Nairobi Metropolitan Area Commercial Office Report – 2024
"Shifting Landscapes"

Cytonn

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I. Overview of Real Estate in Kenya

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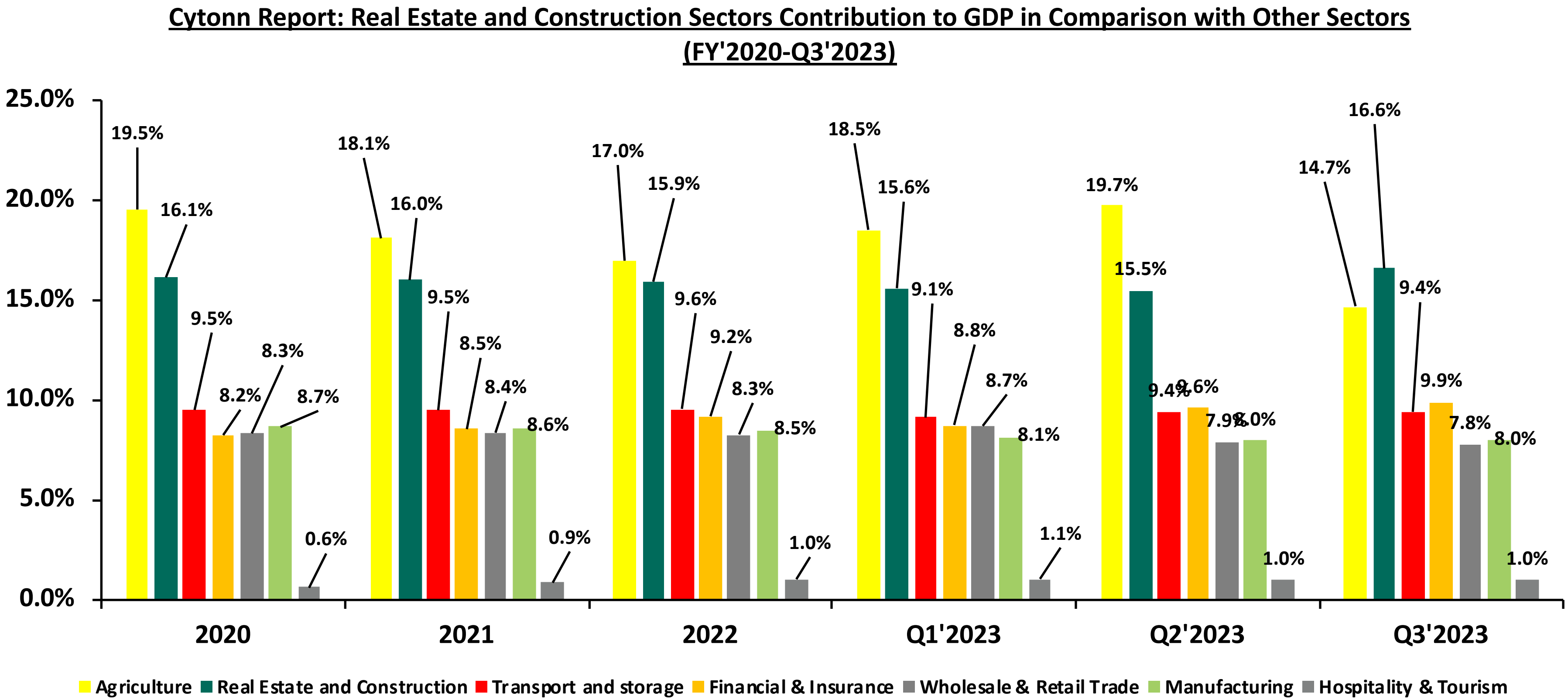
Introduction to Real Estate in Kenya

The Real Estate and construction sectors contributed 16.6% to GDP in Q3'2023, a 1.1% improvement from 15.5% in Q2'2023, evidencing their growing contribution to Kenya's economy

Factor	Characteristics
Macro-economic Contribution	• In 2023, the general Real Estate sector witnessed considerable growth in activity in terms of property transactions and development activities. Consequently, the sector's activity contribution to Gross Domestic Product (GDP) grew by 5.4% to Kshs 785.9 bn in Q3'2023, from Kshs 743.4 bn recorded during the same period in 2022. In addition, the sector contributed 10.5% to the country's GDP, a 0.5% increase from 10.0% recorded in Q2'2023. Cumulatively, the Real Estate and construction sectors contributed 16.6% to GDP, a 1.1% improvement from 15.5% in Q2'2023, evidencing their growing contribution to Kenya's economy. Additionally, the escalation of selling and rental prices persisted, propelled by ongoing inflationary pressures and a depreciated shilling against the United States dollar, leading to an increase in the costs of construction materials
Recent Developments	• In 2023, office supply in the Nairobi Metropolitan Area (NMA) remained subdued with few notable office projects delivered contributing up to 0.1 mn SQFT to the market. These developments comprised Curzon (60,000 SQFT) in Lavington • In H2'2023, Spaces, a subsidiary of IWG (International Workplace Group) and sister brand to Regus, commenced operations on the 14th floor of the prestigious GTC (Global Trade Centre) towers, further highlighting Nairobi's allure as a hub for commercial activities
Real Estate Market outlook	• The overall outlook for the Real Estate sector is **NEUTRAL**, and its performance will be supported by; i) infrastructural development, ii) government and private sector focus on affordable housing, iii) focus on mortgage financing through the KMRC, iv) improved investor confidence amid recovery of the hospitality sector, v) aggressive expansion by both local and international retailers in a bid to maintain market dominance, and, vi) Kenya's positive demographics driving housing demand. • However, factors such as increased construction costs on the back of inflation, constrained financing to developers with increased underdeveloped capital markets, oversupply in select sectors and low investor appetite in Real Estate Investments Trusts (REITs) are expected to subdue the performance of the sector

Introduction to Real Estate in Kenya - GDP Contribution

The Real Estate and Construction sector contributed 16.6% to GDP in Q3’2023, surpassing the Agriculture and Forestry sector that contributed 14.7%,



- The Real Estate and Construction sector contributed 16.6% to GDP in Q3’2023, surpassing the Agriculture and Forestry sector that contributed 14.7%, attributable to increased construction and expansion activities in the market

Source: KNBS

II. Nairobi Metropolitan Area Commercial Office Report

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A. Introduction

Executive Summary

The Commercial Office sector realized an improvement with the average rental yield coming in at 7.7% from 7.6% recorded in FY’2022, due to improved occupancy and rental rates of 0.9% and 7.1% respectively

- We carried out research on 9 nodes within the Nairobi Metropolitan Area (NMA), with an aim of determining the performance and supply of office spaces The 9 nodes are; Gigiri, Kilimani, Upperhill, Nairobi CBD, Karen, Parklands, Westlands, Thika Road, and, Mombasa Road
- In FY’2023, the commercial office sector recorded an improvement in performance with the average rental yield coming in at 7.7% from 7.6% recorded in FY’2022, due to improved occupancy and rental rates of 0.9% and 7.1% respectively
- In terms of sub markets performance, Westlands emerged as the top-performing node, boasting an average rental yield of 8.5%, surpassing the market average of 7.7% by 0.8% points. Gigiri followed closely as the second-best performing node, achieving an average rental yield of 8.2%
- Grade A and Grade B office spaces achieved the highest rental yields, both reaching 7.8%. The strong performance of Grade B offices can be attributed to their growing popularity among tenants, as evidenced by a 0.6% increase in occupancy rates. This rise is mainly due to their comparatively affordable rental rates compared to Grade A offices, which experienced a 2.5% decrease in occupancy rates. Additionally, Grade B offices offer superior technical services compared to Grade C spaces
- The NMA commercial office experienced a consistent oversupply of office space, amounting to 5.8 mn SQFT, similar to 2022 due to escalating construction costs and increasing debt servicing costs on the back of a depreciation currency, which dissuaded developers from initiating new projects or expanding existing ones, thus limiting the influx of additional office space into the market
- We have a **NEUTRAL** outlook for the commercial office sector theme in Nairobi Metropolitan Area (NMA) mainly due to the 6.9 mn SQFT oversupply of space with a rise in incoming new supply at 0.5 mn SQFT. However, the sector will be cushioned by the widespread return to full operational capacity among firms and businesses, driven by improvements in the economy and an increase in the number of start-ups as well as increased entry of international brands, organizations and companies
- Investment opportunities remain promising in areas such as Westlands, Gigiri and Parklands, and which continue to record high returns at 8.5%, 8.2%, and, 8.0%, respectively, compared to the market average of 7.7% as of FY’2023

