RESEARCH

Celebrating 20 Years since 1998 in Kenya

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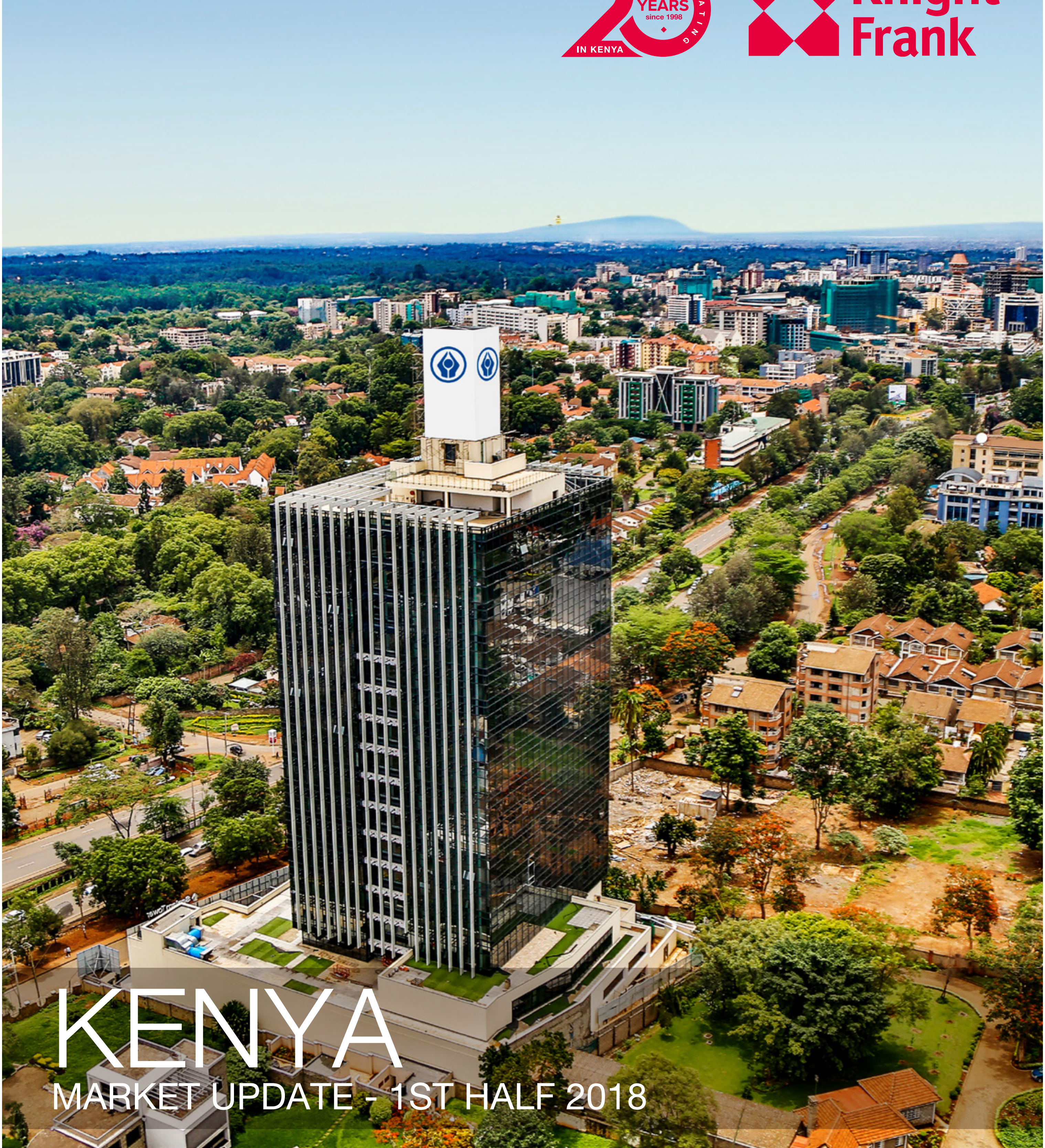


KENYA

MARKET UPDATE - 1ST HALF 2018

Sanlam Tower, Westlands, Nairobi

HIGHLIGHTS

- Kenya's economic outlook positive for 2018
- Kenya Shilling strengthens against Sterling Pound & Euro
- The Treasury recommends lifting Interest Rate Cap
- Government's Housing Agenda gains momentum
- Kenya Mortgage Refinancing Company (KMRC) incorporated
- Fahari I-REIT increases its income-generating property portfolio
- Prime commercial rents decline marginally
- Office space absorption on the increase
- Prime residential rents improve
- Local and foreign retailers take over Nairobi's retail market
- International hospitality chains increase footprint in the Kenyan market
- Kenya Airways prepares for direct flights to the US

The Economy

The Kenyan economy is expected to grow by 5.8% in 2018 compared to 4.9% in 2017, according to the World Bank. This anticipated growth is mainly attributed to the improvement of Kenya's traditionally strong sectors, including tourism and agriculture. The latter is expected to grow due to favourable weather conditions which will result in lower food prices. Other factors include the stabilising political climate, higher exports due to improved global and regional economic growth, and completion of ongoing infrastructure projects. The economy is estimated to have expanded by 5.7% in the first quarter of 2018 compared to 4.8% in a similar period in 2017.

