RESEARCH

Knight Frank

KAMPALA MARKET UPDATE

H1 2018

Cover Image: **Marigold Heights, Plot 92D, Old Kira Road, Kampala, Uganda**

ECONOMIC UPDATE | SECTOR BY SECTOR ANALYSIS | 2018 OUTLOOK

HIGHLIGHTS

Headline Inflation declined to 1.7% in May 2018.

Loans to private sector increased by 7.8% year on year in April 2018.

Bank of Uganda reduced the central bank rate (CBR) by 0.5% to 9.0% in February 2018.

Uganda shilling depreciated year on year by 2.8% against the USD in May 2018.

Uganda's economy projected to grow by 5.8% for FY 2017/18.

5% increase in occupancy rates in prime residential suburbs of Kampala.

Demand for Grade A commercial office space increased by 2% in H1 2018.

Shoprite opened at Acacia and Victoria Malls in April and June respectively.

Cover Image:
***Photo by** Sharon Kamayangi*

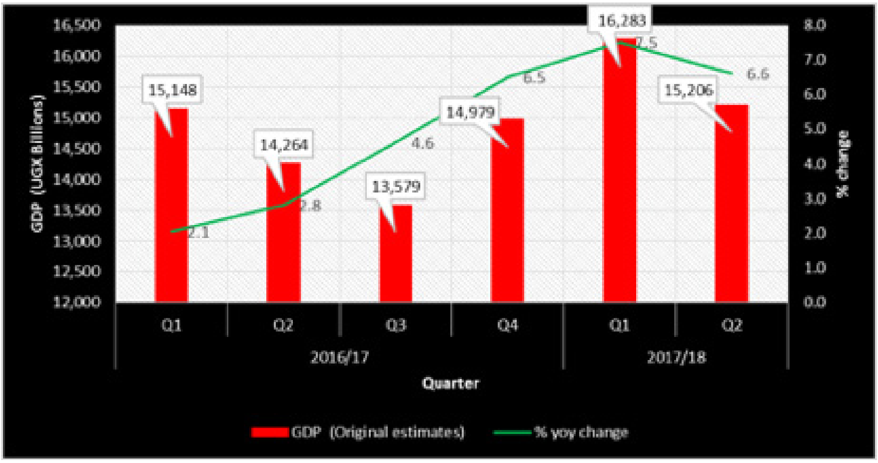
KAMPALA MARKET UPDATE **H1 2018**

GDP

According to the latest quarterly GDP report released by Uganda Bureau of Statistics (UBOS), Uganda's economy saw a strong run of growth during Q2 of financial year (FY) 2017/18 with this expansion gaining momentum to reach a 6.6% year on year growth compared to the 2.8% recorded during the same period last FY. All sectors of the economy recorded better performances in Q2 2017/18 compared to Q2 2016/17.

The improved performance was mainly attributed to a 3.5% increase in food production as a result of favourable weather patterns, a 7.3% increase in crude oil exploration activities and production of drinks and tobacco in the manufacturing sector, as well as an 8.9% growth in performance of financial and insurance activities in the services sector.
This positive start to the 2017/18 FY puts Uganda's economy firmly on track to grow by 5.8%[1] in the current financial, the best performance in six years. [Figure 1]

Figure 1:
QGDP at constant 2009/10 prices (Billion UGX)



Source: UBOS

Consumer Price Index (CPI)

According to the latest data released by Uganda Bureau of Statistics (UBOS), annual inflation declined for the eighth month in May, easing to 1.7% compared to 1.80% recorded for the year ended April 2018. Inflation remained below the central bank target of 5% since October 2017. The main reason for the reduction in headline inflation for the year ended May 2018 was the decline in the volatile food prices to -0.2% compared to 23.1% registered for the year ended May 2017. This drop was attributed to lower fruit prices that was registered at -7.4% compared to 37.2% recorded for the year ended May 2017.
Core inflation, which strips out energy and food costs registered a 0.3% rise in the month of May for an annual rise of 1.1%.

