0% increase, developers are struggling to payback their loans	**Neutral**

2024 Residential Sector Outlook (Supply)

Of the five factors that we expect to shape residential supply, one is negative, three are neutral, and one is positive, and thus our outlook is neutral

Cytonn Report: Residential Supply Outlook		
Metric	**2024 Outlook**	**Effect**
Developer Returns	• In 2023, the residential sector recorded a slight decrease in performance coming in at 6.1% from 6.2% recorded in 2022.The performance was attributed to a decrease in the residential average y/y price appreciation which came in at 0.5% in FY'2023, 0.6%-points lower than the 1.1% appreciation recorded in FY'2022. The average rental yield came in at 5.5% in FY'2023, recording a 0.4%-points uptick from the 5.1% rental yield recorded in FY'2022. This was driven by an increase in the average rent per SQM by 10.9% to Kshs 599, from Kshs 540 recorded in FY'2022 • Going forward, we expect developers will eye on lower-middle segment offering an average total return of 6.1% and 6.6% for detached and apartment units respectively. This is attributable to relatively higher average price appreciation of 0.8% for both, 0.3%-points higher than the detached market average appreciation of 0.5% • Conversely, developers' activities are expected to be hit by the soaring cost of constructions amid a rise in the prices of key construction materials	**Neutral**
Access to Financing	• Accessing funding remains a hurdle for developers in Kenya due to the underdeveloped capital markets. Since the inception of the investment regime in 2013, only one Real Estate Investments Trust (REIT) has been listed in the country. With regards to the above, we note that the REIT's manager has planned to delist it from the main investment market segment of the Nairobi Securities Exchange (NSE) during the year. Subsequently, Fahari I-REIT will be quoted on the Unquoted Securities Platform, joining the Acorn REITs. As a result, majority of developers heavily depend on traditional funding sources like banks which accounts for 95.0%, unlike 60.0% in developed countries • In 2024, we expect developers will continue to seek alternative financing options to fund their projects including equity financing, seeking for Public-Private Partnerships (PPPs), pushing for off-plan sales as conventional lending rates continue to increase	**Neutral**

2024 Residential Sector Outlook (Supply), cont'd…

Of the five factors that we expect to shape residential supply, one is negative, three are neutral, and one is positive, and thus our outlook is neutral

Development Costs	• In 2024, developers will be hit by the rising cost of major construction materials such as cement and steel which registered a 27.7% increase in FY' 2023, majorly driven by depreciation of the Kenyan Shilling against major currencies such as the United States dollar as well as the prevailing inflationary pressures which saw the cost of construction rise to an average of Kshs 71,200 per SQM in 2023, from Kshs 56,075 per SQM in 2022	**Negative**
Infrastructure	• According to the Draft 2024 Budget Policy Statement, the government's Infrastructure, Energy, and ICT allocation for the FY'2024/2025 is forecasted to be Kshs 505.7 bn, representing a 8.0% increase from Kshs 468.2 bn FY'2023/2024. With the increased funding we expect the government to complete various infrastructural projects in the county and rehabilitation of rehabilitate roads, bridges, railways, airports, and affordable housing units, among others. • Infrastructural development will be a big boost in the residential sector, driving the cost of properties up as well as encouraging developers to commit their resources to development projects. Some of the projects in the pipeline such as; Riruta – Lenana – Ngong Railway Line, phase I of Nairobi Railway City, the Meter Gauge Railway (MGR) Link from Mombasa SGR Terminus to Mombasa MGR Station, and the Railway Bridge across Makupa Causeway • However, recent budgetary cuts to the state department for housing, and a general reduction in the country's development expenditure will potentially hinder optimal performance of the sector	**Neutral**

2024 Residential Sector Outlook (Supply), cont'd…

Of the five factors that we expect to shape residential supply, one is negative, three are neutral, and one is positive, and thus our outlook is neutral

Government Incentives	• The government has made efforts to developers in a bid to reduce house deficit in the country, Some of the incentives initiated by the government includes; i) reduction of corporate tax for developers who build a minimum of 100 low cost units from 30.0% to 15.0% under affordable housing program, ii)) exemption of VAT on importation and local purchase of goods for the construction of houses under the affordable housing scheme, iii) forging for reforms in property registration in order to fast track approvals for developers in the affordable housing program, iv) increased efforts by the government to provide land to county governments for construction of affordable housing units, v) reduced tariffs on imported inputs for the construction of housing under the affordable housing scheme, (vi) VAT exemptions for construction inputs for affordable housing program, and, (vii) exemption from 4.0% (urban areas) and 2.0% (rural areas) stamp duty for first time buyers of houses under the affordable housing scheme • These incentives will go a long way in promoting home ownership as well solving housing deficits in the country	**Positive**

2024 Residential Sector Outlook, cont'd…

Our outlook on residential sector performance in 2024 remains NEUTRAL

Cytonn Report: Residential Performance Review and Outlook			
Theme	**2023 Performance**	**2024 Outlook**	**Outlook**
Residential Sector	• During FY'2023, the NMA residential sector recorded a slight downtrend in performance, with the average total returns to investors coming in at 6.1%, a 0.1%-point decline from 6.2% recorded in FY'2022 • On the other hand, the average rental yield came in at 5.5% in FY'2023, recording a 0.4%-points uptick from the 5.1% rental yield recorded in FY'2022. This was driven by an increase in the average rent per SQM by 10.9% to Kshs 599, from Kshs 540 recorded in FY'2022, as landlords sought to cover increased expenses	• The demand for housing is expected to persist in 2024, driven by positive population demographics. Increased efforts by the government to implement its affordable housing agenda is expected to spur further growth in the sector. Additionally, expansion and development of infrastructural projects is set boost the sector, as well as efforts by the government to avail low cost loans to Kenyans through Kenya Mortgage Refinance Company (KMRC) which is poised to enhance homeownership. • Conversely, we expect the sector to be weighed down by the prevailing tough economic environment	**Neutral**
Our outlook remains neutral for the residential sector. On the supply side, our outlook is neutral as we expect the government to intensify its affordable housing activities country wide as it aims to deliver 250,000 units annually. We also expect the private sector to play a crucial rule in supplementing government efforts to bridge the housing deficit. In addition, infrastructural development will play a pivotal role in supporting the development of residential projects. On the demand side, our outlook remains neutral, owing to the tough macro-economic conditions currently being experienced in the country which has weakened buyers' purchasing power			

2024 Commercial Office Sector Outlook

We expect the sector to remain stable

Cytonn Report: Summary of Commercial Office Returns in Nairobi Metropolitan Area (NMA) Over Time											
Year	**FY'17**	**FY'18**	**FY'19**	**FY'20**	**FY'21**	**FY'22**	**FY'23**	**Forecasted Annualized Change**	**2024F**	**Reason for Forecast**	**Outlook**
Occupancy (%)	82.6%	83.3%	80.2%	77.7%	77.6%	79.4%	80.3%	**1.1% points**	**79.2%**	We expect 1.1% points decrease in occupancy rates mainly attributable to an increased incoming supply compared to a similar period last year. Moreover, the existing oversupply estimated at 5.8 mn SQFT in the Nairobi Metropolitan Area (NMA) is expected to further weigh down on the absorption rates. However, we expect occupancy levels to be boosted marginally the entry of multinationals companies entering the country, and increasing number of start-ups	**Negative**
Asking Rents (Kshs/Sqft)	101	101	96	93	94	96	103	**3.3%**	**106**	In FY'2024, we expect a 3.3% increase in asking rents attributed increased preference by landlords to prefer rent payment in US dollars, as well as expected increase in supply of prime offices fetching higher rents such as the Purple Tower, Bishop's Road and The Atrium in Westlands	**Positive**
Average Prices (Kshs/Sqft)	12,649	12,573	12,638	12,280	12,106	12,223	12,673	**1.0%**	**12,803**	Asking prices are expected to realize a 1.0% increase as construction prices continue to soar. However, the prevailing tough macro-economic conditions evidenced by factors such as sustained depreciation of the Kenyan shilling against major currencies and rising inflation may negatively affect demand for office space as businesses may decide to downsize in order to cut costs	**Neutral**
Average Rental Yields (%)	7.9%	8.1%	7.5%	7.0%	7.3%	7.6%	7.7%	**0.2% Points**	**7.9%**	We expect the yields to realize a slight improvement of 0.2% points attributed to the expected improvements in the overall rental rates. However, we expect the projected decline in occupancies to weigh down the sector's optimal performance	**Neutral**

2024 Commercial Office Sector Outlook, cont….

We expect a slight increase in performance by 0.2% points

Cytonn Report: Retail Performance Review and Outlook			
Theme	2023 Performance	2024 Outlook	Outlook
Retail Sector	• In FY'2023, The average rental yield remained stable, registering 0.1% points increase to 7.7% in FY'2023 from 7.6% recorded in FY'2022, due to improved rental and occupancy rates. • The improvement in performance was mainly driven by; high number of Grade A offices which are highly preferred especially by multinational companies, high demand for quality offices by embassies, international organizations and multinational companies in these areas and availability of infrastructural capital such as Nairobi Expressway which has increased accessibility to areas such as Westlands.	• We expect a slight increase in performance by 0.2% points, attributable to the expected increase in the overall rental rates. We expect the improved performance to be supported by; i) increased entry of multinationals companies into the country, ii) Kenya's continued recognition as a regional business hub which continues to attract multinational companies expanding into the continent, iii) increasing number of start-ups, iv) gaining traction in co-working spaces and, v) landlords growing preference for dollar-denominated rental prices, in efforts geared towards mitigating forex losses. • However, we expect that an increased incoming supply compared to a similar period last year and the existing oversupply estimated at 5.8 mn SQFT in the Nairobi Metropolitan Area (NMA) will weigh down on the sector's performance by stifling absorption rates	**Neutral**

