RESEARCH

Knight Frank

KAMPALA MARKET UPDATE

H2 2018

Cover Image: Trust Tower, Plot 5, Kyadondo Road, Nakasero

ECONOMIC UPDATE | SECTOR BY SECTOR ANALYSIS | 2019 OUTLOOK

HIGHLIGHTS

Inflation reduced to 2.2% in December 2018

The Uganda Shilling appreciated by 0.7% against the USD in December 2018

Increased demand for treasury bills

Economy grew by 6.8% in Q1 of FY 2018/19

Bank lending instructions to the residential sector reduced

Residential occupancy rates in prime areas declined by 5%

Office leasing activity increased by 18% in H2 2018

Victoria Mall in Entebbe registered the highest footfall per m² in East Africa at 41 people/sqm/month.

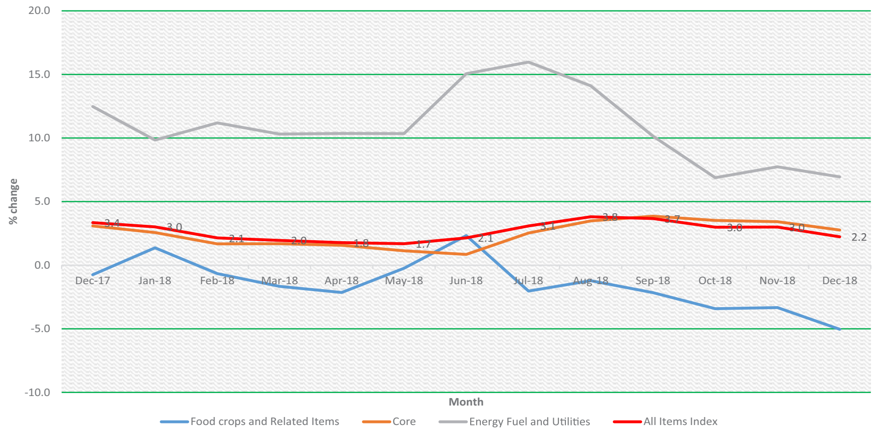
KAMPALA MARKET UPDATE **H2 2018**

Inflation

Annual headline inflation for the year ended December 2018 declined to 2.2% from 3.0 % recorded for the year ended November 2018. This is the lowest inflation rate recorded for the past 6 months since May 2018. The decline in annual headline inflation was driven by food inflation which declined to -5.0% compared to -3.3 % recorded for the year ended November 2018. The reduction in food prices was predominantly due to a decline in fruits inflation registered at -13.2% for the year ending December 2018 compared to -9.3% recorded for the year ended November 2018.

Annual Core Inflation which excludes temporary price volatility, declined to 2.8% for the year ending December 2018 compared to 3.4% registered for the year ended November 2018. [Figure 1]

Figure 1:
Annual Inflation rates for the period Dec - 17 to Dec - 18

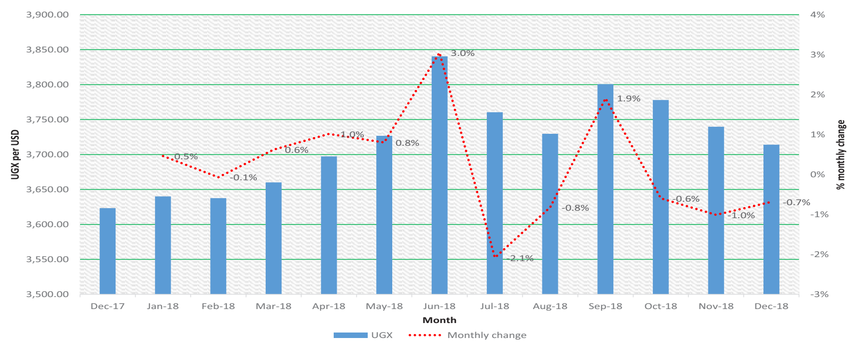


Source: UBOS

Exchange Rates

The Uganda Shilling (UGX) appreciated against the United States Dollar (USD) by 0.7% in December 2018. The UGX opened the second half of 2018 trading at an average rate of 3,760.44:$1 in July 2018 and closed at an average rate of 3,714.13:$1 in December 2018. This translates to a 1.2% appreciation during H2 2018 compared to 0.6% depreciation registered during the same period last year (H2 2017). Uganda's Ministry of Finance attributed the appreciation of the Shilling to higher supply of the US Dollar due to inflows to NGO's, coffee export receipts and offshore players in the Government securities market. [Figure 2]