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[1] Bank of Uganda Monetary Policy Statement June 2018

MONEY MARKETS

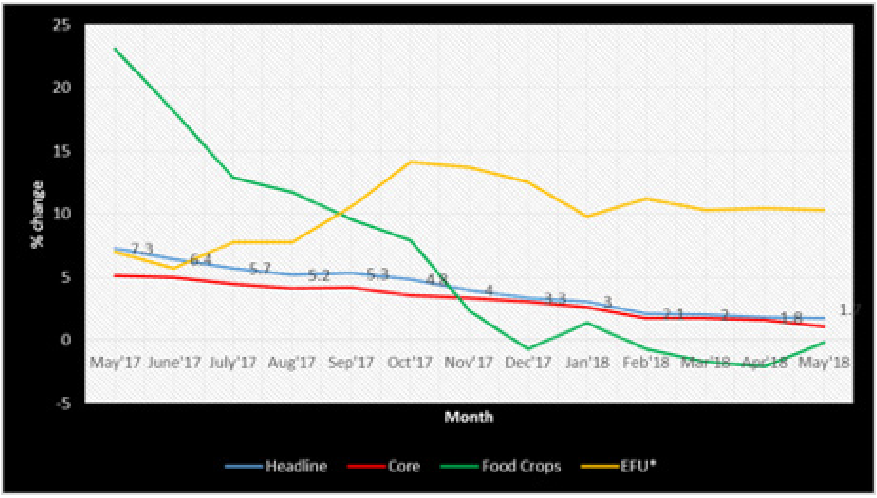
Bank of Uganda reduced the Central Bank Rate (CBR) by 0.5% to 9.0% in February 2018. According to the monetary policy statement for June 2018, Bank of Uganda maintained its benchmark CBR at 9.0%, and forecast that inflation would rise gradually over the course of FY 2018/19 due to the impact of rising import prices as well as the anticipated increase in indirect taxes. This is particularly the case with fuel prices and financial services during FY 2018/19. [Figure 2]

According to data from Bank of Uganda, the banking sector's weighted average interest rates were 20.03% and 7.76% on lending in UGX and USD respectively as of April 2018. Month on month, interest rates on treasury bills rose to 8.83% and 9.15% in May, up from 8.67% and 8.87% registered in April for the 182 and 364 day tenors respectively. [Figure 3]

CURRENCY

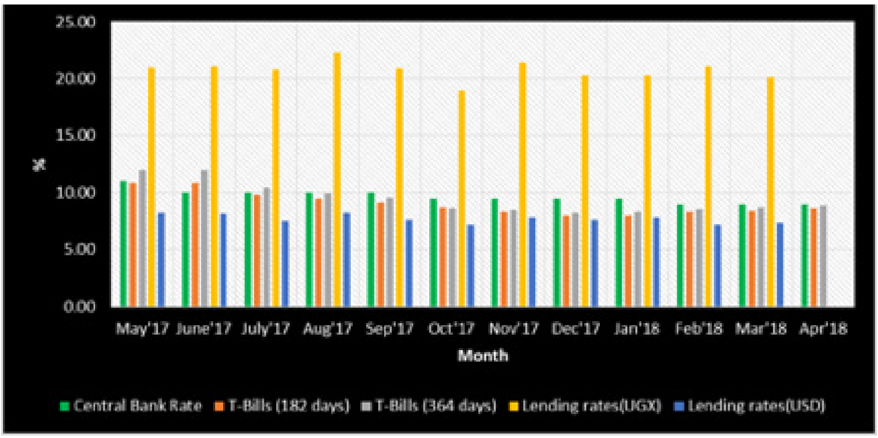
The Uganda shilling (UGX) declined by 2.4% against the United States dollar to a monthly average UGX 3,726.8 per USD, from UGX 3,640.1 per USD in May 2018. This is due to the huge dollar appetite from corporate companies especially in the energy and manufacturing sectors, the global strengthening of the US Dollar, as well as the increased demand for imports in the final quarter of FY 2017/18.
The UGX closed trading on Tuesday, June 19th, 2018 at 3,850 per USD dollar. Overall, the UGX depreciated year on year compared to the same period last year as illustrated in [Figure 4]