NMA Commercial Office Report – Overview of the sector

The investment opportunity lies in Westlands, Gigiri and Parklands, which continue to record high returns at 8.5%, 8.2%, and, 8.0%, respectively

Value Area	Summary	Effect on The Office Market
Oversupply	• The oversupply of commercial office space remained unchanged at approximately 5.8 mn SQFT in 2023 • Escalating construction costs and increasing debt servicing costs on the back of a depreciation currency, dissuaded developers from initiating new projects or expanding existing ones, thus limiting the influx of additional office space into the market	• The vacancy rate reduced from 20.6% to 19.7% in 2023 while the average occupancy rates increased by 0.9% points to 80.3%, from 79.4% recorded in 2022 promoting this consistency in over supply
Returns	• In 2023, the commercial office market in the Nairobi Metropolitan Area (NMA) experienced notable growth in overall sector activities compared to 2022. This progress was propelled by heightened demand for quality grade offices. The growth in demand was fuelled by increased interest from international investors, organizations, diplomatic missions, and multinational corporations. Furthermore, the growing preference for convenience and cost-effectiveness by businesses has contributed to the rising popularity of co-working office setups	• The average rental yields came in at 7.7%, 0.1% point higher than the 7.6% recorded in 2022
Opportunity & Outlook	• We have a **NEUTRAL** outlook for the commercial office sector theme in Nairobi Metropolitan Area (NMA) mainly due to the 6.9 mn SQFT oversupply of space with a rise in incoming new supply at 0.5 mn SQFT. However, the sector will be cushioned by the widespread return to full operational capacity among firms and businesses, driven by improvements in the economy and an increase in the number of start-ups as well as increased entry of international brands, organizations and companies • Investment opportunities remain promising in areas such as Westlands, Gigiri and Parklands, and which continue to record high returns at 8.5%, 8.2%, and, 8.0%, respectively, compared to the market average of 7.7% as of FY'2023	• We expect the occupancy rates to contract by 1.1%-points to 79.2% from 80.3% in 2023 mainly attributed to the persisting uncertainties in the economic landscape, continued adoption of remote work policies by companies, and an oversupply of 6.9 mn SQFT of office spaces in 2024. These factors are likely to hinder absorption rates, potentially leading to a decrease in occupancy rates

Key Factors Driving Office Market in Kenya

Nairobi has continued to stand out as a prime investment destination in the region for multinational corporations in 2023

Factor	Characteristics
Serviced Offices/Co-working Spaces	• Serviced offices and co-working spaces are becoming increasingly preferred in Kenya owing to their convenience and adaptability, appealing to both tenants and investors. Such spaces provide a cost-effective and adaptable choice for entrepreneurs and small businesses reluctant to enter into lengthy lease agreements
Growing Demand for Grade A and Green Spaces	• Increased investor awareness and the influx of multinational corporations (MNCs) into Kenya have spurred a rising demand for premium, Grade A office spaces, with a notable focus on sustainability. This trend stems from the preference among many MNCs for developments offering well-appointed work environments that incorporate Environmental, Social, and Governance (ESG) features, including green technology. Developers are increasingly recognizing that occupants prioritize green buildings, which not only confer a marketing competitive edge but also promote sustainability. Green buildings are easier to market compared to traditional ones in addition to their contribution to sustainable practices
Continued Recognition of Nairobi as a Regional Hub	• Nairobi has continued to stand out as a prime investment destination in the region for multinational corporations (MNCs). As illustrated by the establishment of Commonwealth Enterprise and Investment Council (CWEIC)'s regional office in February 2023, Nairobi serves as East Africa’s business hub, underscoring its appeal to international organizations. This positioning positions Nairobi's commercial office sector as a magnet for investments compared to other cities in the region, thus enhancing the sector's performance. Additionally, in H2’2023, Spaces, a subsidiary of IWG (International Workplace Group) and sister brand to Regus, commenced operations on the 14th floor of the prestigious GTC (Global Trade Centre) towers, further highlighting Nairobi's allure as a hub for commercial activities
Positive National Demographics	• Kenya has a relatively high urbanization at 3.7%, 2.2% points higher than the global average of 1.5% according to the World Bank as of 2022. The swift urban growth is fuelling the need for office accommodations as an increasing number of individuals relocate to urban centres in pursuit of employment prospects and enhanced quality of life. This pattern is anticipated to persist as governmental efforts to encourage urbanization and infrastructure development remain ongoing

Challenges Affecting Office Sector

Developers encounter financial constraint challenges in accessing credit loans, with banks tightening their lending terms and requiring more collateral due to escalating default rates

Challenge	Characteristics
Oversupply of Office Space	• In 2023, the Nairobi Metropolitan Area continued to face an excess supply of office space, surpassing current demand levels and resulting in an oversupply of 5.8 mn SQFT. This surplus has contributed to prolonged vacancy rates, prompting developers to adopt a cautious "wait-and-see" approach regarding new construction projects until the surplus office space is absorbed. Nairobi has long grappled with an oversupply of office space, exacerbated by escalating capital costs, further contributing to developers' cautious stance toward new investments
Remote/ Hybrid Working Model	• The implementation of remote or hybrid work setups by certain companies has adversely affected the overall occupancy rates of office spaces and landlords' returns. However, transitioning from full remote work to a hybrid model by select companies is anticipated to enhance the office occupancy rate within the sector
Difficulty in Accessing Financing	• Developers encounter financial constraints as they face challenges in accessing credit loans, with banks tightening their lending terms and requiring more collateral due to escalating default rates. Gross Non-Performing Loans (NPLs) in the Real Estate sector surged by 29.5% to Kshs 97.9 bn in Q3'2023 from Kshs 75.6 bn in Q3'2022. This situation is exacerbated by the soaring construction costs, which averaged Kshs 6,615 in 2023, marking a 27.0% increase from the Kshs 5,210 recorded in 2022. The surge in construction expenses is primarily attributed to the escalating costs of imported materials, notably steel and cement, along with heightened fuel prices. Consequently, construction projects are encountering budgetary constraints and potential delays, posing significant challenges to the growth and development of the sector

Highlights in the Commercial Office Sector

Office supply in the NMA remained subdued with few notable office projects delivered contributing up to 0.1 mn SQFT to the market

Highlight	Details
New Developments	• In 2023, office supply in the Nairobi Metropolitan Area (NMA) remained subdued with few notable office projects delivered contributing up to 0.1 mn SQFT to the market. These developments comprised Curzon (60,000 SQFT) in Lavington. • Additionally, some of the expansion activities witnessed in the sector include; i. IWG unveiled 16,297 SQFT of workspace on the 14th floor of Nairobi's prestigious Global Trade Centre (GTC) in Westlands ii. New flexible workspace branches like Regus, Spaces, and Ikigai were also opened up in Westlands