Figure 2:
Average exchange rates for the period Dec - 17 to Dec - 18



Source: BoU

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Money Markets

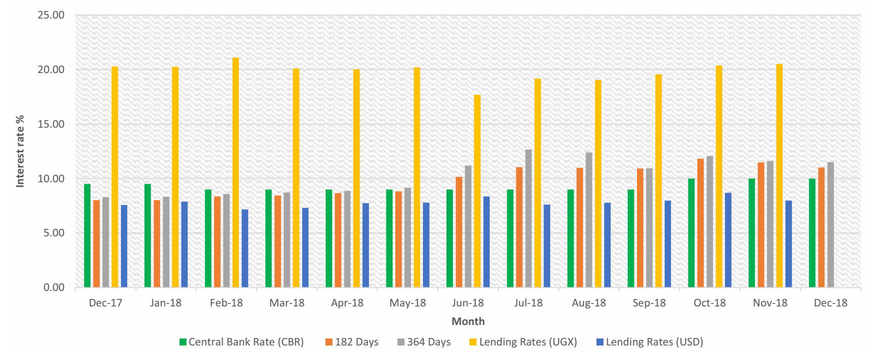
During H2 2018, Bank of Uganda increased the Central Bank Rate (CBR) by 1% to 10% in October 2018, a rate that was maintained up to December 2018. This is higher compared to 9.5% recorded during the same period last year, indicating a year on year higher cost of capital for the last quarter of 2018 vis a vis Q4 2017.

Commercial Bank prime lending rates for the Uganda shillings rose to a weighted average of 20.51% in November from 20.37% in October, whereas USD denominated lending rates declined to a weighted average of 7.99% in November from 8.70% in October 2018. The upward trend in Uganda shilling lending rates followed a 1% increment in the Central Bank Rate recorded from Q3 to Q4 of 2018. The average weighted yields on treasury bills for 182-day and 364-day tenors for December 2018 were recorded at 11.02% and 11.51%, down from 11.47% and 11.61% registered in November 2018 respectively. The decline in yields was largely driven by an increase in demand for treasury bills. [Figure 3]

Gross Domestic Product (GDP)

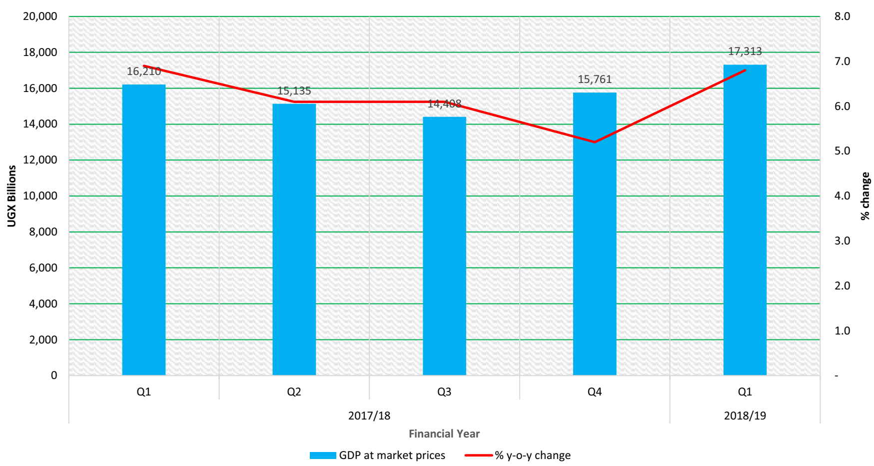
GDP estimates for the first quarter of FY 2018/19 indicate that the economy grew by 6.8% compared to 6.9% registered during the same period of FY 2017/18. The biggest driver of this growth was from the services sector that registered a year on year value added growth of 8.2% in Q1 of 2018/19, compared to an earlier growth of 8.0 % in Q1 the previous year. This growth was driven by Trade & Repair, Public Administration, Education and Health activities. [Figure 4]