From the above, our overall outlook for the Nairobi Metropolitan Area commercial office sector is NEUTRAL. We expect the sector to remain stable with a slight improvement attributable to: i) increased entry of multinationals companies into the country, ii) Kenya's continued recognition as a regional business hub which continues to attract multinational companies expanding into the continent, iii) increasing number of start-ups.We expect that an increased incoming supply compared to a similar period last year and the existing oversupply estimated at 5.8 mn SQFT in the Nairobi Metropolitan Area (NMA) will weigh down on the sector's performance by stifling absorption rates

2024 Retail Sector Outlook

We expect retail space supply to increase to 8.6 mn per SQFT in 2024 due to new developments

Cytonn Report: Nairobi Metropolitan Area (NMA) Retail Sector Performance 2017-2024F											
Item	FY'17	FY' 18	FY'19	FY'20	FY'21	FY'22	FY'23	Forecasted Annualized Change	2024F	Reason for Forecast	Outlook
Asking Rents (Kshs/SQFT)	185	178	176	169	170	174	182	1.7%	185	We expect asking rents to increase by 1.7% mainly driven by enhanced business confidence among investors, influencing demand for available retail spaces and consequently leading to higher rental rates. This is expected to coincide with the ongoing economic recovery, moving towards pre-COVID-19 levels. Furthermore, prime retail locations like Kilimani, Karen, and Westlands, where rents are quoted in dollars, are expected to observe continuous increases when converted to Kenyan currency, attributed to the persistent depreciation of the Kenyan shilling against the Dollar.	Positive
Supply in Nairobi (mn SQFT)	6.2	6.5	7.3	7.3	7.3	8.2	8.3	3.1%	8.6	We expect retail space supply to increase to 8.6 mn per SQFT in 2024 with the addition of an estimated 42,977 SQM through malls such as The Cove in Lavington, Lana Plaza in Kileleshwa, Park Place Avenue in Parklands and Beacon mall in Upperhill. Other notable developments expected to be delivered into the market outside of the NMA include Promenade mall in Nyali and Nyali Bazaar in Mombasa	Positive

2024 Retail Sector Outlook

We expect an increase in rental yields by 0.3% in 2024 due to increased rental charges for spaces

Cytonn Report: Nairobi Metropolitan Area (NMA) Retail Sector Performance 2017-2024F											
Item	FY'17	FY' 18	FY'19	FY'20	FY'21	FY'22	FY'23	Forecasted Annualized Change	2024F	Reason for Forecast	Outlook
Occupancy (%)	80.3%	79.8%	75.9%	75.2%	76.8%	77.6%	79.3%	**0.9% points**	**80.2 %**	The current oversupply of 3.0 mn SQFT, coupled with escalating rental charges on retail properties, a challenging economic environment marked by tax hikes on goods and businesses, and increased Monetary Policy Committee (MPC) rates implemented by the government, may prompt businesses to consider downsizing their operational spaces or adopting a more conservative approach to expansion. This is expected to exert pressure on the occupancy of physical spaces within the formal retail sector. However, there remains a positive outlook with the anticipation of continued expansion and new entries by both local and international retailers. This optimism stems from the growing operations and the identification of opportunities in untapped regions, influencing occupier demand positively.	**Neutral**
Average Rental Yields	9.6%	9.0%	7.8%	7.5%	7.8%	7.9%	8.3%	**0.4% Points**	**8.6%**	We expect a slight increase in rental yields by 0.3% points as a result of increased rental charges of retail spaces and the aggressive expansion by retailers taking up new and previously occupied spaces. Furthermore, infrastructure developments opening areas for investments, and positive demographics are poised to support sector performance. However, oversupply, increased adoption of e-commerce, tougher economic environment for businesses, and presence of informal retail spaces are expected to undermine the performance of the sector in turn affecting rental yields of the sector.	**Neutral**

2024 Retail Sector Outlook, cont….

We have a NEUTRAL outlook for the sector with performance expected to be cushioned by continuous expansion campaign of both local and foreign retailers

Cytonn Report: Retail Performance Review and Outlook			
Theme	2023 Performance	2024 Outlook	Outlook
Retail Sector	• The sector recorded 0.4% points increase in average rental yields to 8.3%, from 7.9% in 2022. Average rents and occupancies also increased by 0.9% and 1.8% points to Kshs 177 per SQFT and 79.2%, respectively • The improved performance was due to; i) an increased presence of quality retail spaces which attract high rents such as the Global Trade Centre (GTC) in Westlands, ii) aggressive expansion by local and international retailers, iii) increased infrastructure developments promoting accessibility to retail centres, and, iv) positive demographics facilitating the demand for spaces, goods and services	• We expect a slight increase in rental yields by 0.3% points as a result of increased rental charges of retail spaces and demand for existing supply amid the aggressive expansion by retailers taking up new and previously occupied spaces, infrastructure developments opening areas for investments, and positive demographics. However, oversupply of physical space, increased adoption of e-commerce, and a tougher economic environment for businesses are expected to undermine the performance of the sector in turn affecting rental yields of the sector during the year • Investment opportunity lies in areas such as Westlands, Karen, and Kilimani which continue to record impressive returns. This is in addition to the undersupplied regions of the country such as Mount Kenya, western and the Coast	Neutral

we have a NEUTRAL outlook on the retail sector's performance which is expected to be driven by; i) continuous aggressive expansion by both local and foreign retailers taking up new and existing spaces, ii) progressive developments in public infrastructure of roads and railway projects boosting accessibility in new areas for investments, and, iii) positive demographics facilitating increasing demand. However, the slow growth in the sector is expected to be facilitated by some negative factors such as; i) existing oversupply at approximately 3.0 mn SQFT in NMA and the rest of the Kenyan retail sector totaling to approximately 1.7 mn SQFT, ii) growing adoption of e-commerce by most retailers which continues to undermine occupier demand, and, iii), limited access and expensive financing from financial institutions to cater for developments, and improvement in operations towards technological levels by small and medium-sized enterprises to enhance their efficiency

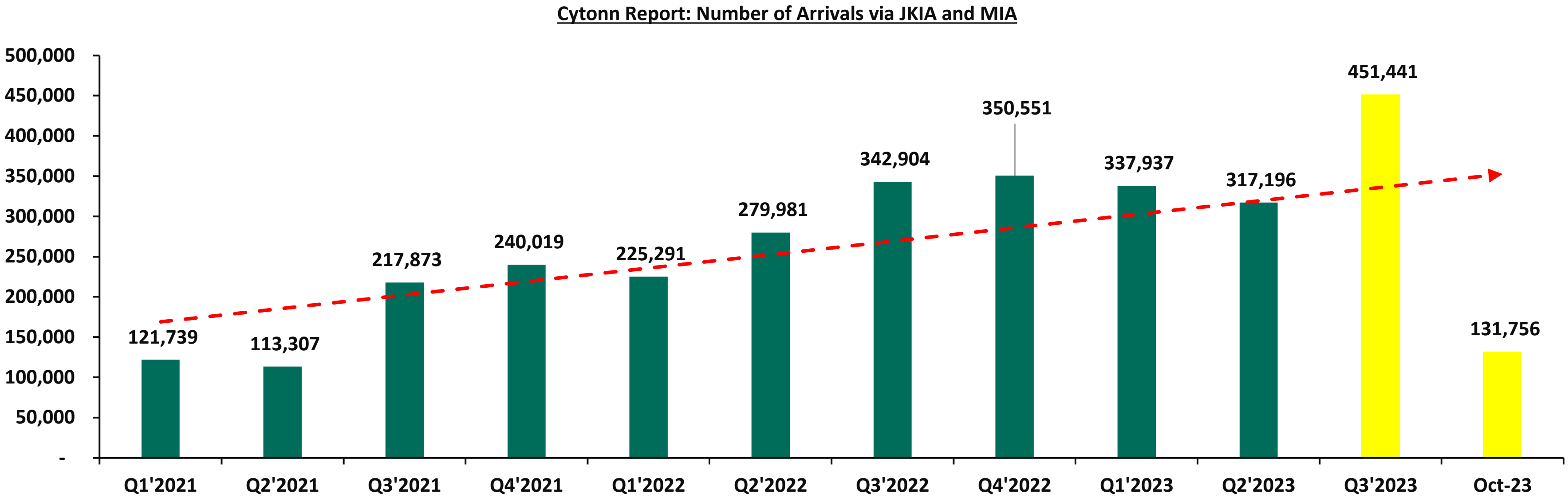
2024 Hospitality Sector Outlook

Domestic tourism is among the key 9 initiatives of the Tourism Strategy 2021 – 2025

- In 2023, the hospitality sector achieved notable advancements, as indicated by the Leading Economic Indicators (LEI) October 2023 report. The report highlighted an upswing in international tourist arrivals, the expansion of operational hotels, increased bed occupancies, and elevated hotel bookings. This positive trend underscored the sector's ongoing recovery from the challenges imposed by the COVID-19 pandemic
- Serviced apartments exhibited improved year-on-year (y/y) performance, with a 0.5%-point rise in occupancy rates, reaching 66.3% compared to the 65.8% recorded in 2022. Moreover, there was a noteworthy 10.9% increase in monthly charges per square meter (SQM), reaching Kshs 3,045 in 2023, up from Kshs 2,716 in 2022. Additionally, average rental yields experienced a 0.6%-point upturn, reaching 6.8% in 2023, compared to the 6.2% recorded in the preceding year
- We expect the performance of the hospitality sector in 2023 to be cushioned by: i) Intensive marketing of Kenya's tourism market which will improve tourist arrivals, ii) positive accolades according Kenya's tourism industry international recognition, iii) collaborative partnerships fostering tourism growth iv) hospitality sector support events, v) direct flights from Dubai to Mombasa by FlyDubai, and, vi) increased promotion of local tourism promoted by the Ministry of Tourism under its Tourism Strategy 2021-2025, which highlights domestic tourism as one of the key nine initiatives it intends to promote under the program
- However, factors such as: i) issued cautionary statements by governments like China and Canada in December 2023, ii) the weakening of Kenyan shilling against the US dollar, iii) difficulty in accessing finance as lenders demand more collateral to cushion themselves owing to elevated credit risk