Source: Knight Frank, Cytonn Research

B. Commercial Office Supply in Nairobi

Commercial Office Space Supply-Nairobi

The NMA commercial market supply reduced to 0.1 mn SQFT in 2023

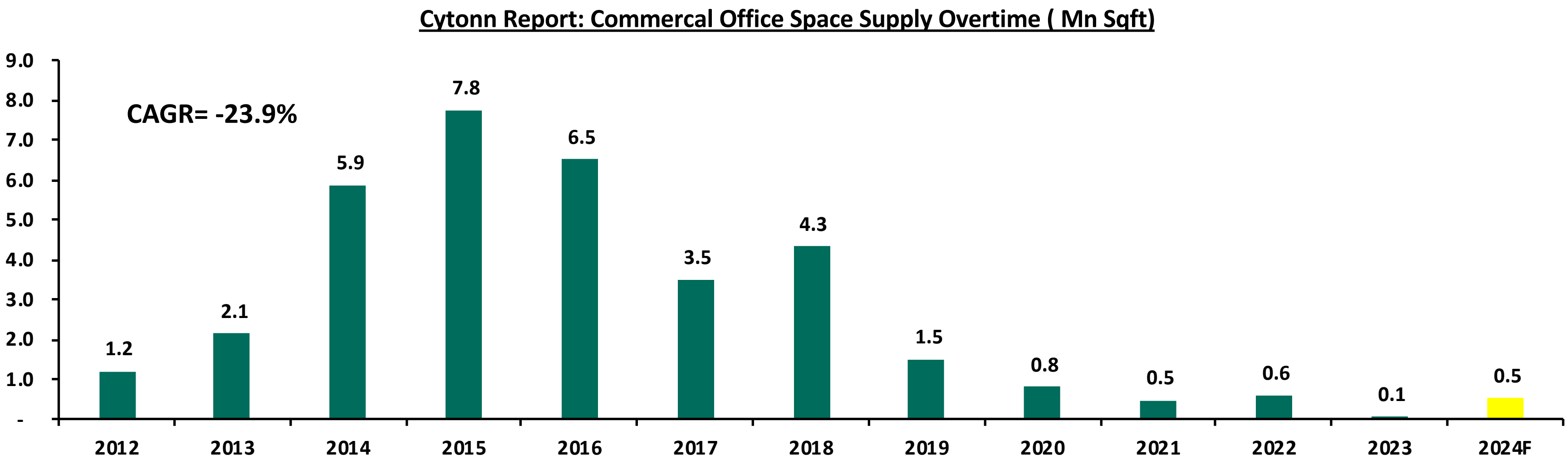
Cytonn Report: Nairobi Metropolitan Area Commercial Office Space Supply						
Major Commercial Office Completion in 2023				Major Incoming Commercial Office Space Supply in 2024		
#	Development	Location	Size (SQFT)	Development	Location	Size (SQFT)
1	Curzon	Lavington	60,000	Purple Tower	Mombasa Road	197,800
2				The Atrium	Westlands	100,000
3				CCI HQ	Tatu City	233,168
Total	**60,000**			**530,968**		

Source: Knight Frank, Cytonn Research

- In 2023, office supply in the Nairobi Metropolitan Area (NMA) remained subdued with few notable office projects delivered contributing up to 0.1 mn SQFT to the market
- This was attributed to escalating construction costs and increasing debt servicing costs on the back of a depreciation currency, which dissuaded developers from initiating new projects or expanding existing ones, thus limiting the influx of additional office space into the market. Additionally, the surge in gross Non-Performing Loans (NPLs) within the Real Estate sector constrained developers' capacity to fund new ventures, prompting them to defer or postpone developments until market conditions stabilized and financing accessibility improved

Commercial Office Space Supply - Nairobi Continued…

The office supply in the NMA realized a 11 year CAGR decline of 23.9% from 1.2 mn in 2012 to 0.1 mn in 2023



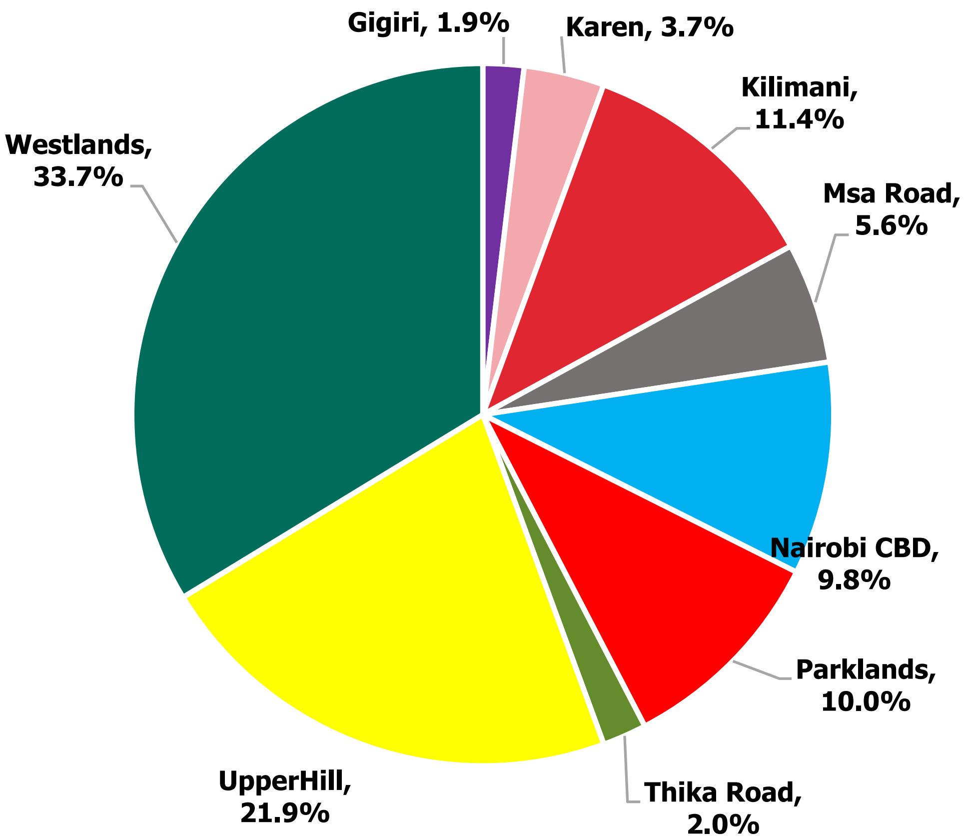
Source: Cytonn Research

- An additional 0.5 mn SQFT of space is set to be introduced into the market in 2024. This upcoming supply includes projects such as CCI Headquarters in Tatu City, Purple Tower in Mombasa Road and The Atrium situated in Westlands
- During 2023, the improved demand led to slightly higher absorption rates of both new and existing developments throughout 2023, even with the introduction of 0.1 mn SQFT of office space into the market—an 83.3% reduction from the 0.6 mn SQFT supplied in 2022. Looking ahead, the injection of an additional 0.5 mn SQFT of office space in 2024 is expected to further exacerbate the oversupply challenge and weigh down on absorption rates

Commercial Office Space Supply – Market Share

Westlands and Upperhill had the highest office supply with market shares of 33.7% & 21.9%, respectively

Cytonn Report: Office Market Share Supply 2023



Source: Cytonn Research 2022

- Westlands, Upperhill and Kilimani had the largest supply of Nairobi office space in 2023, with market shares of 33.7%, 21.9% and 11.4%, respectively
- On the side, Gigiri and Thika Road had the lowest supply with a market share of 1.9% and 2.0% respectively
- Westlands and Upperhill have grown as business nodes as firms move away from the CBD due to traffic congestion and in search of better quality space, hence the high supply

C. Commercial Office Market Performance

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Commercial Office Market Performance Summary

The Commercial Office sector realized a 0.1%-point increase in average rental yields in 2023 to 7.7%, from 7.6% recorded in 2022 attributable to increased occupancy and rental rates