Figure 3:
Average exchange rates for the period Dec - 17 to Dec - 18



Source: BoU

Figure 4:
Quartery GDP at market price (Billion Ugx)



Source: UBOS

RESIDENTIAL SECTOR

Knight Frank Uganda registered a 5% year on year decline from 86% to 81% in occupancy rates for the prime residential suburbs of Kololo, Nakasero, and Naguru. Key among the drivers for this decline, is the fact that tenants opted for accommodation in other suburbs where rents are slightly lower, and yet the quality of stock available is newer and of similar if not better quality than is available in the prime suburbs.

H2 2018 also registered an increase in new stock of prime residential accommodation, 85% of which were apartment blocks. This is exerting downward pressure of approximately 10% - 15% on rentals across the board in response. For example, average rents for prime two bedroom furnished apartments reduced from $2,250 to $1,850 and unfurnished from $1,500 to $1,000. It is expected that approx. 150 housing units will come onto the market over the next 12 months in Kampala's prime residential suburbs, of which 90% are 3 bed apartment units.

Despite a 12% increase in the supply of residential housing stock, the greater Kampala suburbs of Naalya, Kira, Najjera, Namugongo, Buwaate and Kitende that are dominated by mid-income residential properties registered a 2% year-on-year increase in occupancy rates from 80% recorded in H2 2017 to 82% in H2 2018. This is in correction with justifying the steady demand and requirement for affordable housing given that demand has been outstripping supply for the past 5 years.
[Table 1], [Table 2], [Table 3]

Table 1:
Average rents and sales in USD as of H2 2018 in prime residential areas of Kampala

	2 bed Apartment*		3 bed Apartment*		4 – 5 bed Bungalows (0.25-0.5 acres)	
	Rent	Sale	Rent	Sale	Rent	Sale
Tier 1 (Kololo, Nakasero, Naguru, Bugolobi & Mbuya)	$1,850	$225,000	$2,750	$325,000	$3,500	$ 1million
Tier 2 (Ntinda, Luzira, Mutungo, Munyonyo & Muyenga)	$1,200	$120,000	$1,850	$180,000	$2,500	$250,000

*=furnished
Source: Knight Frank Research

Table 2:
Average rents and sales figures of Mid Income Housing in Kampala during H2 2018.

	2 bed Apartment		3 bed Apartment		4 – 5 bed Bungalows (0.10-0.25 acres)	
	Rent (Ugx)	Sale (Ugx)	Rent (Ugx)	Sale (Ugx)	Rent (Ugx)	Sale (Ugx)
Naalya, Najjera, Namugongo, Kitende, Kira, Buwaate etc)	700,000	120 million	1 million	160 million	1.2 million	250 million

Source: Knight Frank Research

Table 3:
Average land prices per sqm for specified residential suburbs (H2 2018)

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

*prices usually quoted in UGX and thus susceptible to foreign exchange volatility
Source: Knight Frank Research
NB: These figures vary depending on the exact location, accessibility and land tenure system

Table 4:
Average prime office rents excl. S/C and VAT

Grade	Price per sqm/month
Grade A	$14-$ 16
Grade AB	$8-$13

Source: Knight Frank Research

COMMERCIAL AGENCY AND OCCUPIER SERVICES (OSCA)

Approximately 13,000 m^2 of Grade A / AB office space in the core central business district (CBD) (between Kampala Road and Yusuf Lule Road) and prime periphery areas (parts of Kololo, Bugolobi, Nakawa, Bukoto) was leased during H2 2018 compared to 11,000 m^2 in H2 2017. This represents an 18% year on year growth in take up rates. There was a 2% annual increase in occupancy for Grade A and AB office space in Kampala to 86% in H2 2018, from 84% registered in H2 2017.