2024 Hospitality Sector Outlook cont.…

Expected increased international arrivals to be among the key factors that will cushion the hospitality sector in 2024



Source Kenya National Bureau of Statistics (KNBS)

- In 2023, international tourist arrivals into the country improved evidenced by a 31.7% Year-on-Year (y/y) increase in the number of international arrivals through Jomo Kenyatta International Airport (JKIA) and Moi International Airport (MIA) in Q3'2023 to 451,441, from the 342,904 recorded in Q3'2022 according to the LEI October 2023 report
- This was attributed to the intensive marketing of Kenya's tourism market through an ambitious marketing plan formulated by the Ministry of Tourism in conjunction with the Kenya Tourism Board that is currently ongoing under the 'Real Deal Kenya' slogan. We anticipate a further increase in international arrivals as a result of the marketing initiative

2024 Hospitality Sector Outlook, cont'd…

Sector investment opportunities in 2023 lie in Westlands, Kilimani and Kileleshwa/Lavington

Theme	2023 Performance	2024 Outlook	Effect
Hospitality Sector	• In 2023, serviced apartments' year-on-year (y/y) performance improved, with occupancy rates increasing by 0.5% points to 66.3%, from 65.8% recorded in 2022. Monthly charges per SQM increased by 10.9% to Kshs 3,045 in 2023, from Kshs 2,716 per SQM recorded in 2022. Additionally, average rental yields increased by 0.6% points to 6.8% in 2023, from 6.2% recorded in 2022 • The sector's overall performance improved attributable to increasing number of hotels in operation, hotel bookings and bed occupancies during the year, in addition to aggressive local and international marketing of Kenya's tourism industry	• We anticipate positive performance in the sector, marked by increased operations, bookings, and occupancies, fueled by convenient direct flights from Dubai to Mombasa by FlyDubai. This is expected to attract more international tourists to Mombasa, enhancing the city's appeal for vibrant tourism experiences in Kenya. However, cautionary statements from countries like China and Canada advising against travel to Kenya, concerns about security, power outages, and transportation issues pose challenges. Additionally, factors like the weakening Kenyan shilling, elevated operational costs, tightened lending conditions, and a projected decline in mergers and acquisitions due to increased capital gains tax may impact the sector negatively • Prime investment prospects lie in Westlands, Limuru Road, and Kilimani, where average rental yields stood at 10.2%, 8.2%, and 7.7%, respectively, surpassing the market average of 6.8% in 2023. This was due to their proximity to the CBD, the existence of top-tier serviced apartments commanding premium rates, convenient accessibility, and their closeness to international organizations, fostering a robust demand for serviced apartments in these areas	**Positive**

- ***Our outlook for the hospitality sector POSITIVE. We expect the sector to continue registering improved performance moving forward in terms of increased international arrivals into the country, overall hotels in operations, hotel bookings, and hotel occupancies***

2024 Land Sector Outlook

We expect average selling prices land in the NMA to experience a slowdown to Kshs 128.5 mn

All Prices in Kshs (mn) Unless Stated Otherwise									
Nairobi Metropolitan Area Land Performance Trend									
Location	Price in 2017	Price in 2018	Price in 2019	Price in 2020	Price in 2021	Price in 2022	Price in 2023	Forecasted 2024 Prices	Annual Capital Appreciation 2024F
Unserviced land- Satellite Towns	20.4	22.7	24.9	12.7	13.5	15.1	16.4	17.9	8.9%
Serviced land- Satellite Towns	14.4	14.3	14.3	14.8	16.4	17.8	18.9	19.8	4.6%
Nairobi High End Suburbs- Low and High Rise Residential Areas	120.4	124.7	127.2	126.8	130.3	137.4	134.7	137.2	1.9%
Nairobi Middle End Suburbs- High Rise Residential Areas	77.6	77.8	81.7	83.6	83.0	80.9	82.3	83.1	1.0%
Nairobi Suburbs - Commercial Areas	429.8	447.3	428.5	413	410.8	403.4	390.7	384.5	(1.6%)
Average	132.5	137.4	135.3	130.2	130.8	131.0	128.6	128.5	3.0%

- The Nairobi Metropolitan Area (NMA) land sector recorded an average annualized capital appreciation of 2.9% in FY'2023, which is 0.3% points lower than the 3.2% average appreciation recorded in FY'2022. Subsequently, the average selling prices for land in the Nairobi Metropolitan Area (NMA) in FY'2023 slowed down at Kshs 128.6 mn, from Kshs 130.2 mn recorded in FY'2022, attributable to uncertainty on future demand cycles given the economic slowdown and challenging micro-economic environment
- We anticipate that the average selling prices for land in the NMA will continue to experience a slowdown and decline slightly to come in at Kshs 128.5 mn in FY'2024, from Kshs 128.6 mn recorded in FY'2023. We attribute this to factors such as increased uncertainty, eroded purchasing power, and a deteriorating business environment, which may impact demand and contribute to a moderation in land prices

2024 Land Sector Outlook, cont….

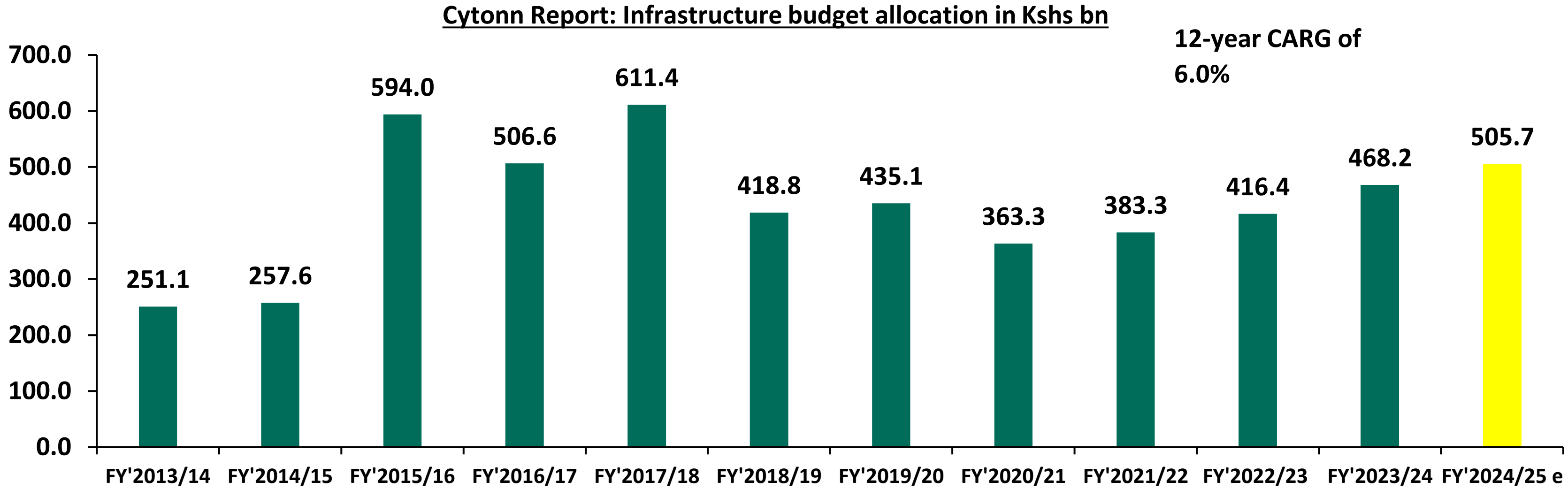
We retain a POSITIVE outlook for the land sector which has displayed great resilience even during times of economic hardship

Sector	2023 Performance	2024 Outlook	Outlook
Land Sector	• The Nairobi Metropolitan Area (NMA) land sector recorded an average annualized capital appreciation of 2.9% in FY'2023 • The overall asking prices for unserviced and serviced land in the satellite towns of the NMA recorded the highest average capital appreciations of 8.8% and 5.9%, which came in 5.9% and 3.0% points higher than the market average of 2.9% respectively • This was mainly attributed to an increased demand resulting from their affordability, having recorded average selling prices per acre at Kshs 16.4 mn and Kshs 18.9 mn compared to the market average of Kshs 128.6 mn in FY'2023. Moreover, infrastructure developments enhancing accessibility to these areas, availability of amenities and high concentration of learning institutions around and within the areas necessitating demand land for development of student housing particularly in Juja and Rongai contributes to the sustained demand for land in these areas	• We expect the performance of the sector to remain positive, with an expected annual capital appreciation of 3.0%, fueled by anticipated high prices in satellite towns. We expect the positive performance will be supported by; i) the completion of major infrastructure projects, ii) rising demand for development land in satellite towns, and, a general increasing demand for land • However, we anticipate that the average selling prices for land in the NMA will continue to experience a slowdown and decline slightly to come in at Kshs 128.5 mn in FY'2024, from Kshs 128.6 mn recorded in FY'2023. We attribute this to factors such as increased uncertainty, eroded purchasing power, and a deteriorating business environment, which may impact demand and contribute to a moderation in land prices • Investment opportunity lies in Juja, Utawala, and Rongai for unserviced land, which recorded annualized capital appreciations of 12.3%, 11.6%, and 9.8% respectively compared to a market average of 8.8%. For serviced schemes, Ruiru-Juja, and Ruai recorded the highest annualized capital appreciations of 6.8% and 6.0%, respectively against the serviced average of 5.9%	Positive