(All Values in Kshs Unless Stated Otherwise)										
Cytonn Report: Commercial Office Performance Over Time										
Year	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**y/y Δ 2023**
Occupancy (%)	89.0%	88.0%	82.6%	83.8%	80.3%	77.7%	77.6%	79.4%	**80.3%**	**0.9%**
Asking Rents (Kshs/SQFT)	97	97	101	101	96	93	94	96	**103**	**7.1%**
Average Prices (Kshs/SQFT)	12,776	12,031	12,649	12,407	12,638	12,280	12,106	12,223	**12,673**	**3.6%**
Node Average Rental Yields (%)	**8.1%**	**8.5%**	**7.9%**	**8.3%**	**7.5%**	**7.0%**	**7.3%**	**7.6%**	**7.7%**	**0.1%**

Source: Cytonn Research

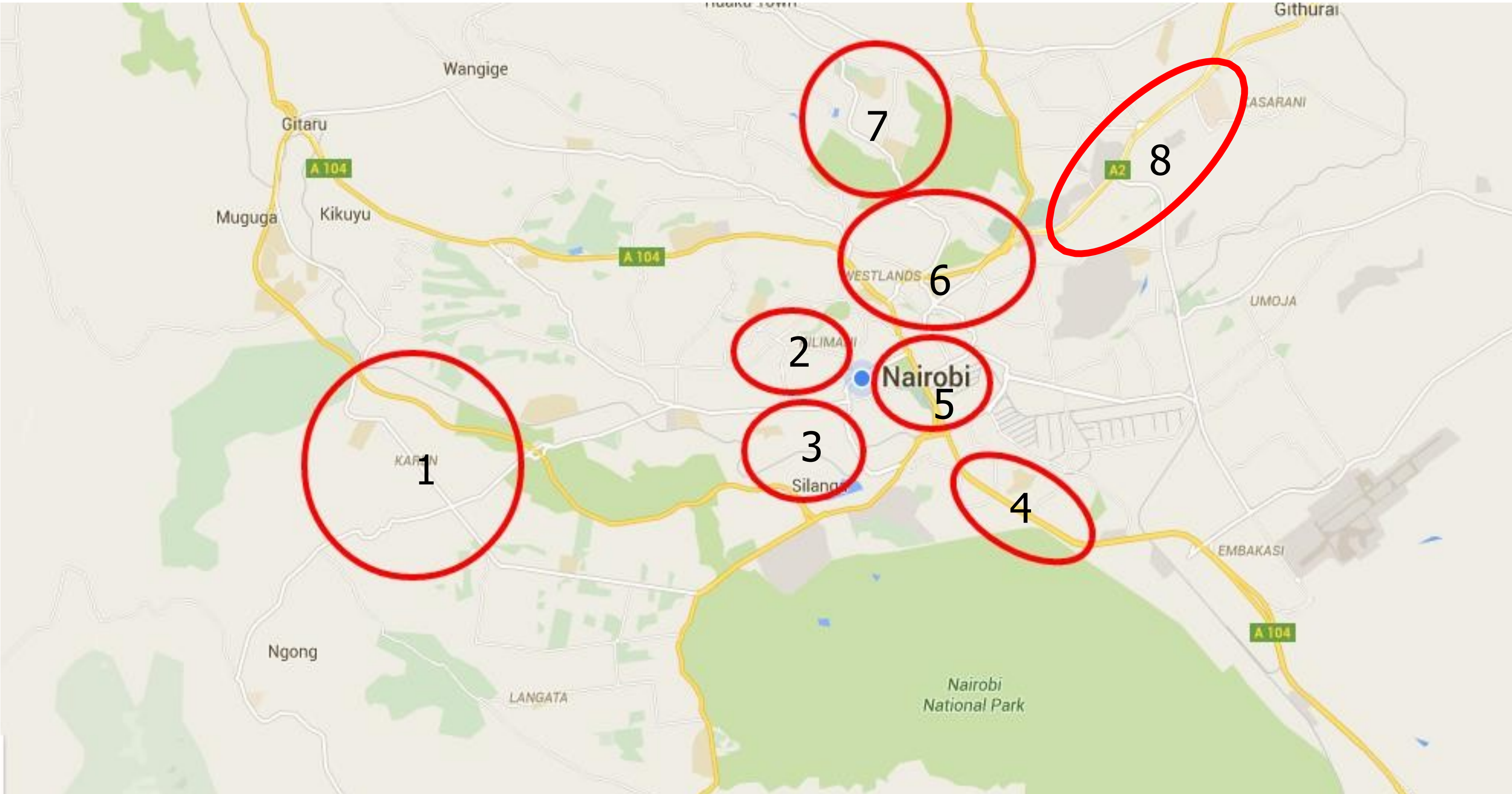
- The Commercial Office sector realized a 0.1%-point increase in average rental yields in 2023 to 7.7%, from 7.6% recorded in 2022 attributable to increased occupancy and rental rates. Average asking rents per SQFT in the Nairobi Metropolitan Area (NMA) increased by 7.1% to Kshs 103 per SQFT from Kshs 96 per SQFT in 2022. Additionally, occupancy rates increased by 0.9%-points to 80.3% from 79.4% achieved in 2022

- The sector's improved performance can be attributed to various factors, including: i) the gradual resurgence of demand for physical spaces as more firms resumed full operations, ii) increased availability of high-quality Grade A office spaces, exemplified by The Piano, The Cube, Karen Green, Principal Place, iii) expansion and entry strategies adopted by multi-national and international companies bolstering occupancy rates, and iv) a more stable and favourable business environment post-COVID-19

i. Performance by Nodes

Major Commercial Office Nodes in the Nairobi Metropolitan Area

The key nodes of focus are in Karen, Kilimani, Upperhill, Westlands, Msa Rd, Nairobi CBD, Parklands, Thika Road and Gigiri



- ***Key: 1. Karen 2. Kilimani 3. Upper Hill 4. Mombasa Road 5. CBD 6. Westlands & Parklands 7. Gigiri 8. Thika Road***

Nairobi Office Sub-Market Performance

Westlands emerged as the top-performing node, boasting an average rental yield of 8.5%, surpassing the market average of 7.7% by 0.8% points

(All values in Kshs unless stated otherwise)

Cytonn Report: Nairobi Metropolitan Area Commercial Office Market Performance FY'2023											
Area	Price/SQFT FY 2022	Rent/SQFT FY 2022	Occupancy FY 2022(%)	Rental Yields FY 2022(%)	Price Kshs/SQFT FY 2023	Rent Kshs/SQFT FY 2023	Occupancy FY 2023(%)	Rental Yield FY 2023(%)	Δ in Rent	Δ in Occupancy	Δ in Rental Yields
Westlands	12,032	108	75.7%	8.3%	12,504	120	75.1%	8.5%	11.1%	(0.6%)	0.2%
Gigiri	13,500	118	81.0%	8.7%	15,000	128	79.8%	8.2%	8.5%	(1.2%)	(0.5%)
Parklands	11,662	91	81.0%	7.7%	11,875	92	85.8%	8.0%	1.0%	4.8%	0.3%
Kilimani	12,260	92	80.8%	7.7%	13,051	102	83.6%	7.9%	11.0%	2.8%	0.3%
Karen	13,431	111	83.0%	8.3%	14,246	115	80.1%	7.8%	4.2%	(2.9%)	(0.4%)
Nairobi CBD	11,971	83	84.4%	7.3%	12,000	90	85.0%	7.6%	7.4%	0.6%	0.3%
Upperhill	12,605	97	75.0%	7.1%	13,086	100	75.2%	6.8%	3.1%	0.2%	(0.3%)
Thika Road	12,571	79	77.9%	6.0%	12,571	79	79.4%	6.0%	0.0%	1.6%	(0.1%)
Mombasa Road	11,325	71	65.5%	5.1%	11,325	72	74.5%	5.7%	0.7%	9.0%	0.6%
Average	**12,223**	**94**	**79.4%**	**7.6%**	**12,673**	**103**	**80.3%**	**7.7%**	**7.1%**	**0.9%**	**0.1%**

