H1 2022 Kampala Market Performance Review

July 2022
The initial projections by the Bank of Uganda indicated a strong recovery improvement in economic activity. policy initiatives to boost private sector activity, are credited with the growth rate of 3.5% in FY 2020/21. The full reopening of the economy that the economy grew by 4.6% in FY 2021/22, compared to a revised GDP estimates from the Uganda Bureau of Statistics indicate growth for 2022, with estimates of 5.5-6.0% positive growth after easing Covid-19 restrictions, the revival of the services sector and growing activity in the oil and gas sector. However, difficult times as a result of global supply disruptions, and rising inflation have dampened prospects for domestic economic growth and increased uncertainty. Despite the slow but gradual recovery recorded for the most part of H1 2022 in different sectors of the economy, these events have culminated in varying results, with particular effects on growth projections which were revised downwards by 20% to rest at 4.5-5.0% as of June 2022.

The Monetary Policy Committee tightened monetary policy measures in response to escalating inflation brought about by: external cost pressures, persisting global production and distribution bottlenecks, and rising domestic food crop prices. In July 2022, Bank of Uganda (BOU) increased the Central Bank Rate (CBR) by 100 basis points for the second month in a row to 8.5% in a bid to stabilise inflation around the 5% medium-term target. This will likely push up lending rates that had declined marginally by 0.54% in the year ended May 2022. The Uganda Shilling, which had strengthened against the US$ by 4.2% in the year ended February 2022, experienced depreciation pressures in March, May and June 2022. This has worsened the inflation forecasts, with projections peaking to a 7.4% peak, until Q2 2023 when it is expected to peak, before gradually declining to stabilise around the 5% medium-term target in mid-2024.

Inflation rose systematically in H1 2022, owing to increased demand against low supply following the re-opening of various economies globally, and aggravated by supply bottlenecks as a result of global tensions induced by the Russian-Ukraine conflict. Due to rising commodity and energy costs, inflation scaled up by 0.5% in June 2022. The Monetary Policy Statement for July 2022 forecasts average annual headline inflation at 7.4% in 2022. The Business Tendency Index, which measures optimism about the business environment, showed positive sentiments for the 12 months to April 2022, but fell marginally by 0.54% in the year ended May 2022. The Uganda Shilling, which had strengthened against the US$ by 4.2% in the year ended February 2022, experienced depreciation pressures in March, May and June 2022. This has worsened the inflation forecasts, with projections peaking to a 7.4% peak, until Q2 2023 when it is expected to peak, before gradually declining to stabilise around the 5% medium-term target in mid-2024.

For H1 2022 also witnessed the opening of the Rwanda-Uganda border at Gatuna/Katuna, following a three-year closure due to an impasse between the two countries. The re-opening of the border is anticipated to increase the volumes of traded goods and cargo across the two East African nations, steadily boosting revenues in the long run.

An uptick in office and leasing activity observed.
- Headline inflation increased.
- The Uganda Shilling depreciated.
- The Landlord and Tenant Bill was assented into law.
- Residential pipeline activity increased.
- Prime office rents remained relatively stable.
COVID-19

COVID-19 restrictions that had been in place for about two years were lifted in January 2022, resulting in a steady increase in activity in previously hard-hit sectors like the Education, Leisure & Hospitality, and Tourism. Furthermore, following the 5th SAC Extraordinary Sectoral Council of Ministers of health, the decision to eliminate mandatory COVID-19 tests for travelers, including truck drivers who had already undertaken tests and had PCR results from SAC-accredited laboratories within a 72-hour validity window was reached.

The reduced COVID-19 situation in H2 2022 resulted in the suspension of the requirement for negative PCR tests done within 72 hours for all outbound travelers who are fully vaccinated, except where it is a requirement of the destination country. Travelers with partial or no vaccination are required to present a negative PCR test done within 72 hours of travel.

A COVID surge was however witnessed in June 2022, with a rise in daily number of COVID-19 cases. This prompted the Ministry of Health to ramp up vaccination drives in different locations within the country and re-echo the importance of vaccination as a key tool to combat the virus.