We retain a Positive outlook for the Nairobi Metropolitan Area land sector as we expect sector performance to continue improving supported by completion of major infrastructure projects and rising demand for land. However, we anticipate the above mentioned factors to weigh down sector performance

2024 Infrastructure Sector Outlook

Budget allocation for the infrastructure sector increased by 12.4% to Kshs 468.2 bn in FY'2023/24 from Kshs 416.4 bn allocation in FY' 2022/23



- In the FY'2023/2024, Infrastructure, Energy and Information and Technology (ICT) budget saw an increase of 12.4%, totaling Kshs 468.2 bn from Kshs 416.4 bn in FY'2022/2023. This underscores the recognition of the capital-intensive nature of infrastructure projects and their direct impact on job creation and regional economic growth. This increase aligns with the government's efforts to enhance critical infrastructure in the road, rail, energy, and water sectors, with the aim of improving transportation, lowering business costs, increasing access to amenities, facilitating cross-border trade, regional integration, and boosting Kenya's competitiveness on the global stage

2024 Infrastructure Sector Outlook, cont….

The government has indulged in adoption of various alternatives to fund the infrastructural budget such as Issuing of Infrastructure bonds, grants, loan and Joint Ventures

Cytonn Report: Sectoral Budget Allocation of Development Expenditure for the Past Five Years (Kshs bn)							
Item	FY'2019/2020	FY'2020/2021	FY'2021/2022	FY'2022/2023	FY'2023/2024	y/y Change	5-Year CAGR
Interest Payments, pensions & Net Lending	553.3	586.5	718.3	869.3	986.2	13.6%	12.3%
Education	494.8	505.1	503.9	544.4	628.6	15.5%	4.9%
Infrastructure, Energy and ICT	435.1	363.3	383.3	416.4	468.2	12.4%	1.5%
County shareable Revenue	310.0	316.5	370.0	370.0	385.4	(3.5%)	4.5%
Public Admin & Int. Relations	298.9	289.3	299.7	342.2	327.0	(4.4%)	1.8%

- The table above illustrates the sectors with the highest expenditure allocation over the past five fiscal years, further highlighting the importance placed on infrastructure development
- However, the government is still experiencing financial shortfall in its expenditure budget and hence financing some of these projects will be capital-intensive and higher-risk. Therefore, the government has been adopting various sources of financing the infrastructure budget such as;

2024 Infrastructure Sector Outlook, cont.…

The government has indulged in adoption of various alternatives to fund the infrastructural budget such as Issuing of Infrastructure bonds, grants, and Joint Ventures

i) **Public-Private Partnerships with local and foreign private firms** like China Roads and Bridges Corporation in construction of Phase 2A of Standard Gauge Railway from Naivasha to Kisumu,

ii) **Issuing of Infrastructure bonds:** The government through the national treasury floated an infrastructure bond in June 2023 named the IFB1/2023/07 valued at Kshs 60.0 bn aiming to complete select projects in the pipeline. The bond recorded an oversubscription of 367.5%. Additionally, the recently issued IFB1/2023/6.5 infrastructure bond was oversubscribed by 177.8%, with the government accepting bids totaling Kshs 67.1 billion at a yield of 17.9%, equivalent to 21.1% on a tax-effected basis,

iii) **Grants and loans from foreign countries** like United States of America (Dualling of Nairobi-Mombasa and Nairobi-Nakuru Highways), United Kingdoms (Nairobi Railway City), South Korean (Konza Metropolis City), Chinese governments, and many more, and,

v) **Joint ventures with several parastatals and agencies**: the government is in joint venture with Kenya Ports Authority and JICA in construction of Dongo-Kundu Special Economic Zone which includes the Dongo-Kundu Bypass

2024 Infrastructure Sector Outlook, cont….

We expect a 8.0% increase in the budget allocation to the infrastructure sector to Kshs 505.7 bn in FY'2024/23 from Kshs 468.2 bn allocation in FY' 2023/24

- According to the Draft 2024 Budget Policy Statement, the government's Infrastructure, Energy, and ICT allocation for the FY'2024/2025 is forecasted to be Kshs 505.7 bn, representing a 8.0% increase from Kshs 468.2 bn FY'2023/2024. This increase is attributed to an extensive array of strategic programs and interventions
- During this fiscal year 2024/2025 and the Medium-Term period, the sector plans to implement various initiatives to enhance infrastructure development and technological advancement. Key programs include the construction of 2,794 km of new roads, rehabilitation of 560 km of roads, maintenance of 137,544 km of existing roads and bridges, construction of 84 new bridges, and the training of 16,230 plant operators, contractors, and technicians. Additionally, the sector aims to complete various projects such as the Riruta – Lenana – Ngong Railway Line, phase I of Nairobi Railway City, the Meter Gauge Railway (MGR) Link from Mombasa SGR Terminus to Mombasa MGR Station, and the Railway Bridge across Makupa Causeway. Other initiatives encompass housing construction, urban development projects, digital infrastructure expansion, electrification efforts, oil and gas potential exploration, and the provision of clean cooking gas to public learning institutions and low-income households. The comprehensive scope of these programs justifies the augmented budget allocation to drive transformative growth in the sector

2024 Infrastructure Sector Outlook, cont….

Allocation to the State Department of Roads reduced by 8.3% to Kshs 230.1 bn in FY'2023/24 from Kshs 250.8 bn in FY'2022/23

- We also note that, according to the Supplementary Budget FY'2023/24, allocation to the State Department of Roads reduced by 8.3% to Kshs 230.1 bn from Kshs 250.8 bn. This was attributed to the redirection of funds to other key sectors such as education, as well as to address mounting costs over debt repayment, on the back of increasing debt obligations exacerbated by the continued depreciation of the Kenyan Shilling. The above indicates a shift in government's spending priorities, signaling reduced roads expenditure through a reduction in budgetary allocations to major capital expenditure road projects in the FY'2023/24. In support of this, various projects including the Nairobi-Mombasa Expressway and Rironi-Mau Summit Highway have been suspended valued at Kshs 320.0 bn and Kshs 160.0 bn respectively. Moving forward, we anticipate that due to the above, Kenya's infrastructure sector will witness a slowdown in the number of initiated and completed road construction and maintenance projects going forward. Furthermore, we expect the reduction in country's overall development budget by Kshs 41.9 bn to Kshs 765.7 bn from Kshs 807.6 bn will have a knock-on effect to the infrastructure sector

2024 Infrastructure Sector Outlook, cont.…

Our outlook for the sector is neutral supported by the government's commitment to construct affordable units but weighed down by recent budgetary cuts

Sector	2022 Performance	2023 outlook	Effect
Infrastructure Sector	• The government continued to make considerable efforts in advancing infrastructural developments across the country amid focus on achieving the Vision 2030 and Big Four Agenda • In the FY'2023/2024, Infrastructure, Energy and Information and Technology (ICT) budget saw an increase of 12.4%, totaling Kshs 468.2 bn from Kshs 416.4 bn in FY'2022/2023 • Some of the key projects implemented in 2023 included; construction of new roads (3,805 km), construction of 73 bridges, repair of roads (240 km), revitalization of the Kisumu-Butere (69 km), Leseru-Kitale (65 km), and Gilgil-Nyahururu (78 km) rail branch lines	• In 2024, we anticipate ongoing and completed infrastructure projects, backed by the government's commitment to: i) construct and rehabilitate roads, bridges, railways, airports, and affordable housing units, ii) enhance diplomatic ties and partnerships with neighboring nations in development, and iii) intensify efforts to attract regional and international investors, positioning Kenya competitively in comparison to other East African countries like Tanzania through railway connections and ports infrastructure • Upon completion, the projects are expected to open up more areas for penetration of Real estate investments across all select sub-sectors, tapping into new opportunities and demand for properties, goods and services • However, recent budgetary cuts to the State Department for Housing and an overall reduction in the country's development expenditure may impede the sector's optimal performance. As per the Supplementary Budget FY'2023/24, the allocation to the State Department of Roads decreased by 8.3% to Kshs 230.1 billion from Kshs 250.8 billion. This reduction was attributed to fund redirection to other key sectors like education and addressing escalating costs related to debt repayment, driven by the continuous depreciation of the Kenyan Shilling	**Neutral**

We have a NEUTRAL outlook for the sector as we expect to continue seeing the progress, and completion of more infrastructural developments in 2024 mainly supported by the above factors. However, recent budgetary cuts to the state department for housing, and a general reduction in the country's development expenditure will potentially hinder optimal performance of the sector

2024 Industrial sector outlook

We expected increased investments and activities in the sector in 2024

- Kenya made remarkable growth in the industrial real estate sector in 2023. Several international companies made significant investments in the sector, such as Perishable Movement Kenya Limited, Improvon and Fresh Handling Kenya Limited. A large number of investors in this sector aims a tapping on the opportunity provided by demand storage space for perishable goods and Fast-Moving Consumer Goods. Players such as Africa Logistics Properties have been steadfast in tapping opportunity presented by demand for quality grade A industrial and warehousing facilities marked by completion of the fourth phase of their Nairobi West Logistics Park in Tilisi, along Nairobi- Nakuru Highway. Notably, in Q1,2023 the sector recorded an occupancy rate of 80.0% signaling a growing demand for quality warehouses which will ultimately support growth in the sector

- Data centers and cold room have been a major driver in the industry. In recent years, there has been a growing demand for cold rooms in the country given that there are currently only 10 cold rooms in Nairobi. This under supply is set to increase demand as businesses activities continue to increase. Similarly, demand for data centers is on the rise and set to boost growth in the sector. As a result, Kenya has been highlighted as a potential for market for data centers among other African nations. Contemporary data centers serve as hubs that link on-site infrastructure to cloud based infrastructure, enabling visualization of networks, applications, and workloads across private and public clouds. In addition, investors in Kenya have adapted to growing demand for quality warehouses in Africa. In the last 5 years, developers have delivered more than 17,000 SQM of quality warehousing space

2024 Industrial sector outlook, Cont …

We expected increased investments and activities in the sector in 2024

- In 2024, we expect increased investments and activities in the sector with major players in the industry such as Africa Data Centre’s (ADC) announcing expansions. ADC is set to open a data center facility in the first quarter of 2024, when it is scheduled for completion. This facility is set to deliver an additional 15 MW of IT load, expand ADC's current infrastructure and addressing the increasing demand for digital services in East Africa. Additionally, developers such as Logistics Properties and Improve on plan to deliver over 4,000 SQM of space in the market by the end of the year.