Figure 2:
Annual inflation rates for the 3 major components May-2017 to May-2018



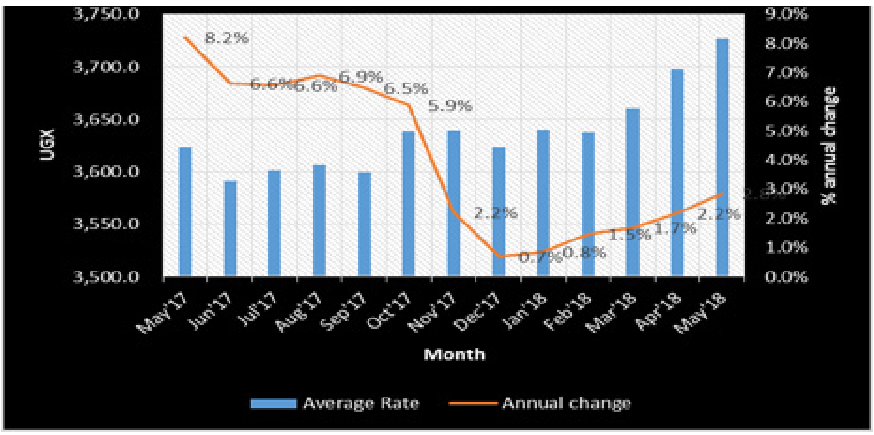
Source: UBOS *=Electricity, Fuel & Utilities

Figure 3:
Money market trends as of May 2018.



Source: Bank of Uganda

Figure 4:
Average exchange rates for the period May 2017- May 2018



Source: Bank of Uganda

PRIVATE SECTOR GROWTH

Private sector credit growth stood at 7.8% year on year in April 2018, which is higher than 6.34% registered for the same period in 2017. As a result of the rise in credit growth, the stock of private sector credit expanded to approximately UGX 12.24 trillion in April 2018 from UGX 11.44 trillion in April 2017.

Overall, monetary expansion during H1 2018 has been higher than was recorded during the same period in the preceding year, indicating an increase in economic activity as well as a benign operating environment for commercial banks. [Figure 5]

RESIDENTIAL

There has been a 5% year on year increase in occupancy rates for prime residential suburbs of Nakasero, Kololo, Naguru and Bugolobi. Knight Frank also recorded a 9% increase in demand for residential property for rent in the secondary residential suburbs of greater Kampala particularly Kira, Najjera, Kyanja, Namugongo and Naalya.

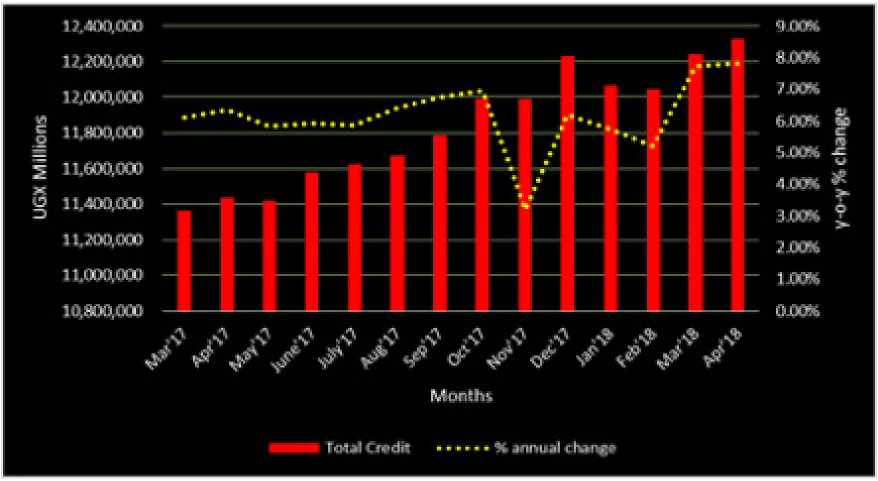
This is on the back of an increase in stock of newly constructed residential properties, (apartment blocks in particular) in the middle income segment, ranging between UGX 100m - UGX 200 million and UGX 400,000 - UGX 800,000 per month for selling and renting respectively.