EMERGING TRENDS: ESG

Environmental, Social, and Governance (ESG) criteria is a trending topic both globally, and in Uganda. With growing expectations from investors, occupiers, and employees and the increasing emphasis on green initiatives, companies are looking to align their operations and investment decisions moving forward. ESG criteria focuses on companies procurement, investment, and distributing retirement funds from Ugandan employees, of the private sector who are not covered by the Government Retirement Scheme. The Retirement Benefits (Regulations) were launched on May 10, 2022, at a public launch event held at the Uganda Retirement Benefits Authority (URBRA) Chief Executive Officer.

The Regulations aim to provide for procedures that a member shall follow in order to use a portion of their benefits to secure a mortgage or loan for the purchase of a residence. This applies to members of pension schemes that are licensed by the Uganda Retirement Benefits Authority (URBRA). The regulations provide members the right to pledge the member’s benefits as collateral for a mortgage or loan from an accredited financial institution for the purchase of a residential home, provided that they meet the strict eligibility requirements outlined in the Regulations.

The National Social Security Fund (NSSF), however, does not currently have an enabling framework that operationalizes the spirit of the Regulations. The Fund is the quasi-government agency in charge of collecting, storing, investment, and distributing retirement funds from Ugandan employees, of the private sector who are not covered by the Government Retirement Scheme. In particular, s 34A(4) of the NSSF Act conflicts with the Regulation by requiring any assignment of, or charge on, the account of a member of the Fund or any benefit payable out of this account or any agreement to assign or charge any such account or benefit. However, there is no cause for alarm as NSSF has gone on public record to say they will accept the conflicting clauses in the NSSF Act.

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The prime office market marked an uptick in leasing activity in H1 2022. Enterprises increased, driven in part by the full reopening of the economy, increased start-up funding, improved activity in the services sector, and the signing of the FID in early February. Demand was from a wide range of sectors including Financial Services, Technology/Telecoms, Oil & Gas, Health, Fitness & Professional Services. The high activity was predominantly driven by start-ups, Industrial/Logistics, Legal as well as Government agencies. These were either new entrants or existing firms that were expanding or relocating. Take-up was also registered from occupiers who had previously downsized at the onset of the pandemic and are currently seeking to reoccupy the spaces they had relinquished. As a result, occupiers increased by 20% in H2 2022 as compared to the same period in 2021. Similarly, Grade A office occupancies were up by 1% while grade AB occupancies increased slightly by 2% in the same period, largely attributed to existing occupiers increasing their space take-up. Despite the positive trend in uptake, several landlords were cautious, opting to maintain prevailing rents. However, a few landlords who had discounted rents at the onset of the pandemic revised their rents upward during contract renewals. This however had a marginal impact service charges accordingly.

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### RETAIL SECTOR

The retail market performance as measured by footfall and turnover improved by 6% and 8% respectively in H1 2022 as compared to a similar period in 2021, attributed to the full reopening of the economy in January 2022. While noticeable uptick in retail activity was observed on a year-on-year comparison, turnover growth for general grocery retail and average footfall remained subdued, showing a negative growth of 20% & 23% compared to pre-Covid numbers respectively as of May 2022.

Positive growth in average turnovers was recorded on a monthly basis in the quarter to April 2022, but dipped by 5.8% in May 2022. This was on the back of rising commodity and fuel prices that affected affordability among consumers. A similar trend was observed with the monthly footfall figures that declined by -9% and -2% in April and May 2022 respectively.

The continuous rise in inflation in Q2 2022 affected consumers' disposable income and spending habits, necessitating prudent expenditure planning. This affected footfalls and had a correlated effect on the average turnovers in the same period. Our outlook is that this trend will likely persist in the short term as countries world over grapple with rising costs of commodities and fuel.

Retail rents (Covid-adjusted) remained stable in the last two years, owing to increasing flexibility among landlords who sought to protect retailers from the effects of the pandemic. As a result, average occupancies in Knight Frank managed malls maintained relative stability in H1 2022 at approximately 86% on the back of new retailers entering the Ugandan market and existing retailers expanding their footprint.