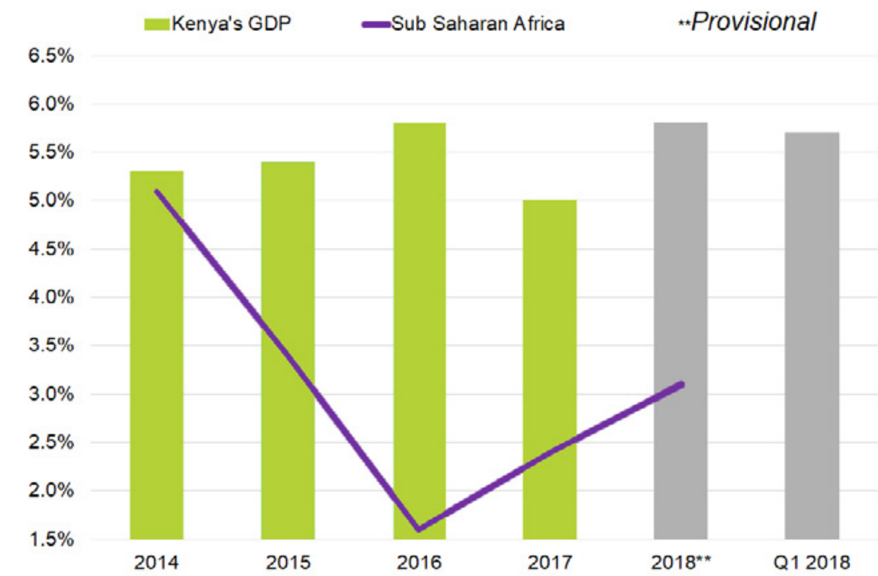
The Sub-Saharan Africa annual GDP rate is expected to rise by 3.1% in 2018 compared to 2.4% in 2017, according to the World Bank. The main factors that will contribute to this expansion include the expectation that oil and metal prices will remain stable, global trading will remain strong, and that individual governments will implement reforms to address macroeconomic imbalances whilst boosting investment. The economic expansion is also attributed to the anticipated growth in the region's three largest economies: Nigeria, Angola and South Africa, and improved agricultural sector growth in East Africa.

Production of cement decreased to 1.46 million metric tonnes (MT) in the first quarter of 2018 compared to 1.63 million MT over the same period in 2017, according to KNBS data. Similarly, consumption of cement slowed down to 1.41 million MT in the first quarter of 2018, compared to 1.53 million MT in a similar period in 2017. The value of building plans approved in Nairobi County decreased to Kshs 60.11 billion in the first quarter of 2018 compared to Kshs 61.72 billion in the first quarter of 2017. The decrease in production and consumption of cement, as well as building plans, may be an indicator that the construction sector is still recovering after the prolonged electioneering period, while the current oversupply in the market and low transactions have made developers hesitate to commence new-builds.

The Kenya Shilling strengthened against major currencies such as the Sterling Pound and Euro in the first half of 2018. Overall, it remains relatively stable against the US Dollar and Chinese Yuan.

The Monetary Policy Committee (MPC) lowered the Central Bank Rate in March from 10% to 9.5% to stimulate economic growth. Similar to the second half of 2017, month-on-month inflation decreased gradually but remained within the government's target range. However, overall year-on-year inflation ticked up for the second consecutive time in June to 4.28%. Commercial banks' interest rates remained capped at 4% above the Central Bank Rate, but the government announced through the