Source: Cytonn Research

- Westlands emerged as the top-performing node, boasting an average rental yield of 8.5%, surpassing the market average of 7.7% by 0.8% points. Gigiri followed closely as the second-best performing node, achieving an average rental yield of 8.2%. Parklands secured the third position with an average rental yield of 8.0%

Nairobi Office Sub-Market Performance, Continued…

Mombasa Road was the least performing node in FY'2023 recording an average rental yield of 5.7%, which was 2.0%-points lower than the market average of 7.7%

- The high demand for premium office spaces and the attractiveness of investment opportunities in these areas can be attributed to several key factors: i) these nodes boast a significant concentration of top-quality office buildings that command premium rental rates and yields, ii) landlords in these areas tend to favor collecting rent in dollars, enhancing the investment appeal, iii) the presence of ample infrastructure and amenities adds value to investments in these locations, and iv) the prominence of multinational corporations, international organizations, and embassies in these areas drives up the demand for quality office spaces, and,
- On the contrary, Mombasa Road emerged as the least performing node in FY'2023, recording an average rental yield of 5.7%, which was 2.0%-points lower than the market average of 7.7%
- Several factors contributed to this underperformance: i) the prevalence of lower quality office buildings in this area results in lower average rental rates, averaging at Kshs 72 per SQFT, ii) its predominant reputation and recognition as an industrial zone, which diminishes its appeal to office-based businesses seeking commercial spaces, and, iii) stiff competition from other sub-markets further exacerbates the challenges faced by the zone in attracting tenants and achieving higher rental yields

Nairobi Office Market Performance, Continued…

Gigiri closely trailed as the second-best performing node, securing an average rental yield of 8.2%

Westlands

- Westlands emerged as the leading node, achieving an average rental yield of 8.5%, exceeding the market average of 7.7% by 0.8% points. This performance also marked a 0.2% points increase from the 8.3% recorded in 2022. The enhanced performance was primarily attributed to the presence of high-quality grade offices commanding premium rental rates, the demand generated by Multinational Corporations (MNCs) and organizations seeking superior office spaces, and the availability of robust infrastructure and amenities in the vicinity, such as the Nairobi Expressway and Waiyaki Way, which improve accessibility

Gigiri

- Gigiri closely trailed as the second-best performing node, securing an average rental yield of 8.2%. However, this marked a slight decline of 0.5% from the 8.7% achieved in 2022. Notably, there was an 8.5% increase in average rental rates to Kshs 128 per SQFT from Kshs 118 per SQFT in 2022, which coincided with a 1.2% decrease in average occupancy rates to 79.8% from 81.0%. The rise in rental rates, while aimed at maximizing returns, led to a reduction in occupancy rates as some tenants were deterred by the higher costs

Parklands

- Parklands recorded an average rental yield of 8.0% in 2023, 0.5% points higher than 0.3% recorded in 2022. The average occupancy rates increased by 4.8% to 85.8% from 81.0% in 2022. Average rents stand at Kshs 92, a 1.0% from Kshs 91 in 2022. Parklands is growing in popularity as an office hub, and is catching up to its neighboring Westlands area

Nairobi Office Market Performance, Continued…

Despite the 7.4% increase in rental prices in Nairobi CBD in 2023, average rental rates were still affordable compared to most nodes

Kilimani

- Kilimani recorded average rental yields of 7.9% in 2023, a 0.2% points increase from the 7.7% recorded in 2022. Kilimani average occupancy and rental rates in 2023 stood at 83.6% and Kshs 102 per SQFT. The commercial office market in Kilimani is majorly influenced by; i) its proximity to CBD and centrality in location which make it easily accessible from many areas in Nairobi, which is convenient, ii) good infrastructure linking Kilimani to multiple Nairobi surburbs, and, ii) the presence of various government embassies making it ideal and attractive for office investments, such as the Nigerian, Chinese, Ethiopian, and Zambian Embassies, among others

Karen

- Karen posted an average rental yield of 7.8% in 2023, marking a slight decrease of 0.4% points from the 8.3% recorded in 2022. Like Gigiri, this decline in rental yield can be linked to a 4.2% increase in rental rates, which in turn resulted in a 2.9% drop in occupancy rates to 80.1% from 83.0% in 2022 as some tenants were deterred by the higher costs

Nairobi CBD

- The Nairobi CBD recorded an average rental yield of 0.3% in 2023, reflecting a significant 7.4% points increase in rental rates to Kshs 90 from Kshs 83. Furthermore, occupancy rates saw a slight 0.6% improvement to 85.0% from 84.4% in 2022. This improvement can be attributed to the growing demand for centrally located office spaces and the implementation of revitalization efforts within the CBD, attracting businesses seeking convenient access to key amenities and transportation hubs. Despite the 7.4% increase in rental prices in 2023, average rental rates were still affordable compared to most nodes

Nairobi Office Market Performance, Continued…

Mombasa Road emerged as the least performing node in FY'2023, recording an average rental yield of 5.7%, which was 2.0%-points lower than the market average of 7.7%

Upperhill

- Upperhill witnessed a marginal 0.3% points decline in average rental yields, settling at 6.8% in 2023, down from 7.1% in 2022. Despite this, there was a notable 3.1% increase in rental prices and a slight 0.2% uptick in occupancy rates. These changes can be attributed to increased demand for premium office spaces and improved infrastructure, which collectively contributed to the upward pressure on rental prices

Thika Road

- Thika Road saw a marginal 0.1% decline in average rental yields in 2023, although this was balanced by a noteworthy 1.6% increase in occupancy rates, rising from 77.9% in 2022 to 79.4% in 2023. Despite this, rental rates remained unchanged during the period. This can be attributed to an increase in demand for office spaces along Thika Road

Mombasa Road

- Mombasa Road emerged as the least performing node in FY'2023, recording an average rental yield of 5.7%, which was 2.0%-points lower than the market average of 7.7%. Several factors contributed to this underperformance: i) the prevalence of lower quality office buildings in this area results in lower average rental rates, averaging at Kshs 72 per SQFT, ii) its predominant reputation and recognition as an industrial zone, which diminishes its appeal to office-based businesses seeking commercial spaces, and, iii) stiff competition from other sub-markets further exacerbates the challenges faced by the zone in attracting tenants and achieving higher rental yields

ii. Performance by Grades

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Classification of Offices in Nairobi

Major categories of commercial office buildings in Kenya

- Commercial office buildings are categorized into three main classes based on the quality and sizes of office spaces as follows:

i. **Grade A:** These are high quality office buildings characterized by their adequate amenities, facilities, and finishes. They therefore fetch higher rental rates and yields compared to other office types. Also these office building sizes range from 100,001 - 300,000 SQFT,