Humle, an international fashion brand, entered the Ugandan market in H1 2022, and the retailer is presently opening two locations at two malls in Kampala, which are anticipated to open in Q3 2022. Century Cinemas, East Africa’s well-known cinema operator, plans to open their third cinema in Uganda in Q3, following the full re-opening of the economy.

CafeSorria, a well-known restaurant established both their third restaurant in Kampala, as well as Frego, their first chicken restaurant, at the Arena Mall.

The prime retail market was void of occupiers to the country and growing activity in the oil and gas sector. Apartments in the upscale neighborhood of Nakasero, Kampala, also were in high demand, with noticeable interest in 1- and 2-bedroom options. As a result, prime residential occupancies increased by 1%, while rents maintained relative stability.

Retailers continued to reduce rents to make available to the affluent suburb market. These decreases are for prime residential accommodation, (which is currently dominated by landlords in the oil and gas sector). Tenants continue to drive harder rent bargains, and in most cases getting them. This is also coupled with the fact that they are taking on numerous residential units which further strengthens their bargaining position.

In terms of number of units, the residential apartment market in Kampala is the most robust in the country, with approximately 88% on the back of new retailers expanding their footprint, assisting small- and medium-sized businesses. The industrial market remained resilient in H1 2022, and the industrial park, provided serviced workspaces in industrial areas within Kampala has prompted landlords to seek locations in the suburbs such as industrial areas within Kampala has prompted landlords to seek locations in the suburbs such as Kampala, Ntinda, Naguru, Mbuya, Bugolobi, Muyenga, Munyonyo, Ms vision, and Luzira, and has attracted larger. Dolder leases were observed in Nasik, Kivulwe, and Najera, which were initially stripping down.

These figures are average rentals for ground floor warehouses and showrooms, with excellent amenities in strategic locations. The limited stock of apartments especially in the suburbs of Nakasero, Kololo, Naguru, Mujuwaka, Bugolobi, stretching to Muyenga, Ntinda, Luzira, Munyonyo, Munyonyo, and Luzira has attracted larger. Dolder leases were observed in Nasik, Kivulwe, and Najera, which were initially stripping down.

### RESIDENTIAL SECTOR

In the period under review, the prime residential market opened up to increased sales and rental activity, on the back of the return of expatriates to the country and growing activity in the oil and gas sector. Apartments in the upscale neighborhood of Nakasero, Kampala, also were in high demand, with noticeable interest in 1- and 2-bedroom options. As a result, prime residential occupancies increased by 1%, while rents maintained relative stability.

We found that there is a rising demand for prime residential accommodation, (which is currently dominated by landlords in the oil and gas sector). Tenants continue to drive harder rent bargains, and in most cases getting them. This is also coupled with the fact that they are taking on numerous residential units which further strengthens their bargaining position.

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Tenants have been observed to opt for quality warehouses and showrooms, with excellent amenities in strategic locations. The limited number of units in the suburbs of Nakasero, Kololo, Naguru, Mujuwaka, Bugolobi, stretching to Muyenga, Ntinda, Luzira, Munyonyo, Munyonyo, and Luzira has attracted larger. Dolder leases were observed in Nasik, Kivulwe, and Najera, which were initially stripping down.

### INDUSTRIAL SECTOR

The industrial market remained resilient in H1 2022, supported by government initiatives to boost industrialization in the country and the signing of the FID in February 2022. Industrial space demand persisted in H1 2022, and 2023 has been highlighted by USAID as the key focus for enhancing domestic investment. The Authority, through a dedicated team (the Domestic Investment Directorate), focused on assisting small- and medium-sized businesses (SMEs) to scale-up to compete with significant local and international investors, offer them serviced workplaces in industrial areas, and provide training and other capacity-building programs.

Industry space demand persisted in H1 2022, driven by increased economic activity following the relaxation of lockdown restrictions, growing movement in the oil and gas sector, growth of e-commerce, and the need to locate production in order to address supply shortages. Agriculture, fast-moving consumer goods, manufacturing, technology, logistics, retail, and energy are among the sectors that are driving demand.