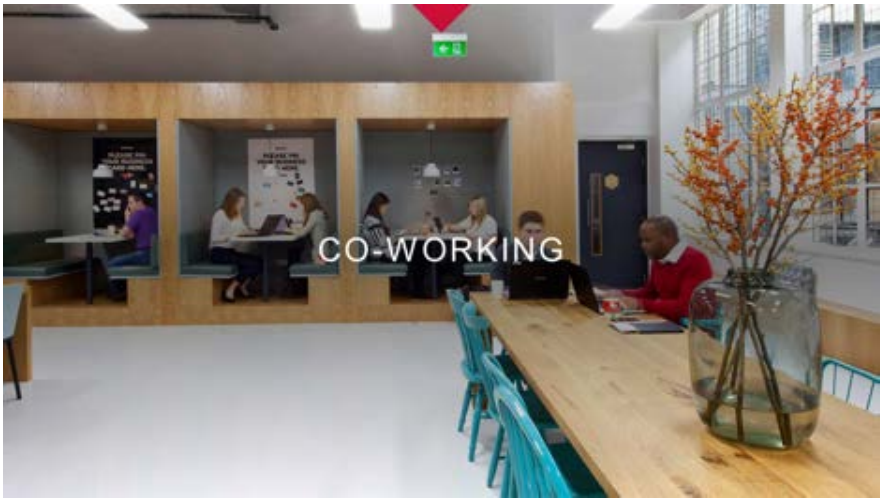
We also noticed increased flexibility from landlords with regards to lease terms at renewal and new leases, in a quest to retain tenants, given the increasing supply of office space coming onto the market amidst increasing economic uncertainty and shrinking profit margins across the board for most businesses. It remains to be said however, that good quality, well located and managed office buildings continue to hold their value, and rent reductions tend to be less significant than the lower quality, older stock of properties. The current trend of corporate tenants and government parastatals moving into their own built to suit buildings will have an adverse effect on office space, by increasing the supply of vacant stock on the market in the short to mid – term. Prime office yields remained stagnant but attractive at 10% and 11% for Grade A and Grade AB buildings respectively. [Table 4]

With regards to Occupier Services, it is becoming increasingly evident that the Kampala office market will continue to be driven and defined by goals and objectives which tenants are intent on achieving. The most important being cost reduction and strategic alignment between real estate and wider business aims. Flexibility, productivity and increased efficiency from both the occupiers and the use of space are top of the list for most corporate office occupiers. Changing tenant expectations (particularly with start - ups and the younger more mobile freelance entrepreneurs) with regards to their space requirements are leaning towards, co-working space through shared offices.

Co-working is a business services provision model that involves individuals working independently or collaboratively in shared office space. Shared offices are becoming more attractive options for occupiers because they allow flexibility to grow or downsize, eliminates many of the real estate responsibilities for the tenants therefore freeing time for them to concentrate on their core business, and reduces the capital tied up in IT, property and business administration.

Across the region in general and Kampala specifically, occupiers are becoming increasingly mindful of occupancy cost escalations which remains a critical concern for most tenants. The increasing risk of economic uncertainty, reduced market share and revenues and general slowdown in trade and commerce for most businesses, have driven corporate tenants to look at ways of optimizing their spatial requirements and efficiencies as a solution to reducing their occupancy costs.

Given our track record as the region's leading property firm, Knight Frank has the expertise and proven ability to be a trusted advisor to property investors and occupiers which will enable both parties achieve their objectives through bespoke strategies and solutions to the demands of the ever evolving office market. Our strong networks and longevity in this market enables us to quickly identify and understand the occupier's requirements, which we are able to address given the size and scale of our commercial property portfolio of assets under management. Our global footprint also means that we are able to enhance the symbiotic relationships between global property investors and occupiers by creating the perfect opportunities for the development of intelligent and flexible buildings to match the specific demands of the modern office occupier.



Source: Knight Frank Research

RETAIL SECTOR

The second half of 2018 has seen a consolidation of retail in the Greater Kampala node after the erratic trading performances of the previous two and a half years. Retailers have reported significant growth over the period and the majority of Malls under Knight Frank management have bedded down exceptionally well since the launch and opening of new anchors in them.

Acacia Mall showed footfall growth averaging 15% for the period under review. Victoria Mall in Entebbe currently has the highest footfall per square meter of gross leasable area of any mall in East Africa, at 41 people/sqm/month, subsequent to the new anchor opening in June 2018. It is followed closely by Acacia Mall at 17 people/sqm/month.