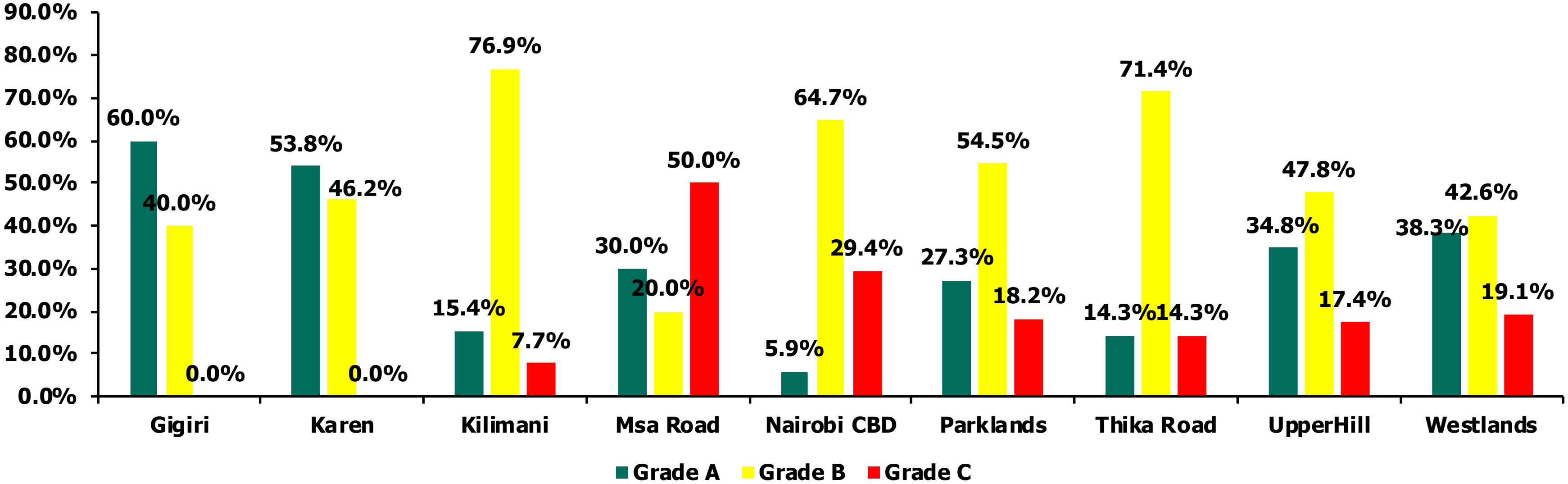
ii. **Grade B:** These office buildings have their sizes ranging between 50,000 to 100,000 SQFT. They have good amenities and services, however not as good as Grade A offices, hence charge moderate rental rates, and,

iii. **Grade C:** These buildings are usually old, hence their lack of adequate services and facilities. Usually, they charge rents below the average market rate

Distribution of Various Classes Offices

Grade B offices accounted for the largest share of office space in the NMA at 52.4%

Cytonn Report: Office Space Distribution by Grades (2023)



Source: Cytonn Research

- Based on our analysis of office grade distribution, Grade B offices dominated the office space market in the Nairobi Metropolitan Area during 2023, comprising 52.4% of the total market share. However, this reflects a slight decline of 1.7%-points from 54.1% in 2022. This decrease can be attributed to the increased completion of Grade A offices, exemplified by developments like Curzon in Lavington. Notably, the supply of Grade A office spaces expanded by 1.8% to reach 30.0% from the previous 28.2%
- In our nodal analysis, Gigiri, Karen, Westlands, and Upperhill exhibited the highest proportion of Grade A offices, accounting for 60.0%, 53.8%, 38.3%, and 34.8% respectively of their total office space inventory

Distribution of Various Classes Offices, Continued…

Mombasa Road accounted for the largest share of Grade C office space in the NMA at 50.0%

- Conversely, Kilimani maintained the highest percentage of Grade B offices at 76.9%. Regarding Grade C offices, Mombasa Road retained a significant share of office spaces, comprising 50.0% of the current market share, which remained relatively unchanged from 2022
- In terms of concentration, Mombasa Road boasted the highest mix of office types, with Grade A, Grade B, and Grade C office spaces making up 30.0%, 20.0%, and 50.0% respectively of its total office inventory

Distribution of Various Classes Offices

Grade A and Grade B office spaces achieved the highest rental yields, both reaching 7.8%

(All Values in Kshs Unless Stated Otherwise)											
Cytonn Report: Commercial Office Performance Based on Grades 2023											
Office Grade	**Price 2022 Kshs/SQFT**	**Rent 2022 Kshs/SQFT**	**Occupancy 2022**	**Rental Yield 2022**	**Price 2023 Kshs/SQFT**	**Rent 2023 Kshs/SQFT**	**Occupancy 2023**	**Rental Yield 2023**	**Δ Rent y/y**	**Δ Occupancy y/y**	**Δ Rental Yield y/y**
Grade A	13,040	104	79.0%	**7.7%**	13,695	119	76.4%	**7.8%**	**12.6%**	**(2.5%)**	**0.2%**
Grade B	12,292	97	81.6%	**7.8%**	12,572	99	82.2%	**7.8%**	**2.0%**	**0.6%**	**0.0%**
Grade C	10,867	83	73.2%	**6.7%**	11,124	86	77.0%	**7.2%**	**3.7%**	**3.8%**	**0.4%**

Source: Cytonn Research

- Grade A and Grade B office spaces achieved the highest rental yields, both reaching 7.8%. The strong performance of Grade B offices can be attributed to their growing popularity among tenants, as evidenced by a 0.6% increase in occupancy rates. This rise is mainly due to their comparatively affordable rental rates compared to Grade A offices, which experienced a 2.5% decrease in occupancy rates. Additionally, Grade B offices offer superior technical services compared to Grade C spaces. However, Grade C office spaces demonstrated the most significant improvement in occupancy rates, increasing by 3.8% in 2023,
- Grade A offices saw the most substantial Year-on-Year (y/y) rise in rental rates, increasing by 12.6% in 2023 to Kshs 119 per SQFT from Kshs 104 per SQFT in 2022. This surge is credited to; i) the premium quality of Grade A spaces, which command higher rents, ii) heightened demand from multinational corporations and organizations, and iii) the preference amongst landlords of prime commercial offices to collect rent in dollars against the depreciation of the Kenyan Shilling during the year,

Distribution of Various Classes Offices

Grade C offices experienced the most significant rise in rental yield, increasing by 0.4%

- Grade B offices saw no change in average rental yields, which can be attributed to the stable demand for these spaces coupled with competitive rental rates compared to Grade A and C office spaces. However, there was a 0.6% increase in average occupancy rates attributable to the flexibility and affordability of Grade B offices, making them a preferred choice for tenants seeking quality office space within a reasonable budget, and,
- Grade C offices experienced the most significant rise in rental yield, increasing by 0.4%. This notable improvement can be credited to a substantial increase in occupancy rates, which surged by 3.8% from 73.2% in 2022 to 77.0% in 2023 due to their affordability

iii. Performance by Nodes & Grades

Cytonn

Performance by Nodes and Grades

For Grade B spaces, Gigiri and Westlands offered the highest rental yields of 8.7% and 8.6% respectively

Cytonn Report: Commercial Office Performance in 2023 by Nodes and Grades						
	Grade A		Grade B		Grade C	
Location	Average of Occupancy (%)	Average of Rental Yield	Average of Occupancy (%)	Average of Rental Yield	Average of Occupancy (%)	Average of Rental Yield
Gigiri	79.0%	8.7%	81.0%	7.5%		
Karen	80.0%	7.5%	80.2%	8.1%		
Kilimani	79.8%	8.0%	85.3%	8.3%	75.0%	4.6%
Msa Road	76.7%	5.5%	75.0%	6.4%	73.0%	5.5%
Nairobi CBD	45.0%	4.7%	87.8%	7.8%	86.8%	7.8%
Parklands	86.7%	8.0%	85.2%	8.0%	86.7%	8.0%
Thika Road	85.0%	7.0%	80.2%	5.9%	70.0%	5.1%
Upperhill	78.6%	7.2%	75.7%	6.6%	67.3%	6.3%
Westlands	70.7%	8.6%	78.8%	8.1%	76.0%	8.8%