FIGURE 1:
GDP Rates

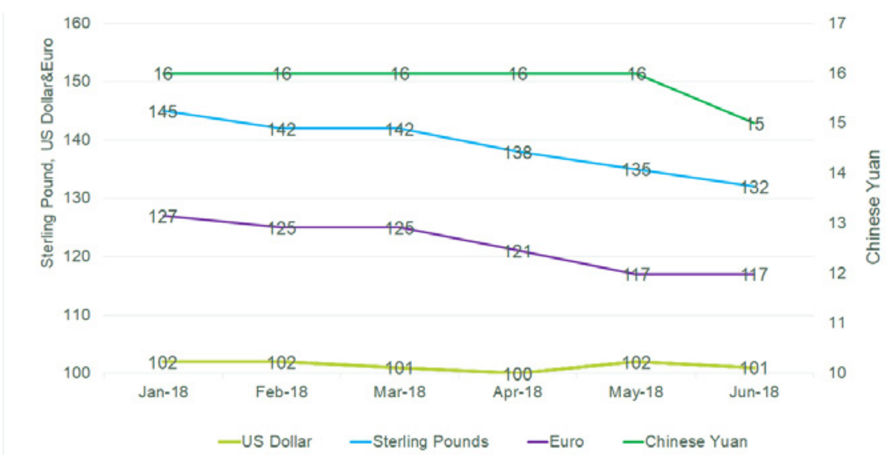


Source: KNBS & World Bank

FIGURE 2:
Value of Building Plans Vs Cement Consumption

Source: KNBS

FIGURE 3:
Foreign Currency Exchange Rates



Source: Central Bank of Kenya

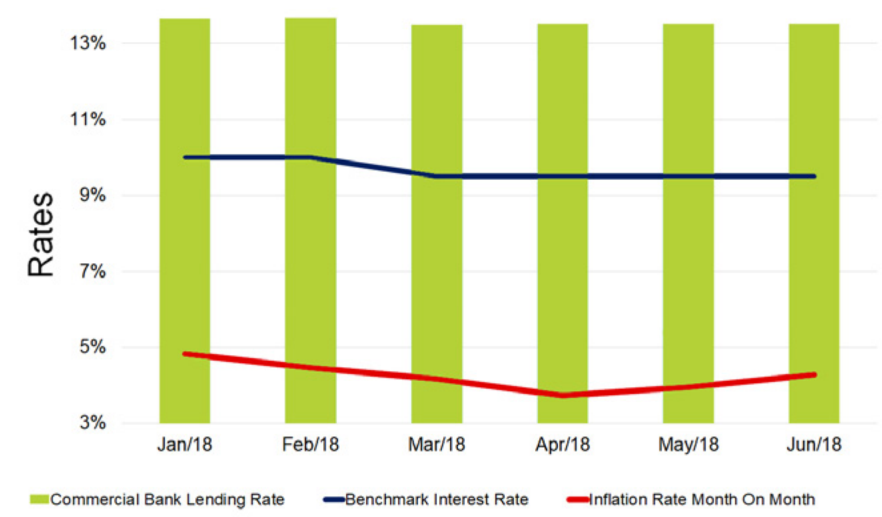
2018/19 Budget Statement a proposal to amend the Banking (Amendment) Act 2016 to allow lenders to provide more credit, particularly to borrowers considered risky. It is anticipated that lifting the interest rate cap would boost the level of liquidity in the economy and increase transactional activity.

The government recently announced the 'Big Four' Plan for development, which by 2022 is expected to:

- Boost manufacturing activity and increase the sector's GDP contribution to 15%
- Enhance food and nutrition security through large-scale production
- Achieve universal and affordable health coverage to all Kenyans
- Support the construction of at least 500,000 affordable houses

Consequently, in its budget for the financial year 2018/19, the government has allocated Kshs 24.5 billion towards affordable housing and urban development.

FIGURE 4:
Benchmark Economic Rates



Source: Central Bank of Kenya

Listed Real Estate Entities

Listed property fund Stanlib Fahari I-REIT acquired 67 Gitanga Place, a commercial office development in Lavington, at a cost of Kshs 850 million, raising its real estate assets from 67% to 90% of the portfolio. This is in compliance with the Capital Markets Authority (CMA) regulations that require the fund to allocate at least 75% of its net assets to income-generating real estate. It expects to earn Kshs 73.8 million from the recently acquired building with an annual yield of 8.59%. China Communication Construction Company Limited is currently the sole tenant in the property.

Fahari I-REIT's unit price remained stable until April when it rose to Kshs 11.95 following the announcement of a Kshs 0.75 per share distribution of profit and the planned acquisition of the additional property. However, both Stanlib Fahari I-REIT and Home Afrika closed the first half of 2018 with lower share prices than their initial listing value. Fahari's share price closed June at Kshs 11.00, which was 45% lower than the initial listing price of Kshs 20.00. Home Afrika's share price closed June at Kshs 0.90, which was 93% lower than its initial listing price of Kshs 12.00.

Infrastructure & Policy

Construction of Phase 2A of the Standard Gauge Railway (SGR) between Nairobi and Naivasha began in January in line with the China Belt and Road Initiative. The 120-kilometre (km) line is being funded by the Exim Bank of China at a cost of Kshs 150 billion, expected to be completed by the second half of 2019. Phase 2B of the project from Naivasha to Kisumu will also be financed by the Exim Bank of China to the tune of Kshs 350 billion.