It is also interesting to note that approximately 80% of the new stock of apartment blocks available on the market in Naalya, Kira, Najjera and Kyanja were sold during H1 2018. With regards to existing stock, we have registered a 10% increase in the supply of residential units during H1 2018 compared to the same period last year. This is mainly attributed to the completion of pipeline projects in H2 2017 with specific reference to the prime residential suburbs of Kololo, Nakasero, Bugolobi and Naguru.

We anticipate the supply of residential apartments in the prime residential suburbs of Nakasero, Kololo, Naguru and Bugolobi to exceed demand over the next 24 months, if the existing and newly completed developments are not absorbed by the market over the next 6 months. [Table 1, Table 2, Table 3]

Figure 5:

Credit extended to the Private Sector by Commercial Banks



Source: Bank of Uganda

Table 1:

Average residential rents and sales prices in prime residential areas

Description	Monthly Rent Unfurnished	Monthly Rent Furnished	Average Sales Prices
2 bed Apartment	$1,250 - $1,500	$1,750 - $2,000	$200,000 - $250,000
3 bed Apartment	$2,000	$2,500 - $3,500	$300,000 - $350,000
4 - 5 Bed Bungalows (0.2 - 0.5 acre plot)	$3,500 - $4,000	N/A	$600,000 - $1,200,000
4 - 5 Bed Bungalows (0.6 -1.0 acre plot)	$4,000 - $5,000	N/A	$1,200,000 - $2,000,000

Source: Knight Frank Research

Table 2:

Average residential rents and sale prices in the outskirts of Kampala Suburbs

Description	Monthly Rents Unfurnished (UGX)	Average Sales Prices (UGX)
2 - 3 bed Apartments	600,000 - 1,500,000	150Million - 300Million
2 - 3 Bed Houses (0.2-0.5 acre plot)	1Million - 3Million	350Million - 500Million

Source: Knight Frank Research

Table 3:

Average land prices per sq. m for specified suburbs

Location	US $ per sqm
Tier 1 (Kololo, Nakasero, Naguru, Bugolobi & Mbuya)	$198 - $618
Tier 2* (Ntinda, Luzira, Mutungo, Munyonyo & Muyenga)	$47- $68
Tier 3* (Namugongo, Najjera, Naalya, Kira & Kyanja)	$27- $58

Source: Knight Frank Research

*prices usually quoted in UGX and thus susceptible to foreign exchange volatility

NB: These figures vary depending on the exact location, accessibility and land tenure system.

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OFFICES

Knight Frank has registered an increase in demand for Grade A office space over the last 12 months with occupancy rates currently at 92% compared to Grade B space at 78%. This is a 2% year on year growth in Grade A occupancy compared to the 90% recorded in H1 2017. That said, there is limited vacant Grade A space in the core CBD and secondary office locations available on the market.

Knight Frank registered a 7% decline in occupancy rates for Grade B office space during H1 2018, from 85% recorded during the same period last year. This is attributed to organizations which acquired their own property and moved out of rented properties, as well as organizations which have downsized or relocated to properties with better facilities and amenities (Grade AB from Grade B buildings), as they take advantage of their current bargaining strength.

Table 4:
Prime office rents (excl. service charge)

Property type	Average Net Rents (@ sq. m)
Grade A	$15 - $16
Grade B+ (AB)	$11 - $14
Grade B	$8 - $11

Source: Knight Frank Research

This has in turn increased the available stock of Grade B space by approximately 2%. The increase in voids of older Grade B stock coupled with the relatively low demand for the same has put further down ward pressure on rental rates with Grade B gross rents (excl. taxes) now ranging between $10 and $12 per m^2 per month depending on the specific attributes of the properties.