2024 Industrial sector outlook, Cont …

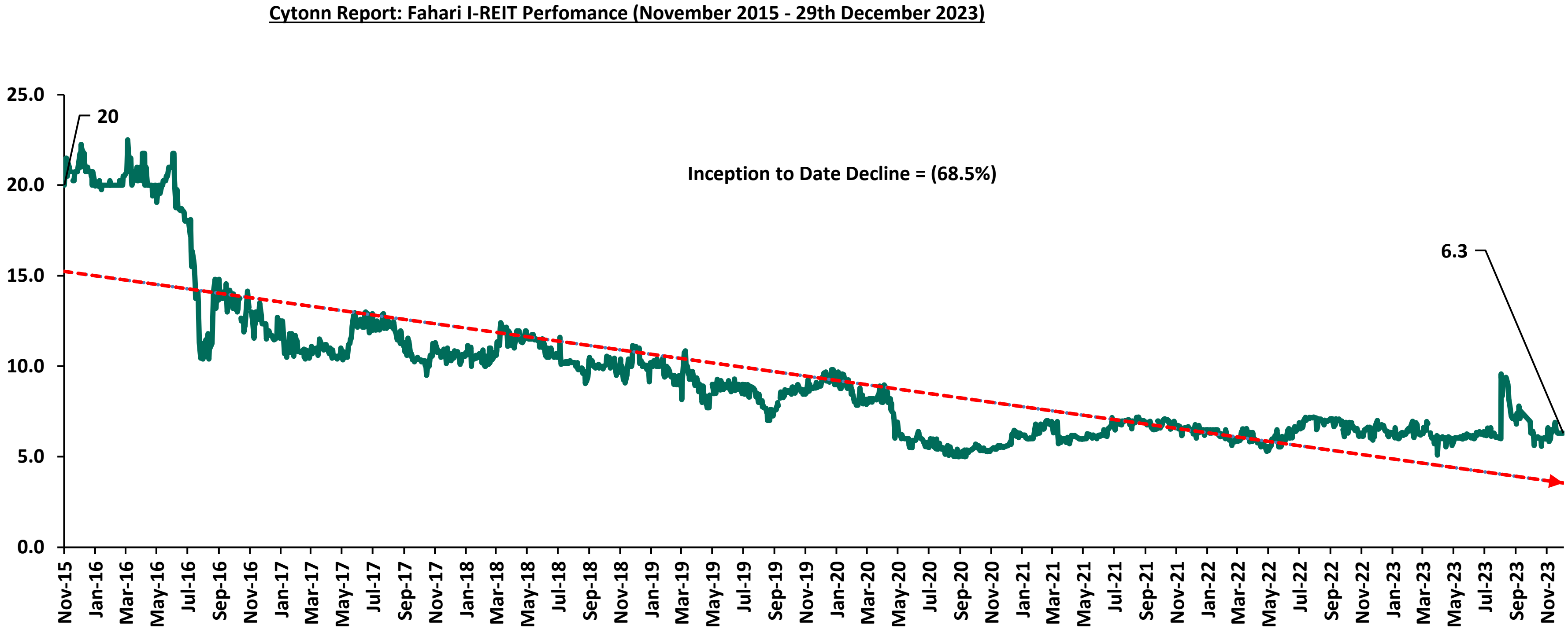
We expect continued growth as investors continue to respond to growing demand

Sector	2023 Performance	2024 outlook	Effect
Industrial sector	• In 2023, the sector was on an upward trajectory, supported by rising demand for e-commerce warehouses in the retail sector as well as increased demand storage space for perishable goods. • Several players in the industry made significant investments in the sector including Perishable Movements Kenya Limited, Fresh Handing Kenya Limited, Improvon among others in setting up production factories and storage facilities. This was in efforts to localise sourcing of raw materials and production of goods, on the back of a depreciating local currency against major trading currencies	• We expect continued growth in the sector as investors continue to respond to the growing demand for industrial space. Data centers, cold rooms, growth in e-commerce and fast-moving consumer goods will drive growth in the industrial sector • In 2024. we expect heightened development activities in the sector with projects such as the Africa Data Centres' (ADC) new facility scheduled for completion in the first quarter of 2024. This facility is set to deliver an additional 15 MW of IT load, expanding ADC's current infrastructure and addressing the increasing demand for digital services in East Africa	Positive

We expect the Kenyan industrial sector will continue on an upward trajectory supported by; i) rising demand for e-commerce warehouses in the retail sector, fuelled by the rising demand for space to store goods meant for delivery to clients across the country, as more people shift towards home delivery as a convenient and efficient way to purchase goods, ii) government's accelerated focus on exporting agricultural and horticultural products to the international market, with an aim to improve the quantity, quality, efficiency, and reliability of Kenya-farmed produce thereby increasing the country's competitiveness, iii) Kenya's continued recognition as a regional hub hence attracting investments, iv) increased demand for cold storage facilities for drugs and vaccines whose demand is driven by the Universal Health Coverage program by the government

2024 Listed Real Estate Sector Outlook

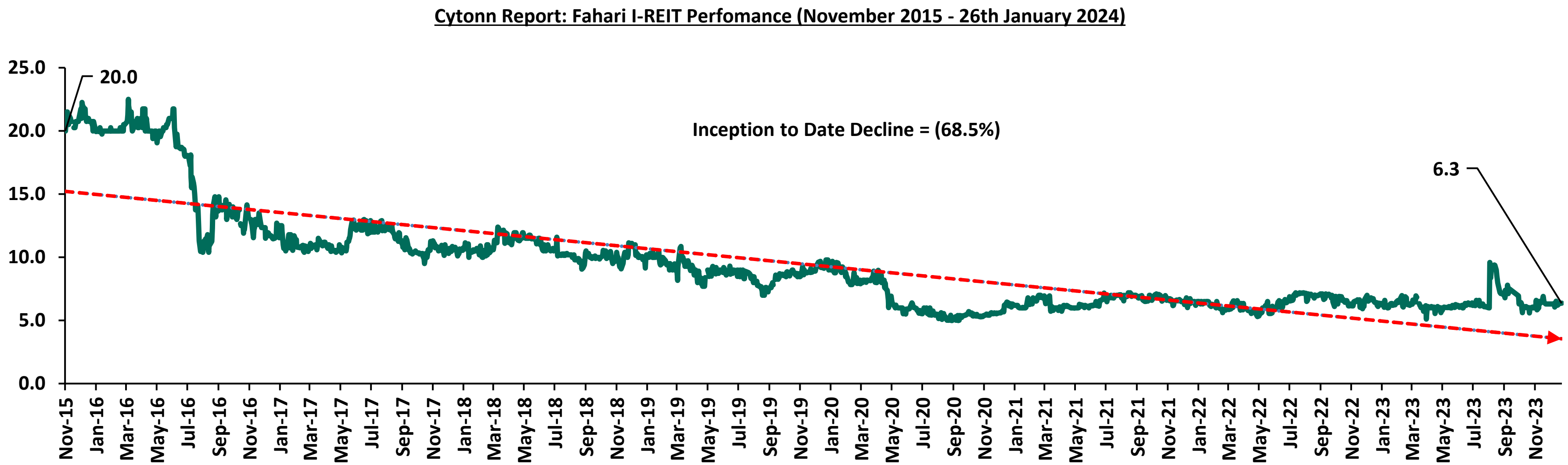
Fahari I-REIT closed the year 2023 trading at Kshs 6.3 per share, representing a 68.5% Inception-to-Date (ITD) loss from the Kshs 20.0 price as at November 2015



- In the Nairobi Securities Exchange, ILAM Fahari I-REIT closed 2023 trading at an average price of Kshs 6.3 per share. The performance represented a 7.1% Year-to-Date (YTD) loss from Kshs 6.8 per share recorded on 3 January 2023, taking it to a 68.5% Inception-to-Date (ITD) loss from the Kshs 20.0 price

2024 Listed Real Estate Sector Outlook

Fahari I-REIT opened the year trading at Kshs 6.3 per share, representing a 68.5% Inception-to-Date (ITD) loss from the Kshs 20.0 inception price as at November 2015



- Fahari I-REIT opened the year 2024 trading at an average price of Kshs 6.3 per share recorded on 2nd January 2024. As at 26th January 2024, ILAM Fahari I-REIT closed the week trading at an average price of Kshs 6.3 per share. The performance represents a 0.9% decline from Kshs 6.4 per share recorded last week. On a Year-to-Date (YTD) basis, the performance remained relatively unchanged from the price recorded on 2nd January 2023
- Additionally, the performance represents a 68.5% Inception-to-Date (ITD) loss from the Kshs 20.0 price. The dividend yield currently stands at 10.3%
- We expect the Fahari I-Real Estate to continue trading in low volumes in 2024, having opened the year with a low trading price of Kshs 6.3 per share, and low investor appetite amid high investment amounts required