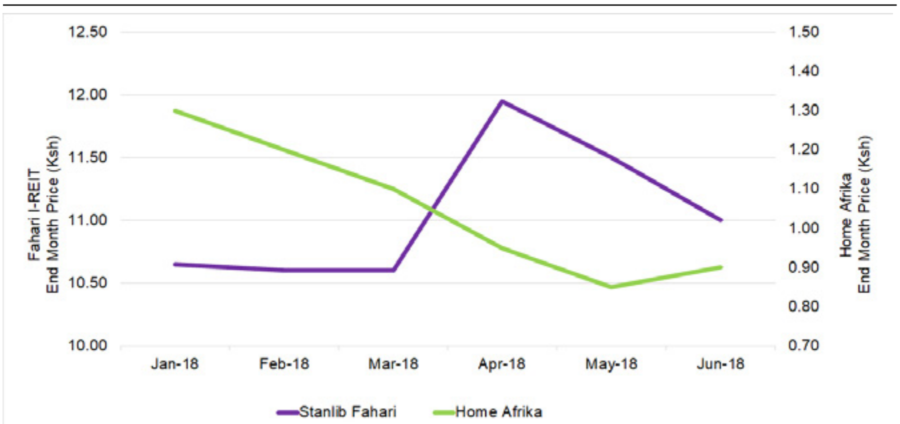
In Nairobi, Phase 1 of the Ngong Road dualling project was completed in March. Japanese firm World Kogyo Kaihatsu Company Limited was awarded Phase 2 of the Ngong Road expansion at a cost of circa Kshs 2.3 billion. The 3.4-km stretch from Prestige Plaza to Dagoretti Corner began in March and is expected to be completed by July 2019. Phase 3 of the project includes the construction of 9.8km from Dagoretti Corner to Karen at a cost of Kshs 1.98 billion which will be fully funded by the national government. This contract was awarded to Chinese firm Quinjian International Group (K) Limited, which is expected to complete the project by the second half of 2019.

At the Coast, the Kenya National Highways Authority (KeNHA) also opened Phase 1 of the Kshs 39 billion Dongo Kundu bypass in Mombasa. The road links the new container terminal to the airport.

Construction of the Malindi (Kenya)-Bagamoyo (Tanzania) highway is expected to commence during the second half of 2018. The African Development Bank (AfDB) will finance it to the tune of Kshs 30 billion, whilst the the two countries will finance the remainder in their respective zones. The 412-km Malindi-Bagamoyo Highway is set to be completed by 2021 and will cost circa Kshs 75 billion, making it one of the largest projects Kenya and Tanzania have undertaken jointly.

Construction of the first section of the Lamu Port-South-Sudan-Ethiopia-Transport Corridor (LAPPSET) infrastructure project, which was expected to commence in June, has been

FIGURE 5:
Real Estate-Related Listings



Source: Nairobi Securities Exchange

pushed back. The 600-km Lamu-Garissa-Isiolo Highway is now expected to begin in September after a funding agreement between Kenya and a South African consortium is signed.

Kenya awarded Japanese firm Toyo Construction Limited the contract to undertake the expansion of Mombasa's port second container terminal. Phase 2, which begun in May, will allow the port to handle an extra 450,000 twenty-foot equivalent units (TEUs) and increase the port's capacity to 2.1 million TEUs. Kenya signed a Kshs 35 billion deal with Japan International Cooperation Agency (JICA), which will be repaid over the next 40 years. The second container terminal is being built on 100 acres at Kilindini Harbour and expected to be ready in 2021.

The Budget Statement announced the allocation of funds towards various infrastructural projects including: Kshs 115.9 billion for on-going road construction projects, Kshs 74.7 billion for the construction of Phase 2A of the SGR, Kshs 2.7 billion for the Mombasa Port Development Project, and Kshs 1.4 billion for the expansion of various airstrips.

Retail

Local and international supermarket chains continue to take up retail space created by Nakumatt's and Uchumi's exits.

In January, Naivas took over retail space at Development House on Moi Avenue previously occupied by Nakumatt, as well as at Capital Centre in April, which was previously occupied by Uchumi. This increased the retailer's total outlets across the country to 45. French retail chain Carrefour opened at Sarit Centre in April, taking over space vacated by Uchumi. Carrefour will operate in the space temporarily and shift operations to the new wing of Sarit Centre upon completion by the end of the year. It will also open its sixth store at Galleria Shopping Mall in July, taking over space previously occupied by Nakumatt.

Botswana-based retailer Choppies is also currently in talks with the owners of Nanyuki Mall to take over the anchor tenant space vacated by Nakumatt in January. South Africa-based retailer Shoprite took up anchor tenant space left by Nakumatt at Westgate and Garden City Mall. Both branches are expected to open within the second half of the year. Game announced it will open the second outlet at The Waterfront Karen, replacing Nakumatt which was initially set to be the mall's anchor tenant.