We expect the supply gap in Grade A office space to narrow in the medium term given the number of good quality developments in the pipeline. Approximately 65,000 m^2 of Grade A space is expected on the market during the next 12 months with at least 50% of it being built for owner occupation by organizations such as law firms and government parastatals. Yields for Grade A office space were recorded at 9%-10% during H1 2018 while those for Grade B office space varied between 11%-12%.

H1 2018 also saw an increase in inquiries for prime commercial office space for purchase. However majority of the inquiries didn't materialize into actual transactions as there were only a few landlords willing to sell and buyers were unable to pay the asking prices.

In their desperate efforts to minimize void rates and attract tenants, some landlords are reducing asking rents by 20% below average passing rates. This is mainly the case for the less prime properties (Grade AB & B) which have been poorly built but in relatively good locations. This may appear to be a seemingly good and practical short term solution but is in turn distorting the market, and clawing back these rents to market rates when the sector's performance does improve, will be difficult and cause further distortions.

Whilst rent reductions as a response to increasing voids is a practical way forward, it must be done prudently. Likewise, rent reductions can only reduce on voids if the subject property is well managed and offers other comparative advantages on top of the reductions. Good quality, well managed and maintained buildings will continue to hold their value in the prime office property market.

Trust Tower - Office space with ample parking at Plot 4 Kyadondo Road
To Let: Contact Knight Frank Uganda

INDUSTRIAL

The Industrial sector accounts for approximately 23.2 % of Uganda's GDP and employs about 4.4% of the labour force. The Government of Uganda (GoU) is in the process of establishing a minimum of twenty two Industrial and Business Parks (IBP's) throughout the Country to mainly stimulate job creation, and value addition to locally available raw materials.

The biggest IBP set up by the Uganda Investment Authority (UIA) is the Kampala Industrial and Business Park (KIBP) located in Namanve 11 km East of Kampala. It is over 2000 acres and will include a number of Industrial clusters and large projects. Numerous manufacturers and investors have developed their allocated plots and relocated their facilities to the park.

UIA also developed two IBP's on the outskirts of Kampala, namely Luzira Industrial Park, which is located 5 km East of Kampala and Bweyogerere Industrial park situated 10 km North East of Kampala. The 70 acre Luzira Park is operational with functional infrastructure (road, water, power). Over fifteen investors have established or are at various stages of developing their facilities in the park.

The Industrial property sector has seen a 10% decline in demand for industrial space over H1 2018 in line with the slowdown in economic activity with some corporate organizations and private businesses downsizing, and opting to take up smaller and or cheaper warehouses. There was also a lot of speculative development of logistics and storage facilities on the back of anticipated demand from the oil and gas sector, but this has not quite materialized. It is also likely that the oil and gas sector will have specific needs and requirements which will have to be built to suit and not speculative.

The traditional industrial areas, (1st – 8th Street), Ntinda, Nakawa and Luzira Industrial areas continue to remain the preferred locations for businesses requiring only storage space as opposed to the manufacturers who have built owner occupied premises in the Namanve Industrial Park and or along Jinja Road. Likewise, a lot of the older stock in the traditional industrial areas is being extensively renovated or plots redeveloped with more modern storage and showroom space.

This trend will continue as owner occupiers relocate to designated industrial and business parks. There are some investors who were allocated plots in the KIBP but have failed to develop them to date, and initial leases and or development permits are nearly expiring. This has increased the supply of land for sale within the park, but little demand to match given the cost of reclamation required to make the land fit for development.
There are also sporadic industrial pockets developing along various axis outside Kampala like Matugga and Bombo Road, where an increase in industrial development activity has been seen. This has had a positive effect on land prices, which are now as high as UGX 70,000,000 per acre.

Table 5:
Average passing industrial rents per sq. m.