2024 Listed Real Estate Sector Outlook

Acorn D-REIT and I-REIT opened the year trading at same unit prices recorded as at 1st December 2024

- In the Unquoted Securities Platform (USP), Acorn D-REIT and I-REIT closed the year 2023 trading at Kshs 25.3 and Kshs 21.7 per unit, respectively, as of 1st December 2023. The performance represented a 26.6% and 8.3% gain for the D-REIT and I-REIT, respectively, from the Kshs 20.0 inception price. The volumes traded for the D-REIT and I-REIT came in at 12.3 mn and 30.7 mn shares, respectively, with a turnover of Kshs 257.5 mn and Kshs 633.8 mn, respectively, since inception in February 2021
- Acorn D-REIT and I-REIT opened the year 2024 trading at same unit prices recorded as at 1st December 2024. In the week ended 19th January 2024, the Kenyan USP market recorded market activity for the first time in 2024, to close at Kshs 24.4 and Kshs 21.7 per unit for the D-REIT and I-REIT respectively. The performance represented a 22.0% and 8.3% gain for the D-REIT and I-REIT, respectively, from the Kshs 20.0 inception price. The volumes traded for the D-REIT and I-REIT came in at 12.3 mn and 30.7 mn shares, respectively, with a turnover of Kshs 257.5 mn and Kshs 633.8 mn, respectively, since inception in February 2021. As at 26th January 2024, Acorn D-REIT and I-REIT traded at Kshs 24.4 and Kshs 21.7 per unit respectively. The performance remains relatively unchanged from that realized on 19th January 2024

2024 Listed Real Estate Sector Outlook, cont'd…

The Kenyan REIT market is poised to experience minimal activity throughout 2024

Sector	2023 Performance	2024 Outlook	Outlook
Listed Real Estate	• In the Nairobi Securities Exchange, Fahari I-REIT continued to underperform closing the year 2023 at Kshs 6.3 per share, representing a 68.5% Inception-to-Date (ITD) loss from the Kshs 20.0 price • The underperformance of the Kenyan REIT sector is attributable to various factors such as; i) lack of sufficient investor awareness regarding the potential of REITs as an investment tool, ii) lengthy approval procedures for establishing REITs have hindered their formation and deployment in the market, iii) high minimum capital requirement of Kshs 100.0 mn for trustees which restricts the involvement of non-bank entities in the role of trustees, and, iv) steep minimum investment amount of Kshs 5.0 mn discourages potential investors from engaging in REITs. These factors have impeded the optimum performance of the sector • In the Unquoted Securities Platform, Acorn D-REIT and I-REIT traded at Kshs 25.3 and Kshs 21.7 per unit, respectively, as of 1st December 2023. The performance represented a 26.6% and 8.3% gain for the D-REIT and I-REIT, respectively, from the Kshs 20.0 inception price. The volumes traded for the D-REIT and I-REIT came in at 12.3 mn and 30.7 mn shares, respectively, with a turnover of Kshs 257.5 mn and Kshs 633.8 mn, respectively, since inception in February 2021	• Anticipatedly, the Kenyan REIT market is poised to experience minimal activity throughout 2024. ILAM Fahari I-REIT is planned for delisting from the Main Investment Market Segment of the Nairobi Securities Exchange (NSE) and subsequent quoting on the USP. This strategic move is part of the ongoing operational restructuring strategy employed by the REIT manager, ICEA Lion Asset Management. Consequently, Fahari I-REIT is set to join the Acorn REITs in trading on the USP. Notably, LAPTrust's Imara I-REIT continues to trade on the Main Investment Market of the NSE, under the Restricted Segment. It is important to highlight that recent developments in the sector have limited investment in the asset class to high-net-worth individuals or professional investors capable of purchasing units worth Kshs 5.0 mn and above. This trend runs counter to the sector's primary goal of facilitating access to the capital markets to retail investors	**Neutral**

2024 Listed Real Estate Sector Outlook, cont'd…

We retain a NEUTRAL outlook for the Kenyan REIT sector

Sector	2023 Performance	2024 Outlook	Outlook
Listed Real Estate		• Moreover, the sector is expected to trail behind compared to other African countries, notably South Africa, due to various challenges. These include insufficient investor awareness about the potential of REITs as an investment tool, prolonged approval procedures hindering their establishment and deployment, a high minimum capital requirement of Kshs 100.0 million for trustees limiting the participation of non-bank entities, and a substantial minimum investment amount of Kshs 5.0 million deterring potential investors from involvement in REITs • Nonetheless, initiatives like the proposed establishment of the Kenya National REIT (KNR), operational restructuring strategies by industry leaders like Fahari I-REIT aimed at business and financial optimization, and the introduction of the Vuka Investment Platform towards the end of 2022 are anticipated to neutralize and mitigate the aforementioned challenges. These efforts are expected to collectively contribute to enhancing the overall performance of the sector in the Kenyan Real Estate capital markets	Neutral

We retain a NEUTRAL outlook for the Kenyan REIT sector, however, leaning more towards the negative. Some of the factors expected will continue hindering the optimal performance of the sector market include; i) low investors' appetite in trading and investing in the market, ii) lengthy registration, licensing, and approval process, iii) high minimum investment smounts Set at Kshs 5.0 mn, iv) insufficient Investment Knowledge and Awareness of the REITs Market v) subdued performance in some Real Estate sectors with oversupply of spaces in Commercial Office Sector at 7.3 mn SQFT and Retail Sector at 3.0 mn SQFT in the NMA expected to affect performance of the instrument due to low rental yields, and, vi) high Minimum capital requirements for a Trustee of Kshs 100.0 mn. However, we expect initiatives including; i) the proposed establishment of the Kenya National REIT (KNR), ii) business operational restructuring strategies employed by key industry players such as Fahari I-REIT geared towards achieving business and financial optimization as well as sustainability, and iii) the launch of the Vuka Investment Platform towards the end of 2022 will assist neutralize and mitigate the above challenges, thereby contributing to the overall enhancement of the sector's performance.in the Kenyan Real Estate capital markets.

Q&A

Cytonn

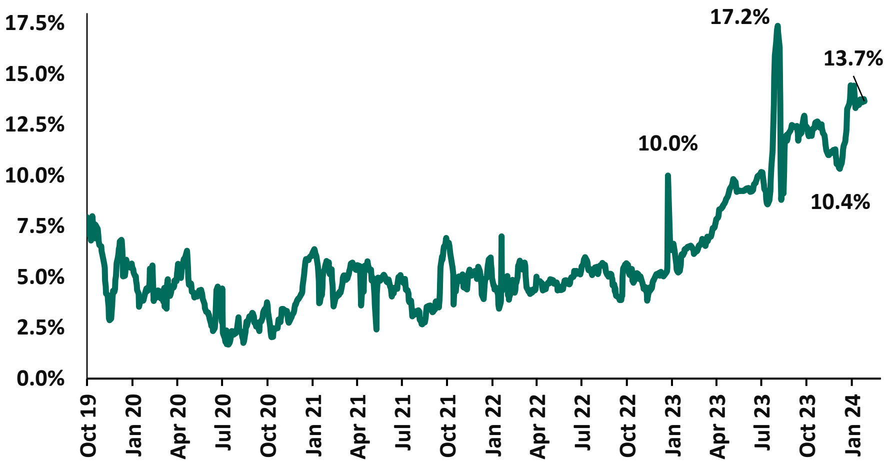
VII. Appendix

Cytonn

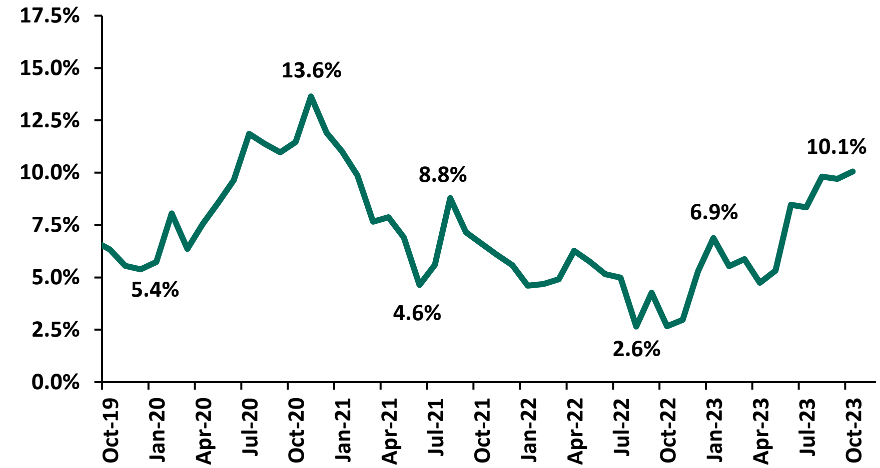
Market Liquidity and Money Supply

We expect liquidity to improve in 2024 driven partly by increased access to credit

Interbank Rates (%)



Money Supply Growth (M3) (y/y)