Source: Cytonn Research

- In 2023, Grade A offices in Gigiri and Westlands achieved the highest rental yields, reaching 8.7% and 8.6% respectively. This was due to; i) their strategic locations, attracting high-end clientele willing to pay premium rates, often in dollars, ii) the presence of adequate amenities and infrastructure in these areas enhancing accessibility, iii) the tranquil environment offered ideal office settings away from the city centre's hustle and bustle. On the other hand, Grade B offices in Kilimani, Karen, and Westlands boasted the highest rental yields at 8.3% for Kilimani and 8.1% for both Karen and Westlands. Similarly, Grade C offices in Westlands and Parklands delivered the best returns with average rental yields reaching 8.8% and 8.0% respectively

iv. Serviced Offices Performance

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Serviced Offices Performance

Serviced offices in Karen and Kilimani recorded the most substantial rent hikes of 8.5% and 8.4% respectively

(All values in Kshs Unless Stated Otherwise)

Cytonn Report: Nairobi Metropolitan Area Serviced Office Performance						
Location	Revenue Per SQFT 2022		Revenue Per SQFT 2023		Serviced Offices Revenue growth (%)	Unserviced Offices Revenue growth (%)
	Serviced Offices	Un-serviced Offices	Serviced Offices	Un-serviced Offices		
Westlands	220	108	237	120	6.9%	10.0%
Karen	199	111	217	115	8.5%	4.0%
Parklands	171	91	185	92	7.4%	1.0%
Gigiri	210	118	230	128	6.5%	7.8%
Upperhill	243	97	243	100	0.0%	3.0%
Kilimani	199	92	217	102	8.4%	9.9%
Nairobi CBD	168	83	167	90	(0.5%)	6.9%
Msa Rd	-	71	180	72	0.0%	0.7%
Thika Rd	110	79	114	79	3.8%	0.0%
Average	**190**	**94**	**199**	**103**	**5.9%**	**5.4%**

Source: Cytonn Research

- In 2023, serviced offices experienced a 5.9% year-on-year (y/y) growth in rental revenues, with average rental rates rising to Kshs 199 per SQFT, up from Kshs 190 per SQFT in 2022. In contrast, unserviced offices saw a revenue increase of 5.4%, with average rental rates climbing to Kshs 103 per SQFT in 2023, compared to Kshs 94 per SQFT in 2022
- Notably, serviced offices in Karen and Kilimani recorded the most substantial rent hikes of 8.5% and 8.4% respectively

Serviced Offices Performance, Continued…

Westlands established itself as the leading office hub with the introduction of new flexible workspace branches like Regus, Spaces, and Ikigai

- The improved performance in these areas can be attributed to several factors: i) the presence of quality infrastructure, enhancing accessibility, ii) increased demand for serviced offices driven by a high-end clientele and international firms with evolving preferences, iii) diverse themes and sophisticated designs demanding top-tier standards, and, iv) high-quality facilities attracting premium rents, often in dollars

Co-working Spaces

- In 2023, there was a noticeable surge in the development of specialized office spaces tailored to specific niches in Kenya, particularly in the realm of co-working spaces. Westlands, for example, established itself as the leading office hub with the introduction of new flexible workspace branches like Regus, Spaces, and Ikigai
- Illustrating this trend, IWG, a global leader in hybrid working solutions known for its prestigious line-up of brands like Spaces and Regus, unveiled a workspace centre on the 14th floor of Nairobi's prestigious Global Trade Centre Westlands. Spanning an impressive 16,297 SQFT, this centtr offers a diverse array of co-working zones, private offices, cutting-edge meeting facilities, and inspiring creative spaces.

Serviced Offices Performance, Continued…

We expect a rise in the establishment of additional co-working spaces in the future

- We expect a rise in the establishment of additional co-working spaces in the future. According to Knight Frank's H1 2023 Kenya Market Update, sizable corporations with more than 50,000 employees will likely decrease their leased office space by 10.0% to 20.0%, aiming to streamline expenses and optimize the advantages of adaptable work environments. The table below highlights major co-working office spaces released into the market in 2023;

Cytonn Report: Notable Co-working Space Office Developments delivered in 2023				
#	**Space provider**	**Office Name**	**Location**	**Size (SQFT)**
1	IWG Spaces-brand	14th Floor GTC	Westlands	16,297
	Total			**16,297**

Source: Cytonn Research, Knight Frank

D. Office Space Opportunity

Office Space Opportunity – Methodology

Gap Analysis was used to estimate over/undersupply situation in the market, where supply is subtracted from demand, and if a positive, the market is undersupplied, with a negative indicating an oversupply

- Gap analysis is a tool that measures the under or oversupply situation of an office market using demand and supply dynamics
- To gauge the supply situation in Nairobi, we used the **Gap Analysis** technique
- **Demand** is calculated by adding up net absorption (space taken up in a market in a year) by the space required to replenish depreciated office stock
- **Supply** is calculated by summing up the completed office stock in a given year and the vacant stock from the previous year
- To get the over/undersupply in the market, the supply is subtracted from the demand
- If it is a positive figure then the market has an under supply that is demand is more than supply and if it is a negative figure then the market has an oversupply that is supply is more than demand
- **Based on building plan approvals data, in 2023, the market had a supply of 7.5 mn SQFT against a demand of (1.7) mn SQFT resulting in an oversupply of 5.8 mn SQFT assuming a lag between building approvals and completion of construction**

Office Space Opportunity

In 2023, the commercial office sector had an oversupply of 5.8 mn SQFT

Cytonn Report: Nairobi Metropolitan Area Office Space Analysis													
Year	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024 F**
Stock (Mn SQFT)	7.7	9.7	15.4	22.9	28.9	31.8	35.5	36.3	36.4	36.8	37.4	**36.9**	36.7
Completions (Mn SQFT)	1.2	2.1	5.9	7.8	6.5	3.5	4.3	1.5	0.8	0.5	0.6	**0.1**	0.5
Vacancy Rate (%)	9.0%	10.0%	10.0%	11.0%	12.0%	16.8%	16.7%	19.5%	22.3%	22.1%	20.6%	**19.7%**	20.8%
Vacant Stock (Mn SQFT)	0.7	1.0	1.5	2.5	3.5	5.3	5.9	7.1	8.1	8.1	7.7	**7.3**	7.6
Occupied Stock (Mn SQFT)	7.1	8.8	13.9	20.3	25.4	26.5	29.6	29.2	28.3	28.7	29.7	**29.6**	29.1
Net Absorption	1.0	1.7	5.1	6.5	5.1	1.0	3.1	(0.4)	(1.0)	0.4	1.0	**0.9**	(0.6)
Demand	1.1	1.9	5.3	6.8	5.6	1.6	3.7	0.4	(0.2)	1.2	1.8	**1.7**	0.2
Available Supply, AS(T)	1.7	2.6	6.5	8.8	8.4	6.3	9.0	6.7	7.1	7.9	7.6	**7.5**	7.1
Gap, GAP(T)	**(0.5)**	**(0.8)**	**(1.2)**	**(2.1)**	**(2.9)**	**(4.7)**	**(5.2)**	**(6.3)**	**(7.3)**	**(6.7)**	**(5.8)**	**(5.8)**	**(6.9)**

Source: KNBS, NCG Completions data, Cytonn Research

Office Space Opportunity

Some zones still have relatively low supply and high returns, such as Gigiri with a market share of 1.9% and a rental yield of 8.2% thus offering a good investment opportunity