Victoria Mall has shown footfall growth in excess of 109% per month establishing itself as the "go to" venue for both consumers and retailers in the south eastern location of the Greater Kampala node. The performance of these Malls subsequent to the replacement of the anchor tenant by Knight Frank, bodes well for firstly, Village Mall which will see Shoprite open their 5th store in the country, in the first quarter of 2019.

Shoprite Lugogo Mall which is also managed by Knight Frank, saw the start of an upgrade to entrances, exits and parking in this half year period. The redevelopment of these areas was undertaken to ease traffic congestion on both Lugogo Bypass and Shoprite/ Jinja Roads. Phase one of the refurbishment was completed in time for the traditional Black Friday sale that was held at the end of November and for the opening of the 8th Café Javas store in Uganda.

Café Javas is a phenomenally successful Ugandan homegrown brand of world class standard, which has now expanded into the Kenyan market by opening two stores in Nairobi. The opening of Café Javas at Lugogo Mall was well received by the primary catchment market of this neighborhood and has added to the leisure and dining options available at the development.

Black Friday sales in November were hosted in 4 of the Knight Frank managed malls, and this saw record turnovers for retailers that got involved in the promotion resulting in Malls registering record footfall days on the 23rd November, 2018. The concept of Black Friday has been positively embraced by consumers, and the excitement and plentiful bargains attained by all has ensured that this concept will grow from strength to strength and will be hosted in all Knight Frank Malls in 2019.

The latter half of 2018 saw the demise of Deacons Group in Uganda.
The Kenyan based master franchisee of numerous international fashion brands experienced trading setbacks

Table 5:

Prime Retail Rental Rates in Kampala

Size	Rates
<10m²	$200
<50m²	$48
<100m²	$28
<500m²	$23
>500m²	$20.00
>1000m²	$14.50

Source: Knight Frank Research

Table 6:

Average passing industrial rents per sqm

Area	Average Rents Per Sq. m per month
Traditional Industrial Area/Ntinda	$5.50 - $7.00
Luzira Industrial Area	$5.00 - $6.00
Namanve Industrial Area	$3.50 - $4.00

Source: Knight Frank Research

and challenges in its home market, and this spilled over into Uganda, seriously impacting on their ability to trade due to poor and insufficient stockholding.

Century Fashions, MRP's Tanzanian based franchisee was awarded the franchise for Uganda and the stores re-opened and re-stocked in late July with new clothing ranges. MRP will be expanding their footprint in Kampala with the opening of The Arena Mall in March 2020.

Knight Frank research registered increasing enquiries for retail space across various retail malls in general in H2 2018. The majority of inquiries came from international based retailers specifically in the fashion sector, which bodes well for consumers and developers alike as we head into 2019.

Retail rental rates have remained stable in the past half year and market related rentals in malls.

Warehouse, Plot M467, Hankook Road, Industrial Area Ntinda

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INDUSTRIAL

The industrial sector continues to be dominated by owner occupied property, and speculative development of warehousing space for rent. The KIBP continues to develop steadily, and is now taking shape as an industrial park of note. There also seems to be increased development of industrial space along Jinja Road up to Mukono and beyond, which has had a positive impact on land values for well located, encumbrance free land.

