H2 2022 Kampala Market Performance Review

January 2023

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KEY INSIGHTS

HEADLINE INFLATION INCREASED

THE UGANDA SHILLING DEPRECIATED

CBR RATE INCREASED

PRIME OFFICE OCCUPANCIES INCREASED

RESIDENTIAL PIPELINE ACTIVITIES INCREASED

RETAIL FOOTFALL INCREASED

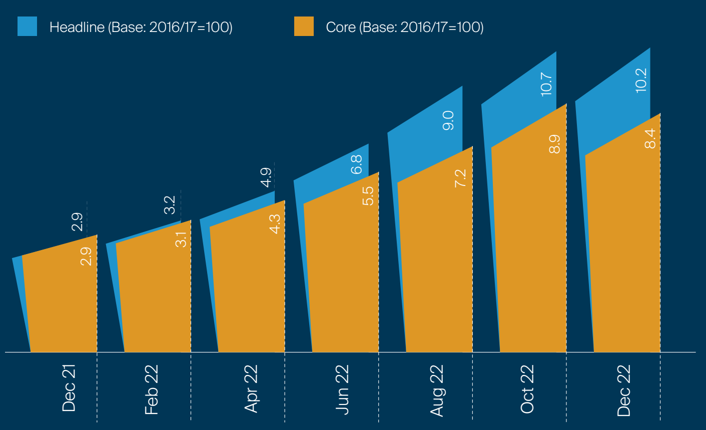
THE ECONOMY

"The tight monetary control measures instituted by the Central Bank resulted in high commercial bank lending rates for both shilling and foreign currency denominated loans"

2022 was a year of resilience, circumspection, and optimism. The positive rebound in economic activities recorded in 2021 and early 2022 was followed by slow developments as risks continued to emerge. Negative spillovers from geopolitical tensions, COVID-19 induced supply chain disruptions, the Ebola outbreak, and adverse weather conditions further dimmed the prospects for domestic economic recovery. Across the different real estate subsectors, the post-pandemic recovery was optimistic, with demand and supply indicators pointing to positive growth on a year-on-year comparison.

The sharp rise in inflation, recorded at 10.2% as of December 2022, caused by a combination of global factors, adverse weather conditions and the weaker shilling as compared to other foreign currencies triggered tighter monetary control measures, with BOU increasing the CBR by 3.5 percentage points year-on-year to 10.0% as of December 2022, and also increasing the cash reserve requirement by 2 percentage points effective June 2022, in an effort to reduce the amount of money in circulation. A cost-of-living crisis was imminent given the reduced real incomes. While some investors froze their investment decisions until the tide was calmer, others took the bold decision to proceed with business as usual.

Annual Inflation Rate Development

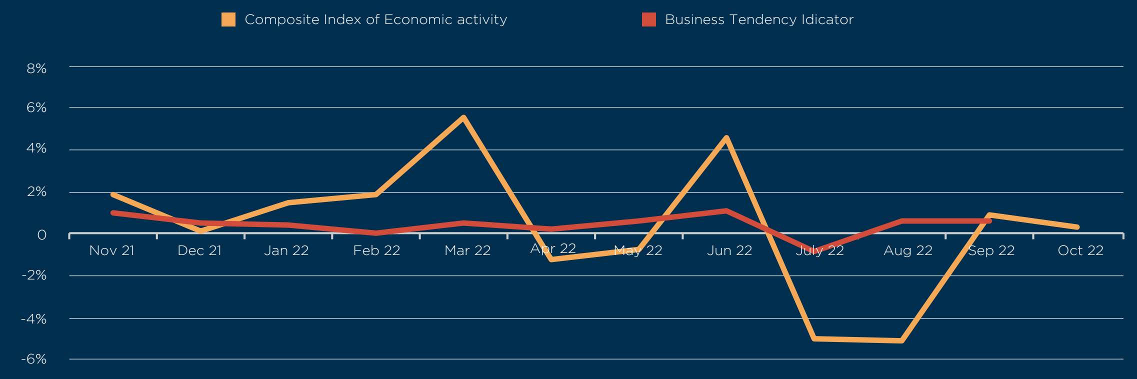


On a positive note, sentiments about the business environment as measured by the Business Tendency Index improved in the quarter to October 2022, while the composite index of economic activity showed a pickup in activity in the same period.