Concept/Market Niche	Characteristics
Mixed-Use Developments	• Mixed-Use Development (MUD) refers to a Real Estate development containing more than one Real Estate theme • In 2023, they had attractive returns with average rental yields of up to 8.4%. Such developments will increase the occupancy rates of a building due to their convenience and hence the greater returns to investors
Serviced Offices	• In 2023, serviced offices experienced a 5.9% year-on-year (y/y) growth in rental revenues, with average rental rates rising to Kshs 199 per SQFT, up from Kshs 190 per SQFT in 2022. In contrast, unserviced offices saw a revenue increase of 5.4%, with average rental rates climbing to Kshs 103 per SQFT in 2023, compared to Kshs 94 per SQFT in 2022
Low Supply Zones	• Despite the oversupply in the market, some zones still have relatively low supply and high returns such as Gigiri with a market share of 1.9% and a rental yield of 8.2% thus offering a good investment opportunity
New Markets	• Westlands emerged as the top-performing node, boasting an average rental yield of 8.5%, surpassing the market average of 7.7% by 0.8% points. Gigiri followed closely as the second-best performing node, achieving an average rental yield of 8.2%. Parklands secured the third position with an average rental yield of 8.0% • In our nodal analysis, Gigiri, Karen, Westlands, and Upperhill exhibited the highest proportion of Grade A offices, accounting for 60.0%, 53.8%, 38.3%, and 34.8% respectively of their total office space inventory • Undersupplied zones such as Thika Road and Gigiri that currently have market shares of 2.0% and 1.9%

E. Office Market Conclusion and Outlook

Office Market Conclusion and Outlook

Our overall outlook for the Commercial Office sector is Neutral, with a current oversupply of 6.9 mn SQFT, in the Nairobi Metropolitan Area (NMA)

Cytonn Report: Nairobi Commercial Office Outlook				
Measure	**2022 Sentiment**	**2023 Sentiment and 2024 Outlook**	**2023 Review**	**2024 Outlook**
Supply	The sector recorded an oversupply of 5.8 mn SQFT of office space in 2022, a 13.4% decrease from the 6.7 mn SQFT realized in 2021 in NMA. This was due to increased demand for office spaces which in turn increased the occupancy rates by 1.8% points to 79.4% in 2022 from 77.6% in 2021 at the back of the continuous recovery of the economy in post-COVID-19 period. This is as most corporate organizations and businesses reverted to full operations and use of physical spaces. The incoming supply in 2022 came at 0.6 mn SQFT 20.0% higher than the 0.5 mn SQFT recorded in 2021	The oversupply of commercial office space remained unchanged at approximately 5.8 mn SQFT in 2023. Escalating construction costs and increasing debt servicing costs on the back of a depreciation currency, dissuaded developers from initiating new projects or expanding existing ones, thus limiting the influx of additional office space into the market. Despite the persistent oversupply, there was a notable decline in the average office vacancy rate, decreasing from 20.6% in 2022 to 19.7% in 2023. This decline was attributed to the gradual recovery in demand for office space following the impact of the COVID-19 pandemic in 2020. Consequently, the improved demand led to faster absorption rates of both new and existing developments throughout 2023, even with the introduction of 0.1 mn SQFT of office space into the market—an 83.3% reduction from the 0.6 mn SQFT supplied in 2022 In 2024, we expect the office space oversupply to increase by 19.0% to 6.9 mn SQFT in 2024 from 5.8 mn SQFT in 2023 due to an increase in incoming supply However, we expect rising construction costs, elevated credit risk and relatively higher debt servicing costs on the back of continued currency depreciation will impact on the optimal supply of newer office developments by developers subsequently limiting incoming new supply	Neutral	Neutral

Office Market Conclusion and Outlook

We expect the occupancy rates to contract by 1.1%-points to 79.2% from 80.3% in 2023

Cytonn Report: Nairobi Commercial Office Outlook				
Measure	**2022 Sentiment**	**2023 Sentiment and 2024 Outlook**	**2023 Review**	**2024 Outlook**
Demand	There was an increased demand for office spaces in the NMA, evidenced by the 1.8% increase in the average occupancy rates which came in at 79.4% in 2022 from 77.6% recorded in 2021. This was mainly attributed to a slow but rising demand for physical space on the back of various firms resuming full operations, coupled with the expansion strategy by various firms such as Call Centre International (CCI) Group and the rising trend in serviced office spaces spearheaded by firms like Nairobi Garage, Kofisi, and Regus. In addition to this, the absorption of office spaces increased by 150.0% to 1.0 mn SQFT in 2022 from 0.4 mn SQFT recorded in 2021 attributed to a further increase of occupation of physical unserviced and serviced spaces at the back of full operations of businesses and organisations	In 2023, there was an increased demand for office spaces in the NMA, evidenced by the 0.9% increase in the average occupancy rates which came in at 80.3% in 2023 from 79.4% recorded in 2022. This was mainly attributed to i) the gradual resurgence of demand for physical spaces as more firms resumed full operations, increased availability of high-quality Grade A office spaces, exemplified by The Piano, The Cube, Karen Green, Principal Place, iii) expansion and entry strategies adopted by multi-national and international companies bolstering occupancy rates, and iv) a more stable and favourable business environment post-COVID-19. Notably, office space uptake reduced by 10.0% to reach 0.9 mn SQFT in 2023, down from the 1.0 mn SQFT registered in 2022. This decrease is credited to lingering uncertainties in the economic environment, and cautious decision-making by businesses amidst a challenging micro-economic environment necessitating operational cost reduction. As a result, significant number of businesses and organizations have downsized their office spaces accommodating flexible work arrangements such as remote working and co-working spaces. We expect the occupancy rates to contract by 1.1%-points to 79.2% from 80.3% in 2023 mainly attributed to the persisting uncertainties in the economic landscape, continued adoption of remote work policies by companies, and an oversupply of 6.9 mn SQFT of office spaces in 2024. These factors are likely to hinder absorption rates, potentially leading to a decrease in occupancy rates	Positive	Negative

Office Market Conclusion and Outlook

We anticipate a modest increase by 0.2% to 7.9% in rental yields for the sector in the Nairobi Metropolitan Area (NMA) in 2024

Cytonn Report: Nairobi Commercial Office Outlook				
Measure	**2021 Sentiment**	**2022 Sentiment and 2023 Outlook**	**2022 Review**	**2023 Outlook**
Office Market Performance	The average rental yield improved by 0.3% points to 7.6% in FY'2022 from 7.3% recorded in FY'2021, due to improved occupancy and rental rates. Average asking rents per SQFT in the NMA increased by 2.1% to Kshs 96 per SQFT from Kshs 94, owing to an increased supply of Grade A offices fetching higher rents such as Karen Green and Global Trade Centre (GTC) Office Tower, among others. The overall occupancy rates increased by 1.8% points to 79.4% from 77.6% as a result of slow but rising demand for physical space on the back of various firms resuming full operations, coupled with the expansion strategy by various firms such as Nairobi Garage and Call Centre International (CCI) Group	The average rental yield improved by 0.1% points to 7.7% in FY'2023 from 7.6% recorded in FY'2022, due to improved occupancy and rental rates. Average asking rents per SQFT in the NMA increased by 7.1% to Kshs 103 per SQFT from Kshs 96, owing to increased availability of high-quality Grade A office spaces, exemplified by The Piano, The Cube, Karen Green, Principal Place. The overall occupancy rates increased by 0.9% points to 80.3% from 79.4% as a result of a slow but rising demand for physical space on the back of various firms resuming full operations, coupled with expansion and entry strategies adopted by multi-national and international companies We anticipate a modest increase by 0.2% to 7.9% in rental yields for the sector in 2024, driven by several factors; i) the growing popularity of serviced office spaces is expected to contribute positively to this trend, and, ii) the growing preference for landlords to collect rent in dollars. While the sector's expansion may be gradual, it is steadily progressing, supported by the ongoing recovery of the economy towards pre-COVID-19 levels. As a result, we foresee an improvement in asking rents, which will ultimately enhance average rental yields. However, the projected oversupply of office spaces, estimated at 6.9 mn SQFT in the Nairobi Metropolitan Area, is expected to exert downward pressure on the sector's overall performance by dampening demand for physical space thus affecting occupancy rates	Neutral	Neutral

- Investment opportunities remain promising in areas such as Westlands, Gigiri and Parklands, and which continue to record high returns at 8.5%, 8.2%, and, 8.0%, respectively, compared to the market average of 7.7% as of FY'2023

Cytonn