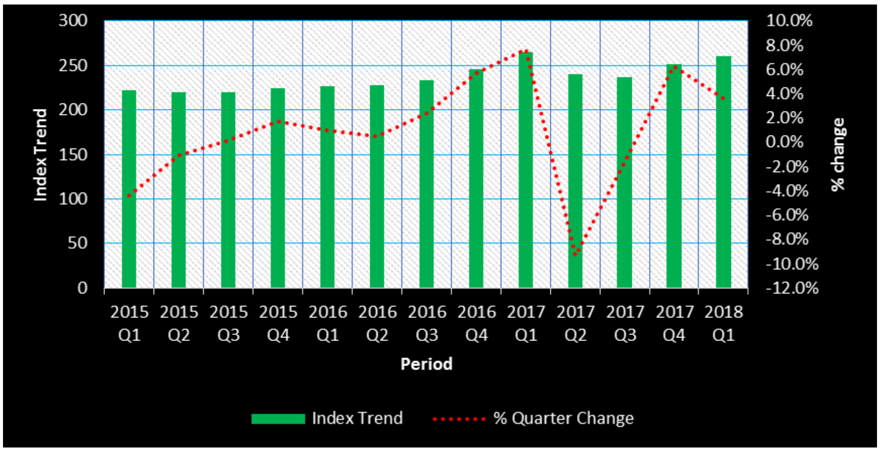
Knight Frank research recorded a slight (5%) year-on-year decline in rental rates for warehouses in the traditional industrial areas of Ntinda, Luzira, Bugolobi and 1st - 8th Street. This was mainly due to supply outstripping demand as some companies' continued to relocate to smaller premises. Additionally, we registered an overall 5% year on year reduction in occupancy rates from 77% in H2 2017 to 72% in H2 2018 on account of large corporations who moved from rented to owner occupied premises. This trend is likely to continue for the mid – short term.

On a positive note, Knight Frank registered a 4% annual increase in the take up of new warehouses (warehouses built in the last 1-3years) compared to the older stock of warehouses. This move has been driven by factors like the modern and high-quality specifications that the new warehouses offer. Approx. 26,000m^2 was leased in H2 2018 compared to 24,960 m^2 recorded for the same period last year. 90% of the leasing activity was recorded in the traditional industrial areas of Ntinda, Port Bell Road, 1st - 8th Street, Luzira. Average occupancy rates for the newer stock of warehouses was at 95% whereas the older stock sat at 49%.

Going forward, we anticipate an increase in demand for warehousing space in the next 12 months as the volume of goods produced by the manufacturing sector in the economy is projected to increase as evidenced by a 3.6% quarter on quarter increase recorded during Q1 of 2018. Likewise with projections of increased economic growth, increased trade and imports of consumer goods should translate into demand for storage and logistics space, boding well for this sector of the property market. [Table 6] [Figure 5]

Figure 5:

Quarterly trends for Index of production 2015-2018



Source: UBOS

VALUATIONS

The November 2018 performance of the economy report released by the Ministry of Finance, Planning and Economic Development revealed that the outstanding month on month stock of private sector credit reduced by 0.1% in October 2018 compared to September 2018 due to successful loan repayments that offset the increase in new credit extensions.

Our numerous discussions with various banks and financial institutions revealed that, despite the existing appetite from borrowers for financing, banks are not as bullish about lending, and are keener on streamlining their loan books with a view to minimizing non-performing loans. This is being done through "health check" re-valuations and peer reviews.

The valuation practice in Uganda is finally coming of age thanks to the Institution of Surveyors of Uganda (ISU), and the Regulatory body of the profession, The Surveyors Registration Board (SRB) who have advocated and indeed pushed for the full adoption and implementation of International Valuation Standards (IVS) as the guiding principles of valuations in Uganda.

This will not only build confidence and public trust in the profession which has suffered its fair share of bad publicity over the past few years, but also promote transparency and consistency in the valuation practice.

COMMERCIAL BRIEFING
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OUTLOOK FOR H1 2019

According to the December 2018 monetary policy statement released by Bank of Uganda, economic activity is projected to grow steadily over the next 12 months above the previously projected figure of 6%. The increase in economic growth in 2019 is expected to be driven mainly by a higher private sector credit extension thus spurring domestic consumption, multiplier effects of public infrastructure investment as well as improved agricultural productivity. Completion of on-going road infrastructure projects around Kampala coupled with the burgeoning middle class is expected to increase demand for home ownership particularly in areas surrounding Greater Kampala.

We envisage steady but slow improvement in office leasing activity, mainly driven by relocations from older to newer buildings, but also take up of office space by large corporations and organisations within the financial sector e.g. Afriexim Bank who will be opening their regional headquarters in Kampala in 2019. Performance of the residential rental sector continues to be dominated by demand from expatriates in the mid-level rental range where the "sweet spot" is between \$1,500 - \$2,000. Strong retail sector performance continues to be driven by the fashion, food, entertainment and leisure offerings at the malls in support of Kampala's reputation as a strong consumer driven market compared to other east African cities.


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