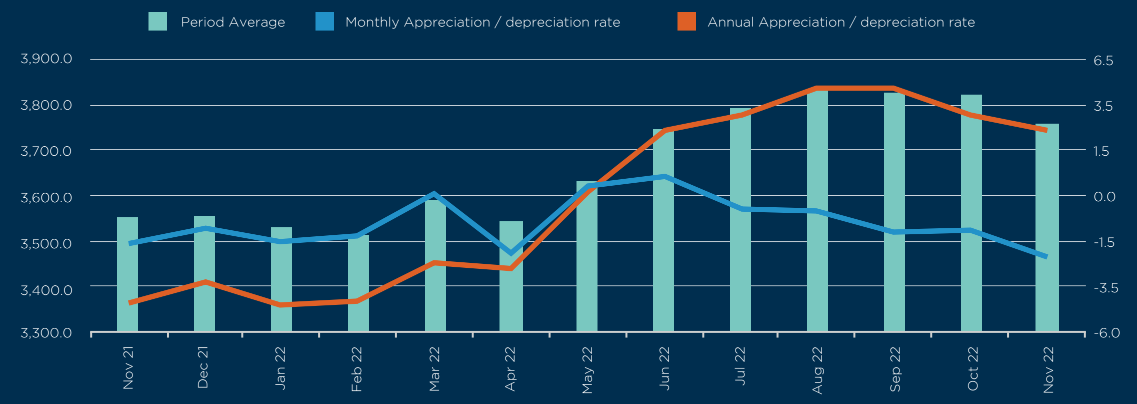
The performance of the shilling remained subdued in the period under review, recording an average annual depreciation of 5.9% as of November 2022. Performance improvements were recorded in October and November 2022, with monthly appreciations of 0.08% and 1.6% respectively, supported by the tightening of the monetary policy, a decline in global commodity prices, an increase in remittances and foreign direct investment in the oil and gas sector.

The tight monetary control measures instituted by the central bank resulted in high commercial bank lending rates for both Shilling and foreign currency denominated loans. As a result, the weighted average Shilling-denominated lending rate increased by 1.3% in the quarter to October 2022. Similarly, yields on Treasury Bills increased to 15.4% for the 364- day treasury bill, while the 91-day treasury bill remained relatively stable month-on-month at 11.4% in November 2022.

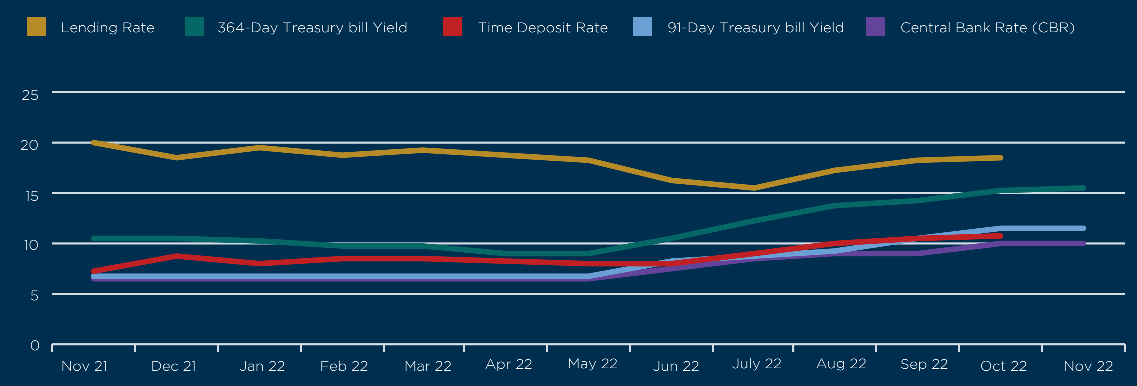
Real Sector Indicators Growth Trend



Exchange Rates Performance



Annual Interest Rates Performance



Source:Bank Of Uganda

THE REAL ESTATE SECTOR

OFFICE

The pace of construction slowed down, given supply bottlenecks and the high costs of materials as a result of high inflation, resulting in longer than anticipated construction periods

In the office market, occupier activities were vibrant at the start of the year, following the signing of the FID and the full reopening of the economy. The high inflation rates in H2 2022 affected disposable incomes, resulting in some potential occupiers differing their space needs, while others downsized. On an annual basis, absorption rates were high, with approximately 12,800 square meters of lettable space taken up in 2022, resulting in average occupancy rates increasing by 8%. The high occupier activities in the first two quarters prompted some landlords to revise the initially discounted rents upwards as the market conditions pointed to a return to normalcy. As a result, average rents in prime office buildings increased by 3% in H2 2022.

Occupier interests were hinged on relocations, expansions, and start-ups, driven by sectors like oil and gas, financial services, and business and professional services. Typical size requirements varied, with a noticeable rise in demand for smaller office spaces (between 50 to 200 square meters).

The high costs of doing business as a result of high inflation rates prompted occupiers to drive harder bargains for rent discounts although landlords insisted on maintaining the prevailing rates.

Strong demand for best-in-class office space against a backdrop of limited supply in this segment persisted, especially from financial institutions and oil and gas-affiliated organizations. Newer buildings with better facilities and fittings, sufficient parking, and professionally managed, were proven to be more attractive to blue chip occupiers. This encouraged some landlords to upgrade/refurbish the existing stock of buildings to meet the growing demand. The limited supply of this standard of property presents an opportunity for developers seeking to enter the market and those with projects in the pipeline, to ensure the quality of stock meets the demand requirements of the occupier and the trending ESG requirements.