Occupancy levels remained high for established malls at 90% and between 60-75% for new retail centres. The high occupancy levels indicate that there is still good demand for retail space in the right locations. Footfall in major shopping malls increased slightly in the first half of 2018, as expanding retailers took up anchor tenant spaces vacated by ailing rivals.

Prime retail rents remain unchanged in the first half of 2018 at US$55/sqm/month while the service charge across retail malls in Kenya ranged from Kshs 480 to Kshs 615 per square metre per month. The stagnation is attributed to continued oversupply in certain locations, slow recovery from the 2017 political situation and the economic downturn. Increased supply continued to exert a downward pressure on escalations that stood at circa 7.5% per annum for Kenya Shilling leases.

The second half of 2018 projects a positive outlook mainly due to improvement in the economy, which is anticipated to boost the consumer spending power.

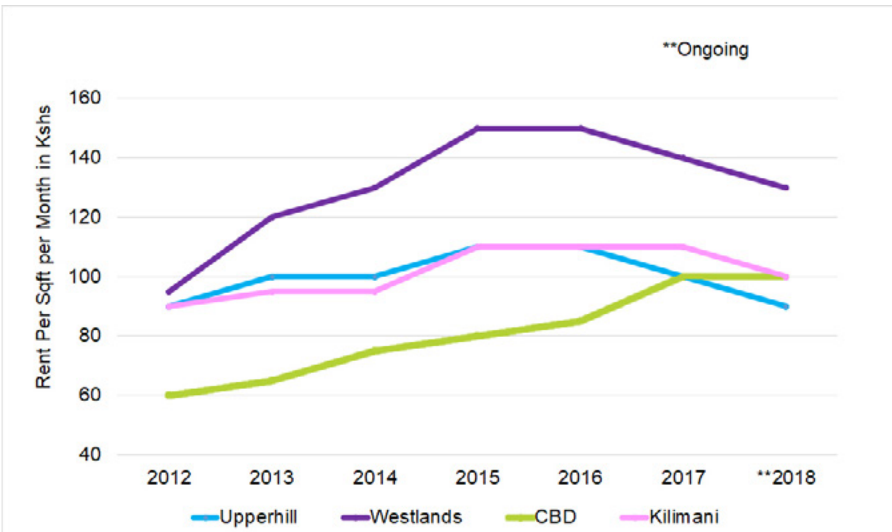
Several major international brands expanded with new shops across the country in the first half of the year. LC Waikiki opened its doors at City Mall Nyali, while Japanese lifestyle brand Miniso opened three new stores at The Junction, Southfield Mall and Thika Road Mall, with an additional store set to open at The Hub Karen during the second half of 2018. Choppies supermarket opened at Southfield Mall in Embakasi while Tuskys Supermarket took up 35,000 square feet at Diamond Plaza II. French sports retailer Decathlon is expected to enter the Kenyan market by opening it's first branch at The Hub Karen during the second half of 2018.

TABLE 1:
Retail Developments in the pipeline

RETAIL DEVELOPMENT	LOCATION	SIZE (SQM)
Westgate Mall Phase II	Westlands, Nairobi	14,000
Diamond Plaza II	Parklands, Nairobi	8,361
The Waterfront Mall	Karen, Nairobi	19,509
The Well	Karen, Nairobi	7,432
Sarit Centre Phase 3	Westlands, Nairobi	30,000
Rupa Mall	Eldoret	13,935
ENA Hub	Nakuru	10,766
Kiambu Mall	Kiambu	14,000
Signature Mall	Mlolongo	20,570
Airport Centre Mall	Changamwe, Mombasa	16,000

Source: Knight Frank Kenya

FIGURE 6:
Average Prime Office Rental Rate per Month



Source: Knight Frank Kenya

Retail developments in the pipeline for the second half of 2018 are illustrated on table 1.

By the end of 2018, the retail market will have increased retail space supply by circa 340,000sqm.

Office

Absorption of Grade A and B office space increased by 12% in the first half of 2018 compared to the uptake in the second half of 2017.

Prime asking rents reduced marginally in the period to US$1.3/sqft/month. The second half of 2018 is expected to record an increase in prime asking rents mainly due to economic recovery and the take up of existing space specifically in prime buildings in the right locations.

Fewer completions were recorded in the first half of 2018 in comparison to the second half of 2017, as developers pushed back dates due to delays occasioned by the political climate last year. Completions in the review period in the country's capital included Sanlam Towers (14,864sqm) and Galleria Office Park (7,432sqm). Major developments in the pipeline are illustated on Table 2.