Area	Average Rents Per Sq. m per month
Traditional Industrial Area/Ntinda	\$4.00 - \$6.00
Luzira Industrial Area	\$5.00 - \$6.00
Namanve Industrial Area	\$4.00

Source: Knight Frank Research

Table 6:
Land Prices in Various Industrial Locations

No.	Location	Price Per acre
1	KIBP* (Namanve)	\$80,000 - \$200,000
2	Ntinda	\$700,000 - \$750,000
3	Bweyogerere	UGX 400 Million - UGX 600 Million
4	1st – 8th Street , Industrial Area	\$1 Million - \$1.2 Million
5	Luzira Industrial Park	UGX 600 - UGX 700 Million
6	Nakawa Industrial Area	\$600,000 - \$800,000
7	Kawempe Industrial Area	UGX 800Million - UGX 1 Billion


Modern Warehousing space in Kisubi along Entebbe Road.
To Let: Contact Knight Frank Uganda

RETAIL

The first half of 2018 has seen a resurgence of retail activity in the Greater Kampala node after the depressed trading performances of 2016 and 2017. Retailers have been reporting 11% year on year growth to date. This increase is in excess of the Consumer Price indices (CPI) which has recorded an average inflationary rate of 2.12% for the first five months of 2018 and Gross Domestic Product which is projected to increase to approximately 5.8% for the FY 2017/18. This bodes well for the retail property industry in the short to long term.

This six month period (H1 2018) has seen Shoprite supermarkets open at Acacia Mall in Kisementi and Victoria Mall in Entebbe, and also confirmed their entry into Village Mall. This is the culmination of Knight Frank's well thought out and strategic re-development plans for these Malls. Shoprite is scheduled to open at

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Bugolobi Village Mall in December 2018 in conjunction with the launching of an all new fashion wing which Knight Frank has successfully re-merchandised and re-tenanted and are currently letting.
The demand for retail space in core CBD has also increased during this period with Knight Frank registering an increase of nearly 80% on inquiries for space.

The period under review has seen a net take up of approximately 12,000m^2 of retail space in Knight Frank managed Malls, taking occupancy levels to over 95% in most Malls. Some significant Lettings in the period under review are Illusions Nightclub of the Future, Caramel Café and regional retailer Lintons opening at Acacia Mall. Victoria Mall saw the opening of discount fashion retailer PEP. Pep Stores are part of the Pepkor group which has over 4,000 stores in Africa. Middle East Shopping Complex saw the opening of Shax Unlimited convenience store in the space formerly occupied by Nakumatt.

The opening of Shoprite at Acacia and Victoria Malls has shown vindication to the strategy of anchoring the Malls with a Supermarket rather than the Hypermarket option. Supermarkets carry roughly 65% of their product range in fresh goods with the remaining 35% in the grocery and domestic essential categories. This is the opposite of traditional East African Hypermarkets, which carry very little fresh product, (less than 10% of floor area,) and have their major trade groups as groceries (non-perishable foods), electronics and appliances, clothing and textiles.

The supermarket alternative targets the daily shopper / shopping experience for the consumer versus the hypermarket experience which is more of a once a month experience. The supermarket option tends to increase daily footfall to a Mall and also benefits the other retailers who are not necessarily competing with the Anchor tenant on product and price point. This change in philosophy for Malls has proven itself as viable and optimum in more sophisticated retail markets, which has led to successful and hugely profitable malls for consumers, retailers and property developers alike.

Footfall at both Acacia and Victoria Malls averaged at 100% and 170% growth respectively for the week of Shoprite's opening over the same period under review the previous year. Acacia Mall foot traffic stabilized after the opening week to an average daily increase of 30%, Victoria Mall is yet to stabilize as the Mall was still in Shoprite's opening week at the time of printing this report. The footfall attracted to malls of this size is phenomenal and both malls showed more feet per m2 of gross leasable area than any other Mall in East Africa. Both Victoria and Acacia Mall are currently averaging in excess of 10,000 customers per day.

Retail rents have seen a slight increase in 2018, due to better trading performance in the sector and on the back of more robust demand for space.

Table 7:
Prime Retail Rental Rates in Kampala

Size	Average Rents per sq.m
10m^2	$200
50m^2	$48
100m^2	$28
500m^2	$23
500m^2	$20.00
1000m^2	$14.50

These figures are average rentals for ground floor space in Kampala Shopping Malls but do not take Shop front to depth ratio into account and exclude service charge.