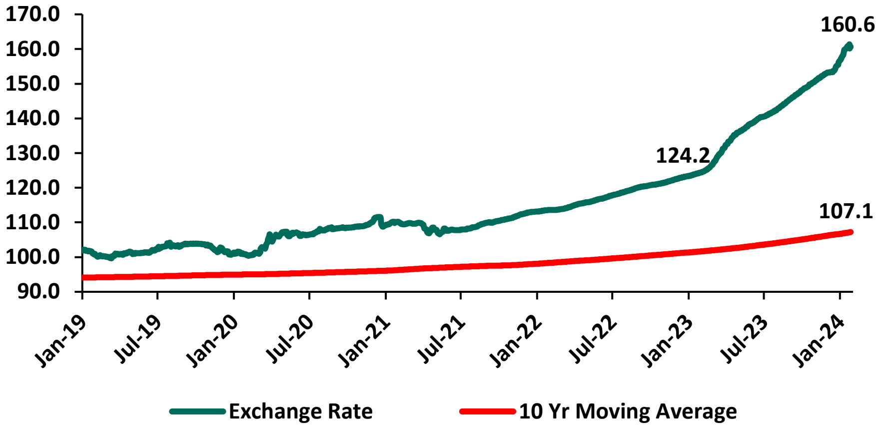


- In 2023, liquidity levels tightened as evidenced by the doubling of the average interbank rate to 9.8% in 2023, from 4.9% in 2022, while the average volumes traded in the interbank market increased significantly by 16.2% to Kshs 21.6 bn in 2023, from Kshs 18.6 bn recorded in 2022,
- The tightened liquidity is partly due to government remittances which offset payments
- Cash Reserve Ratio (CRR) remained unchanged at 4.25% in 2023, in a bid to ease the liquidity in the market by increasing supply of money with commercial banks
- We expect liquidity to improve in 2024 driven by increased access to credit as banks gradually increase their lending to the private sector and the continued adoption of risk-based lending by banks. However, should the government structure some of its local debt in the bid to increase the debt tenors, we may see the liquidity growth being hampered

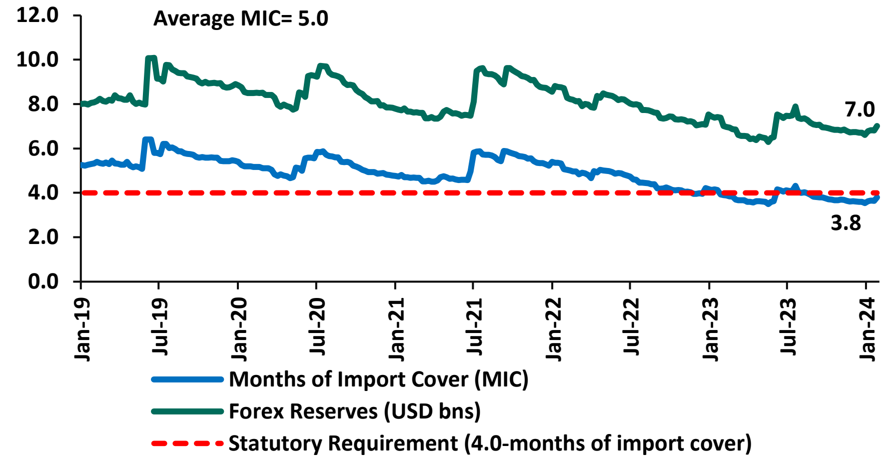
Exchange Rate

We expect the shilling to trade within a range of Kshs 183.2 and Kshs 189.6 against the USD with a bias towards a 16.4% depreciation by the end of the year

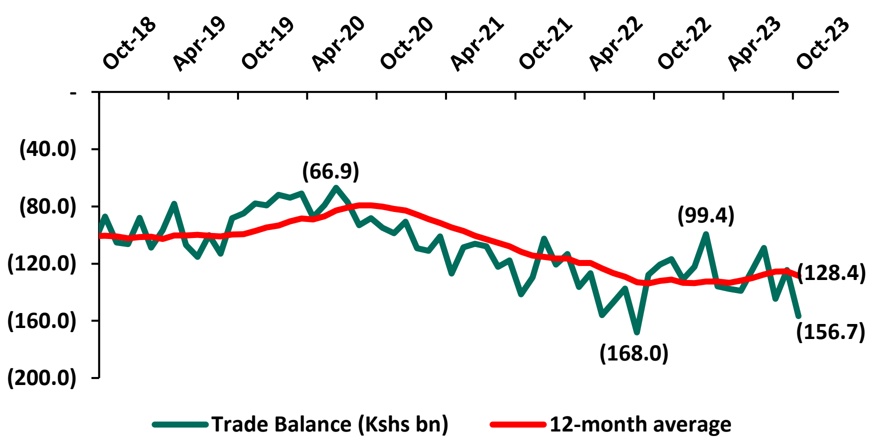
Kshs. Vs USD



Kenya Months of Import Cover and Forex Reserves



Trade Balance (Kshs bn)



- **We expect the shilling to trade within a range of Kshs 183.2 and Kshs 189.6 against the USD with a bias towards a 16.4% depreciation by the end of the year due to:**

i. Persistent current account deficit resulting in increased demand for foreign currency,

ii. The increasing debt servicing costs which continue to put pressure on forex reserves, and

iii. Elevated risk of increase in global crude oil prices as a result of supply chain disruptions following the rising geopolitical tension in the Middle East,

2023 Macroeconomic Outlook –Government Borrowing

Government borrowing is overall Negative with the government expected to borrow aggressively in 2024 to plug in the fiscal deficit and help service its existing loans

Macro-Economic & Business Environment Outlook			
Macro-Economic Indicator	Factors	2024 Outlook	Effect
Government borrowing	**Revenue Collection**	• On revenue collection, we expect continued improvement in 2024 due to the raft of measures the new administration has put in place to boost tax collection such implementation of the Finance Act 2023 which revised a number of taxes upwards and widened the tax base to include the informal sector and digital services. The tax regime has also taken measures to strengthen tax administration by leveraging on technology to seal leakages, rolling out a Tax Invoice Management System (e-TIMS), and enhancing both the iTax platform and the Integrated Customs Management System (iCMS). • The government is also employing a raft of measures to boost revenue collection through non-tax channels by streamlining its services to the public e.g. Citizen services, the Ministry of Lands and Immigration services. However, the upward revision of taxes comes at a time when the business environment remains subdued, underpinned by the elevated inflationary pressures and the aggressive depreciation of the Kenyan shilling that has suppressed business production levels weighing down on the projected revenue performance.	**Neutral**
	Foreign Borrowing	• Going into 2024, the administration has been trying to focus more into multilateral lending, a move from the commercial lending which is deemed to be more expensive. This has seen the contribution from Multilateral lenders increase by 4.7% points to 49.9% in October 2023 from 45.2% of total external debt in October 2023 while commercial debts declined by 2.0% points to 26.2% in October 2023 from 28.2% in October 2022, while contribution of bilateral debt declined by 2.7% points to 23.7% in October 2023, down from 26.4% recorded in October 2022. • In our view, the level of foreign borrowing will also increase in 2024 due to the following reasons; i) Need to service the upcoming maturities such as the 10-year USD 2.0 bn (Kshs 226.0 bn) Eurobond maturing in June 2024 with the government being locked out of the international Eurobond market due to high yields demanded by investors, (ii) Disbursement of concessional loans from the IMF under the EFF/ECF and RSF arrangements, coupled with funding from the World Bank under the Development Policy Operation (DPO) arrangement, and (iii) Disbursement of commercial loans from commercial lenders such as the Trade & Development Bank (TDB) and the African Development Bank.	**Negative**
	Domestic Borrowing	• On the domestic front, we expect the government to borrow aggressively from the domestic market as it aims to plug in the fiscal deficit, which is projected to come in at Kshs 704.0 bn in the FY'2024/25 budget, 3.9% of the GDP. The government intends to plug this fiscal deficit through Kshs 326.2 bn in external financing and Kshs 377.7 bn in domestic borrowing. Borrowing domestically is less costly for the government than acquiring debt denominated in foreign currencies, which not only carry higher interest rates but also come with the added risk of currency fluctuations.	**Negative**

2024 Macroeconomic Outlook -Currency

We expect the Shilling to range between Kshs 183.2 and Kshs 189.6 to the USD with a bias to a 16.4% depreciation by the end of the year

<table>
<tr><th colspan="4">Macro-Economic & Business Environment Outlook</th></tr>
<tr><th>Macro-Economic Indicator</th><th>Factors</th><th>2024 Outlook</th><th>Effect</th></tr>
<tr><td rowspan="4">Currency</td><td>Balance of Payment</td><td>• Kenya’s balance of payments position (BoP) deteriorated during the quarter, registering a deficit of Kshs 131.5 bn in Q3’2023, from a deficit of Kshs 112.7 bn recorded in Q3’2022, and a reversal from the Kshs 152.9 bn surplus recorded in Q2’2023
• The y/y performance in BoP was mainly driven by the reversal of the financial account balance to a deficit of Kshs 20.6 bn from a surplus of Kshs 175.1 bn in Q3’2022, which outweighed the 42.1% narrowing of the current account balance deficit to Kshs 122.5 bn in Q3’2023 from Kshs 211.6 bn in Q3’2022 and the 448.2% increase in the capital account balance to Kshs 3.4 bn from Kshs 0.6 bn recorded in a similar period in 2022</td><td>Negative</td></tr>
<tr><td>Forex Reserves</td><td>• The Country’s forex reserves, as at the close of 2023, stood at USD 6.6 bn (equivalent to 3.5-months of import cover), which is below both the statutory requirement of maintaining at least 4.0-months of import cover, and the EAC region’s convergence criteria of 4.5-months of import cover,
• On the downside, Kenya’s forex reserves have been declining due to subdued inflows from exports and repayment of debts and will face more strain in 2024 due the USD 2.0 bn Eurobond maturity in June. Despite this, we expect the same to be supported by the improving diaspora remittances as well as the gradual economic recovery</td><td>Neutral</td></tr>
<tr><td>Differentials in Interest Rates</td><td>• The United States Federal Bank hiked their interest rate by 100 bps in 2023 from a range of 4.25%-4.50% in December 2022 to a range of 5.25%-5.50% in July 2023 to control inflation in the country. This lead to a depreciation in the Kenyan shilling relative to the US Dollar as more investors prefer the dollar to the higher yield offered.
• The interest rate deferential resulting from the aggressive Fed Rate hikes increased the investment attractiveness of the US market and negatively impacted the risk return profile of emerging market economies thus leading to capital flight. Given that the Fed paused the interest rate hikes and expected to cut them going into 2024, we only anticipate continued pressure on the shilling as a result of the strengthening dollar
• We expect the restrictive policy stance utilized in 2023 to be maintained in the short term of 2024 as the Monetary Policy Committee evaluates the effect of the high CBR on the country’s inflation rate and local currency performance.</td><td>Negative</td></tr>
<tr><td>Diaspora Remittances</td><td>• Diaspora remittances improved, standing at a cumulative USD 4.2 bn for the year 2023, representing a 4.0% y/y increase from the total remittances of USD 4.0 bn recorded in 2022. In 2024, diaspora remittances are set to improve further, mainly driven by the recovery of the global economy, increasing Kenyan population in the diaspora, and advancing technology that has facilitated easier transfer of money,</td><td>Positive</td></tr>
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2024 Macroeconomic Outlook – Interest Rates