Residential

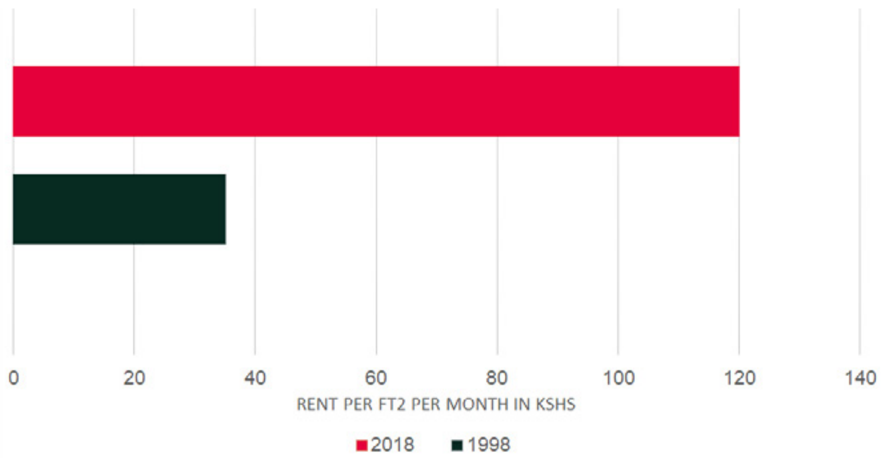
Prime residential prices improved by 0.4% in the first half of 2018 compared to a 1.8% decline in the second half of 2017. Prime residential rents also improved marginally in the period by 0.33%, having remained unchanged in the second half of 2017. The increase in prime residential prices and rents is attributed to an improved political climate and the thawing of the wait-and-see attitude among buyers and occupiers. This trend is expected to continue into the second half, with transactions only occurring where landlords and sellers are willing to negotiate with potential tenants and buyers, particularly in areas currently experiencing oversupply such as Karen.

The upcoming mixed-use development Tatu City in Kiambu County is constructing a prime residential estate as part of its Kijani Ridge development. The proposed 'low density' estate aimed at the prime end of the market is meant to rival Nairobi's upmarket residential neighbourhoods such as Muthaiga and Karen, with houses sitting on more than an acre each.

Developer Lordship Africa in February completed a sales office and show house to facilitate the sale of its proposed 44-storey residential tower in Upperhill named 88 Nairobi. The 288 furnished apartments will sit on two acres and cost an estimated Kshs 5 billion to develop. Upon completion by 2020, the development is touted to be the tallest residential structure in Sub-Saharan Africa and one of the first of its kind in Nairobi's residential market besides The Pinnacle.

Kenya currently has an accumulated housing deficit of more than two million units, according to official statistics. The government aims to achieve affordable housing over the next five years as part of President Uhuru Kenyatta's 'Big Four' agenda. It is proposed that the state will partner with 35 private firms to construct a million housing units by 2023 at a cost of Kshs 2.6 trillion (US$ 2 billion). A pilot scheme was launched in Mavoko, Machakos County, in February, while the other projects will be across various locations such as Kitengela and Athi River. A low-cost housing project to build 30,000 houses is also planned for Eastlands, Nairobi County, starting with 2,000 units in July. Development of a further 5,000 units

FIGURE 7:
Westlands Commercial Prices 1998-2018 (per square foot per month in Kshs)



Source: Knight Frank Kenya

TABLE 2:
Commercial Developments in the Pipeline

COMMERCIAL DEVELOPMENT	LOCATION	APPROX. SIZE (SQM)
One Africa Place	Westlands, Nairobi	12,821
The Promenade	Westlands, Nairobi	20,067
Merchant Square	Riverside, Nairobi	15,329
1 Park Avenue	Parklands, Nairobi	12,356
Laxcon Plaza	Parklands, Nairobi	9,290
Church Commissioners for Kenya (CCK)	Kilimani, Nairobi	11,128
Capital Square	Parklands, Nairobi	8,361
Victoria Towers in Two Rivers	Nairobi	7,897
Le' Mac	Westlands, Nairobi	9,290
AVIC Towers	Westlands, Nairobi	63,000
Sandalwood	Riverside, Nairobi	23,226
Pinnacle	Upperhill, Nairobi	6,503
The Address	Westlands, Nairobi	22,575
19 Kabasarian Avenue	Lavington, Nairobi	7,120

Source: Knight Frank Kenya

in Shauri Moyo, 20,000 units in Makongeni and 3,000 units in Starehe is due to begin in October.

Additionally, the state has offered incentives to facilitate the private sector in low income housing, including reducing the corporation tax and scrapping levies charged by the National Construction Authority (NCA) and the National Environment Management Authority (NEMA); and redeveloping high-rise buildings in areas with large populations such as Eastlands.