A sustained growth in industrial market activities is projected, especially with the drive to ramp up local manufacturing. Agro-industrialization, one of the key priority sectors in line with the NDP II, was emphasized as a key focus area for the upcoming fiscal year in the budget read in June 2022. Some of the intervention strategies to promote agri-industrialization, standards and market-entry include: Expanding storage and processing capacity for agricultural commodities, Enhancing the use of the Warehouse Receipt System to improve commodity storage, Reduce post-harvest losses, Improve value chain management.

Sources: Knight Frank Research

The rise in inflation is projected to result in high cost of production for local manufacturers.

The rising cost to local production will likely have a large effect on the H2 2022 market. The list of incentives should inflation persist in the long run.

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An extension in the geographical scope of the dollar market was observed in H1 2022. This market, which was historically concentrated in the affluent suburbs of Nakasero, Kololo, Naguru, Mujuwaka, and Bugolobi, stretching to Muyenga, Ntinda, Luzira, Munyonyo, Munyonyo, and Luzira has attracted larger. Dolder leases were observed in Nasik, Kivulwe, and Najera, which were initially stripping down.

This suggests that multi nationals with lower rental allocations are now moving outwards to more affordable areas.

Demand for residential space in the suburbs has persisted, attributed to the slighty lower rentals and the high quality of the new available stock. Given the increasing demand in the affordable market segment, developers are now offering more affordable options.

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There have been continuous parallels drawn between the unforeseen risks caused by the pandemic and the climate crisis, which have both significantly affected the global economy. This has resulted in a need for greater investment and progress on matters relating to Environmental, Social, and Governance (ESG) by both investors and policy makers. This has also attracted the attention of lenders and other property stakeholders as ESG may affect prospects of rental and capital growth and would as a result influence investment approach. This prompted theRICS to develop and prepare a new guidance note entitled “Sustainability and ESG in Commercial Property Valuation and Strategic Advice”, which focuses on commercial property valuations. The guidance note, which was effective from 31 January 2022 is partly aimed at relating commercial valuation practice to the wider ESG and sustainability landscape.

The proposed tabling of the valuation bill will be a milestone for the valuation profession, which has for long relied on global standards in the absence of local ones. The bill when passed into law will establish the office of the Chief Government Valuer and provide a backbone for the valuation of property and other assets. Furthermore, the bill is expected to establish the criteria by which valuation surveys shall be prepared. It is hoped that the tabling of the valuation bill will support the drafting of local valuation standards and guidelines which are currently anchored on the International valuation standards as best practice recommends, but yet to be formally adopted. According to the Background to the Budget FY2022/23 issued by Ministry of Finance, Planning and Economic Development, the ratio of Non-Performing Loans (NPLs) to total loans increased by 0.4% year-on-year in Q2 2022. The sectors that saw the highest increase in NPLs were building/construction & real estate and business services, which increased from 9.7% and 7.2% to 10.1% and 8.8% respectively within the same period. This trend is consistent with the increase in instructions for foreclosures witnessed in the period under review.

The hospitality and tourism industry, which has been on a recovery trajectory following the reopening of boarders globally, will continue to see improvements thanks to higher COVID-19 immunization rates, loosened travel restrictions, and enhanced government support.

The current high commodity and fuel prices have affected consumers’ disposable incomes. As customers prioritize their purchases, the ongoing price increase is anticipated to have an impact on domestic demand, causing a decline in foot traffic and turnover at various shopping centers.

Future developments are projected to take into account the growing need for 1-bedroom units given the limited supply and the fact that the bulk of current and upcoming projects offer 3-bedroom units.

The rising number of apartments, particularly 3-bedroom units in Kololo and Naguru suburbs, is anticipated to exacerbate the problem of an oversupply of prime units in the long run, necessitating downward rent reviews in an effort to manage vacancy pressures.

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With Mezini earmarked as a supply terminal and logistical hub for the oil activities, and Luwero and Nakawuka designated as logistics and supply terminal’s transit nodes, increased infrastructure development in these areas will support the ongoing activities and provide accommodation for project staff and the expatriates is expected.

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