We expect upward pressure on interest rates due to increased pressure on the government to meet its domestic borrowing target and raise funds for budgetary support

Macro-Economic & Business Environment Outlook			
Macro-Economic Indicator	**Factors**	**2024 Outlook**	**Effect**
Interest Rates	Economic Growth	• The Kenyan economy recorded a 5.9% growth in Q3'2023, faster than the 4.3% growth recorded in Q3'2022. pointing towards continued economic recovery. Consequently, the average GDP growth rate for the 3 quarters in 2023 averaged 5.5%, a slight decline from the 5.6% expansion recorded during a similar period of review in 2022. The average GDP growth rate for 2023 is expected to be 5.3%, an improvement from the 4.8% expansion witnessed in 2022 • We anticipate the economic growth to continue on its recovery trajectory in 2024, with the GDP growth rate ranging between 5.0% - 5.4%. We expect the GDP growth to be supported by the continued recovery of the agricultural sector and a robust performance in the services sector driven by growth in information and technology as well as accommodation and food services as a result of increased tourism. However, there are several risks could potentially hinder this growth such as the high risk of debt distress, elevated inflationary pressures, currency depreciation, and a restrictive monetary policy stance.	Neutral
	Exchange Rate	• We expect the Shilling to range between Kshs 183.2 and Kshs 189.6 to the USD with a bias to a 16.4% depreciation by the end of the year.	Negative
	Inflation	• We expect the annual average inflation rate to fall back within the government's target of 2.5%-7.5% coming in at an average of 6.9% in 2024 as compared to 7.7% in 2023. We expect the decline in inflation to be driven by the rebound in the agricultural sector and the expected cooling in inflation, both globally and locally as the tightened monetary policy continues to take effect. However, we expect inflationary pressures to remain elevated due to high electricity prices, high fuel costs, and continued depreciation of the Kenyan shilling.	Neutral
	Government Borrowing	• On the domestic front, we expect the government to borrow aggressively from the domestic market as it aims to plug in the fiscal deficit, which is projected to come in at Kshs 704.0 bn in the FY'2024/25 budget, 3.9% of the GDP. The government intends to plug this fiscal deficit through Kshs 326.2 bn in external financing and Kshs 377.7 bn in domestic borrowing. • In our view, the level of foreign borrowing will also increase in 2024 due to the following reasons; i) Need to service the upcoming maturities such as the 10-year USD 2.0 bn (Kshs 226.0 bn) Eurobond maturing in June 2024 with the government being locked out of the international Eurobond market due to high yields demanded by investors, (ii) Disbursement of concessional loans from the IMF under the EFF/ECF and RSF arrangements, coupled with funding from the World Bank under the DPO arrangement, and (iii) Disbursement of commercial loans from commercial lenders such as the Trade & Development Bank (TDB) and the African Development Bank.	Negative

2024 Macroeconomic Outlook - GDP

Kenya's economy is expected to register growth between 5.0% - 5.4% in 2024

Macro-Economic & Business Environment Outlook			
Macro-Economic Indicator	**Drivers**	**2024 Outlook**	**Effect**
GDP	Private Sector Credit Growth	• In the first 10 months leading to end of October 2023, the average private sector credit growth rate increased slightly by 0.6% points to 12.1%, from 11.5% recorded in over a similar period in 2022. Growth of credit to the private sector is expected to improve on the back of existing policy measures, including the MSMEs Credit Guarantee Scheme, and continued economic recovery • Despite the elevated Gross Non-Performing Loans Ratio in Q3'2023, which increased to 13.1%, as compared to 12.2% in Q3'2022, the banks continued to advance credit to the private sector albeit cautiously through the risk based lending model	Neutral
	Infrastructural Development	• We expect to continue seeing the launching, execution, and completion of more infrastructural developments in 2024 mainly supported by the government's drive to; i) initiate and implement projects, ii) increase its diplomacy and partnerships in development among neighbouring nations, and, iii) step up the competition for attracting regional and international investors against other countries in Eastern Africa like Tanzania through railway connections and ports infrastructure • According to the Draft 2024 Budget Policy Statement, the allocations to Infrastructure, Energy, and ICT in the FY'2024/25 are projected to be Kshs 505.7 bn, representing a 2.2% increase from the Kshs 494.7 bn in FY'2022/23. The increase in spending coupled with the Public-Private partnership approach will improve the government's ability to fund new infrastructure projects;	Positive
	Key Sectors (Agriculture, Manufacturing, Construction, Tourism, Real Estate)	• Agriculture and Forestry recorded a growth of 6.7% in Q3'2023. The performance was an increase of 8.0% points, from the contraction of 1.3% recorded in Q3'2022. The positive growth recorded during the quarter was mainly attributable to favorable weather conditions that characterized the first three quarters of 2023 • The manufacturing sector recorded a decelerated growth of 1.9% in Q3'2023 compared to a 6.0% growth in a similar period of review in 2022. We expect its growth to remain subdued due to high electricity and fuel costs • Notably, Accommodation and Food Services sector recorded the highest growth rate among all the sectors in Q3'2023, having expanded by 26.0%, higher than the 16.9% recorded in Q3'2022. We expect the robust performance to persist into 2024 due to improved tourism and security. In 2024, we will also expect to see increased GDP output from sectors such as Real Estate and Construction as the government pursues the Affordable housing agenda	Neutral
	Fiscal and Monetary Policy	• In 2023, the MPC raised the CBR by 375.0 bps from 8.75% in January to 12.5% in December, in a bid to anchor the inflation rate within the CBK's target range of 2.5%-7.5% and also to support the Kenyan shilling. We expect the CBK its restrictive monetary policy stance in the medium term • We expect the government to continue its fiscal consolidation efforts by aiming to reduce its expenditure through freezing of employment in non-priority sectors and abandonment of stalled projects. Due to the stringent terms imposed by the IMF we expect the government to continue the implementation of the Finance Act 2023 with more focus on widening the tax base and more efficient tax collection measures in order to increase tax revenue	Negative

2024 Macroeconomic Outlook – Investor Sentiment

Investor sentiment is Neutral, but with a negative outlook on currency perfomance

Macro-Economic & Business Environment Outlook			
Macro-Economic Indicator	Measures	2024 Outlook	Effect
Investor Sentiment	Eurobond Yields	• Yields on Kenyan Eurobonds also recorded marginal declines at an average of 0.6% with the 10-year Eurobond issued in 2014, declining by 0.4% points to 12.3% in December 2023, from 12.7% recorded in December 2022 partly attributable to the reassurances by the government on its ability to meet is debt obligations with the country making payment of USD 67.8 mn due in December 2023 and its efforts to acquire a concessional loan from the IMF and the World Bank • Generally, we expect a slight increase in the yields as we approach the USD 2.0 bn Eurobond maturity in June. However, we could see the interest rate environment stabilize in the medium term as the government receives a boost from concessional loans from the IMF and the World Bank, thereby improving the country's credit outlook	Neutral
	Foreign Direct Investment (FDI)	• Kenya is one of the largest recipients of FDI in Africa, with FDI inflows significantly increasing from 2010 up to 2017 at a 7-year CAGR of 34.3% to USD 1.4 bn from USD 0.2 bn • According to UNCTAD's World Investment Report 2023, FDI inflows improved in 2023, increasing by 63.9% to USD 759.0 mn from the USD 463.0 mn received in 2022. However, the country had significant FDI outflows amounting to USD 138.0 mn in 2023, albeit lower than the USD 410.0 mn recorded in 2022. This is mainly attributed to aggressive hike in US Fed rates, making investments in the US attractive at the expense of emerging markets. • However, we expect the recovering economy to improve investor sentiments leading to a potential of more FDIs in Kenya	Neutral
	Stock Market Valuations	• Foreign investors remained net sellers in 2023, with a net outflows of USD 92.0 mn, compared to net outflows of USD 204.3 mn recorded in FY'2022. The foreign-investor outflows during the year can be attributed mainly to increased sell offs by foreign investors as they exited the market and interest rate hike in developed economies such as US making dollar investments to be more appealing. In 2023, the market closed the year with a P/E of 5.1x, 57.7% below the 12-year historical average of 12.1x, and a dividend yield of 9.4%, 5.0% points above the historical average of 4.4%. This indicates that there may be pockets of value in the Kenyan equities market • We expect the equities market to register muted foreign investments in 2024 attributable to uncertainties in the macro environment attributable to depreciating shilling and elevated inflation	Neutral
	Currency	• In 2024, the shilling is likely to face continued pressure due to i) The persistent current account deficit with Kenya being a net importer, which will increase dollar demand in the market placing more strain on the local currency, ii)the increasing debt servicing costs continue to put pressure on forex reserves. However, we also expect improved diaspora remittances to support the shilling coupled with sufficient forex reserve	Negative

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