VALUATIONS

This sector recorded an 18% year on year reduction in valuation instructions in H1 2018. This is mainly on account of a 33% decline in non-bank instructions. On the other hand, there has been a 9% increase in bank instructions in H1 2018 compared to the same period in 2017. The upward trend in bank instructions can partly be attributed to increased lending for mortgages, building, construction and real estate sub sectors by commercial banks as evidenced by data released by Bank of Uganda in May 2018.

Table 8:
Breakdown of Bank Instructions H1 2017 vs H1 2018

Bank Instruction Trends	H1 2017	H1 2018
Residential	65%	62%
Commercial	35%	38%

Source: Knight Frank Research

INTERESTING DEVELOPMENTS IN H1 2018

Income Tax Act 2018: Interest on a mortgage for the construction or purchase of rental properties will now be an allowable deduction for rental income earned by an individual. Given that interest on mortgages was already an allowable expense for companies, this amendment is aimed at bringing consistency within the tax law as well as incentivize individuals to promote the mortgage market.

Rental Income Tax: Uganda Revenue Authority (URA) has embarked on an aggressive drive to register legible landlords for Rental Income tax. This is tax levied on the average annual income on a rental apartment/property in the country. URA hopes to raise 117 billion shillings ($30m) from this initiative.

Landlord and tenant Bill: The bill, intended to regulate the relationship between landlords and tenants is being re-drafted given the poor drafting of the first bill. It was unnecessarily punitive towards landlords, proposing imprisonment for evicting a tenant without the approval of the minister for example. However, the Ministry of Lands, Housing and Urban development hit a snag when the bill was met with huge uproar from the public and various real estate regulatory bodies, thus requiring a redraft of the bill. The amended draft is yet to be presented before cabinet for approval.

A positive outcome of the uproar however, is that the Ministry of Lands, Housing and Urban Development stated that the recent amendment of the Income Tax Bill which required all rents to be paid in Uganda shillings, was to be reversed giving the two parties an option to mutually agree on the currency in which rent will be paid.

OUTLOOK FOR H2 2018

The government has acknowledged the need to raise the country's tax to GDP ratio, which currently stands at 13.5%. According to the recent budget 2018/19 passed by parliament on June 1, Uganda Revenue Authority (URA) is expected to collect Shs 17 trillion this financial year, an increase of 2 trillion from last financial year's collections. URA is exploring several avenues to increase tax collection and compliance. Some of these include the introduction of Excise duty on over the top (OTT) services of UShs 200 per day of access.

OTT services include the transmission or receipt of voice or messages over internet protocol network including access to VPN, but does not include educational or research sites prescribed by the Minister. In addition, Excise duty on mobile money transactions at a rate of 1% will be charged on the value of mobile money transactions on receipt, payment and withdrawal. And finally, the excise duty on mobile money transfer fees has been increased from 10% to 15%.

There has also been an increment in excise duty on fuel (diesel & petrol) of 100/- per litre. This will certainly have a negative impact on local transport and subsequently food prices. This will most likely drive up construction costs as well as headline inflation in general.

According to the Monetary Policy Statement released by the Central Bank in June 2018, Uganda's economic growth prospects remain favourable in the medium term buoyed by multiplier effects of public infrastructure investments, higher agricultural productivity, increase in household consumption and the overall strengthening of the global economy. However, the envisaged downside risks to the macro economy include exchange rate depreciation coupled with increasing oil prices.

Above all, on April 11th, 2018, Government of Uganda signed a Project Performance Agreement (PFA) with the Albertine Graben Refinery Consortium (AGRC) to develop, design, finance, construct, operate and maintain the oil refinery in Hoima district. This milestone is expected to trigger more inflow of Foreign Direct Investments (FDIs) and hopefully bring the date for Final Investment Decision (FID) and production of first oil closer.

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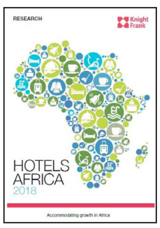

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