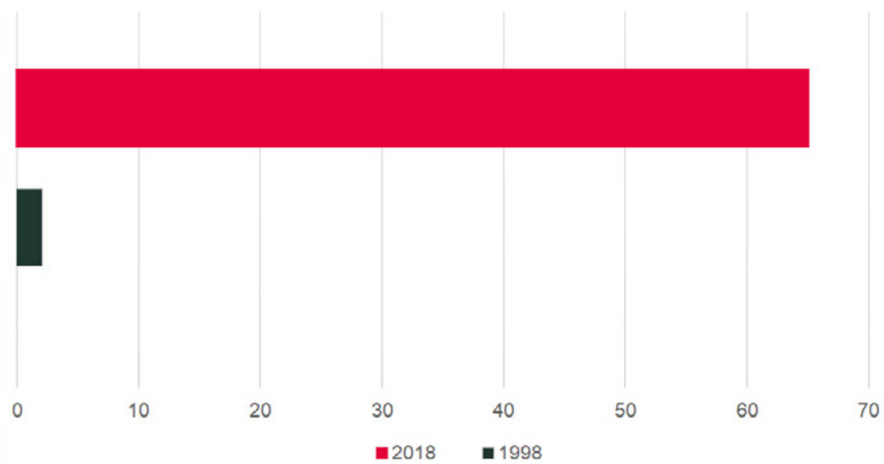
In line with the State's plan to provide affordable housing, the government has proposed to set up the National Housing Development Fund (NHDF) under the proposed Housing Bill.

In April, the government incorporated a mortgage liquidity facility named the Kenya Mortgage Refinancing Company (KMRC), which is set to be launched in February 2019. It will provide secure long-term funding to mortgage lenders, which is expected to subsequently boost the availability and affordability of mortgage loans to Kenyans. This will be achieved by financing commercial banks and Saccos to enable them offer affordable home loans to low-income earners. KMRC will have an initial capital of Kshs 1.5 billion, 20% of it from the government and 80% generated from local lenders. Additional funding is also being considered from international financiers such as the World Bank. KMRC is expected to facilitate commercial banks and Saccos to issue 50,000 additional mortgages by 2023. The affordable housing initiative is expected to result in a 'housing multiplier effect' and benefit the entire economy.

FIGURE 8:
Prime Residential Rent and Sale Prices

Source: Knight Frank Kenya

FIGURE 9:
Karen Residential Prices 1998-2018 (Kshs M/Acre)



Source: Knight Frank Kenya

Chinese property developer Erdemann Property has announced plans to construct 8 blocks of a 34 storey apartment development in Ngara, Nairobi which will sit on 2.3 acres. The firm has sought permission from the National Environment Management Authority (NEMA) to upgrade Jadongo Road, which will improve accessibility of the property and have a positive impact on the area.

Hotel & Tourism

The first half of 2018 saw a number of international hospitality chains open facilities in the country. These included City Lodge, owned by City Lodge Group, at Two Rivers Development; Mövenpick Hotel & Residences by Mövenpick Hotels & Resorts in Westlands; and Hilton Worldwide's Hilton Garden Inn near the Jomo Kenyatta International Airport (JKIA). Greenhills Investment Limited, the owner of Village Market and the Tribe Hotel in Gigiri, also opened a 215-room hotel named Trademark Hotel in the new Village Market extension. This will be a more affordable facility in comparison to the Tribe, its sister hotel.

In the review period, global hospitality chains also strategically increased their footprint in the Kenyan market by taking over hotels that were already operational. Hilton Worldwide, for instance, took over Nairobi's Amber Hotel under a franchising agreement and renamed it Double Tree by Hilton, which opened in February. In addition, global hotel chain Best Western International has allowed the Meridian Hotel in the CBD to operate under its brand name as well. The hotel is currently operating as Best Western Plus Meridian. Rwanda-based CityBlue Hotels took over the Creekside Hotel Mombasa, previously operated by Best Western International. The hotel was rebranded from Best Western Plus Creekside Hotel to CityBlue Creekside Hotel & Suites, Mombasa. Intercontinental Hotels Group (IHG) took over the management of Sarovar's Lazizi Premiere Hotel, a JKIA-based hotel which opened in 2017, and rebranded it to Crowne Plaza Nairobi Airport Hotel in May. This increased the number of hotels under the Crowne Plaza brand in Kenya to two.

Major hotel developments in the pipeline include The Alba Hotel in Lavington and Azure Best Western at Signature Mall, both part of the Best Western's Collection; Radisson Arboretum by Carlson Rezidor; and the JW Marriott hotel at the Avic International complex in Westlands that is set for completion in 2020.

Overall the tourism industry experienced an increase in bed occupancy mainly due to improved security and effective promotion strategies both locally and internationally. According to the KNBS, hotel bed-nights occupancy increased by 11.3% to 71,742,000 in 2017 from 64,485,000 in 2016. International visitor arrivals have recovered following the lifting of travel advisories against by major source markets. Tourist arrivals rose to 1,448,800 in 2017.

In June, national carrier Kenya Airways (KQ) begun direct flights to Cape Town and Mauritius, where it already had pre-existing code sharing agreements with Air Mauritius. KQ is also set to commence daily direct flights between Nairobi and New York in October, which is expected to further boost trade with the United States of America (USA), particularly since it's one of Kenya's top source markets for visitors. The economy is expected to benefit from jobs created directly at Kenya Airways and indirectly through the airline's suppliers. Two approvals by the US Transportation Security Administration (TSA) and Federal Aviation Authority (FAA) are currently pending before the direct flights can commence. The TSA is supposed to certify JKIA as the last point of departure, while the FAA will grant KQ an Air Operator Certificate after inspecting the carrier's equipment and facilities. Kenya Airways is optimistic that the approvals will be granted before October.

Jambo Jet, a Kenya Airways subsidiary, started daily flights to Uganda in February. The budget airline has also applied for rights to fly to other regional routes within East Africa including Rwanda, Ethiopia, Sudan, Congo, Tanzania and Burundi. To carry on with the expansion plan, the airline intends to add four aircraft by the first half of 2019 to increase its fleet size to eight.

Industrial Market

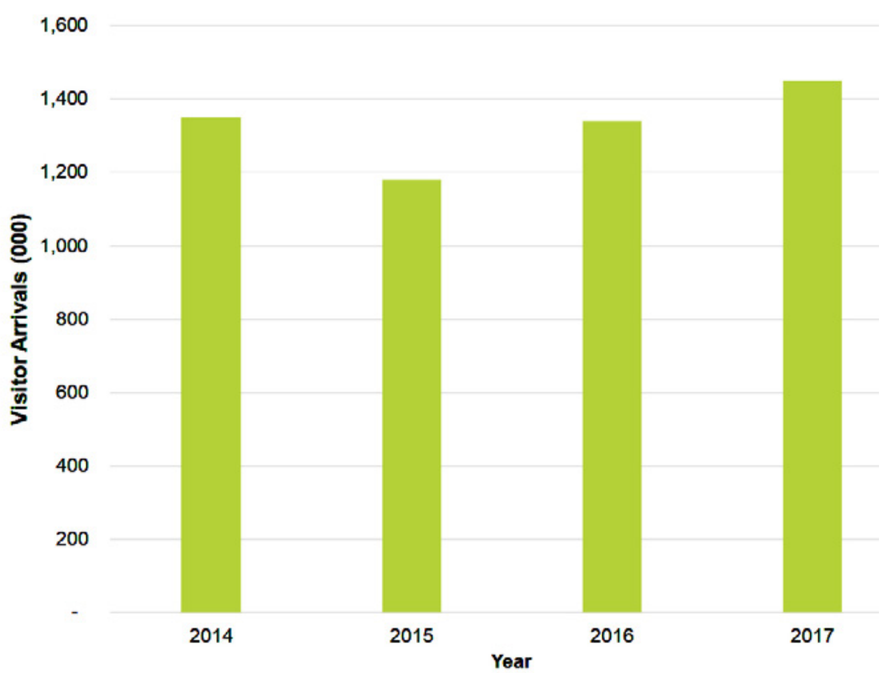
The government announced it has set aside Kshs 73 billion towards the ongoing development of the Konza Technopolis. Firms are already taking up space in the 5,000-acre city, including Korean University, Kenya Electricity Transmission Company, National Construction Authority and Craft Silicon. The first phase of Konza City is projected to be complete by 2020.

Africa Logistics Properties (ALP) in February signed a long term lease with Copia, an e-commerce retailer for 4,500sqm of warehousing space at ALP North. It has currently pre-let 63% of its 50,000-sqm logistics and distribution complex. Phase 1 of ALP North is expected to be ready for occupation in September. Construction of ALP's second project, ALP West, is currently underway. The 100,000-sqm facility will sit on 49 acres and is located on the A104 Nairobi-Nakuru highway. Phase 1 is set to be completed by mid-2019.

Institutional Market

Educational investors continued to demonstrate interest in the Kenyan market in 2018, with Africa's largest private education provider and Johannesburg Stock Exchange-listed AdvTECH having recently acquired the Makini Group of Schools. It is also set to open a school in Kiambu's Tatu City in September. The institution will have a capacity of 1,700 students. Meanwhile, Acorn Holdings Africa opened its second students' residence under its Qwetu brand in Ruaraka, Nairobi, having opened the first facility on Jogoo Road in 2017. Both residences cost the firm an estimated Kshs 800 million and have a combined capacity of 734 rooms.

FIGURE 10:
International Visitor Arrivals



Source: KNBS

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