Office Key Take Aways

- 12,800 SQUARE METERS TAKEN UP
- 8% AVERAGE ANNUAL INCREASE IN OCCUPANCIES
- STRONG DEMAND FOR PRIME SPACE PERSISTED
- 150,000 SQUARE METERS OF OFFICE SPACE IN THE PIPELINE

Source: Knight Frank

Luthuli House, prime office space to let.

Construction activity remains high, especially in the suburbs of Nakasero, Kololo, and Bugolobi, with new buildings completed, including the PPDA-URF Towers, the New ERA House, Cementers, Uganda Business Facilitation Centre (UBFC), Insurance Tower and Luthuli House, accounting for about 60,000 square meters of total new stock, and at least 150,000 square meters in the pipeline, expected in the next 12 to 24 months. 95% of the total new stock is for owner occupation, largely by government agencies.

With the planned government campus in Bwebajja, a one stop complex for government ministries, measuring approximately 150,000 square meters, we anticipate vacancy pressures on lower grade buildings to persist. This pressure will be particularly high in buildings where the government agencies and ministries previously had, and currently have their offices. Landlords will be pushed to upgrade their premises to meet the demand for best-in-class facilities, in order to compete favourably, or discount rents to remain attractive.

The pace of construction slowed down, given supply bottlenecks and the high costs of materials as a result of high inflation, resulting in longer than anticipated construction periods. Project construction periods, which typically averaged at two years pre-pandemic, are now averaging between three to four years post pandemic.

Net Zero initiatives and ESG standards coupled with flexible office options, and coworking models will be pivotal in the future office, supported by multinational requirements. With at least 4.2 million square meters of EDGE-certified floor space throughout Africa, Uganda, is still in the nascent stage of green development. This, coupled with the fact that 40% of annual global carbon emissions are attributed to the built environment, initiatives to reduce the carbon footprint will be key, and as such, developers will be pushed to deliver on these metrics.

Office Rent and Occupancy Performance-H2 2022

GRADE A

US$ 15.0 Average Net Rent Per SQM per month

95% Average Occupancy

GRADE AB

US$ 12.5 Average Net Rent Per SQM per month

84% Average Occupancy

Source: Knight Frank

RETAIL

Footfall figures remain circa 18% below the pre-pandemic performance, particularly due to the high inflation rates that caused consumers to adopt cautious and conscious spending habits, and the outbreak of the deadly Ebola virus in September 2022

A slow but steady recovery was observed in the retail sector, with improvements in footfall, turnover and occupancies. Across Knight Frank managed malls, average footfall improved by 40%, turnovers for general grocery retail recorded a 15% growth and average occupancies were up by 2.7% year-on-year.

The sector recovery in terms of foot traffic was aided by the return of Black Friday promotions, as well as the steady recovery of the cinema industry, with the return of blockbuster movies. The footfall figures however, remain circa 18% below the pre-pandemic performance, particularly due to the high inflation rates that caused consumers to adopt cautious and conscious spending habits, together with the outbreak of the deadly Ebola virus in September 2022. The threat of the spread of the virus in the country and the commercial hub of the greater Kampala region, affected the anticipated recovery in the hospitality and retail sectors, as there was increased cautionary spending and panic cancellations from travellers during this period. With the current statistics from the Ministry of Health, pointing to the disease as under control, thanks to the strict protocol and immediate control measures that were instituted by the government, the spread of the virus was contained, thus alleviating fears of country-wide lockdown and boosting the sector recovery.

SQFT
48,440
space leased out in Knight Frank managed malls for H2 2022

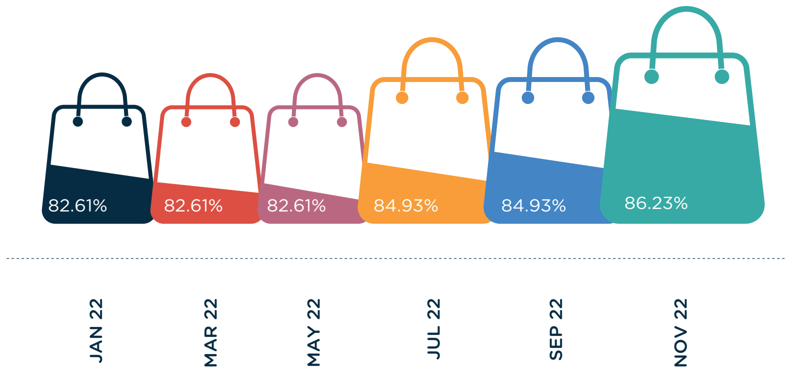
The retail leasing market was vibrant, with approximately 48,440 square feet of space leased out in Knight Frank managed malls for H2 2022. New retailers entered the market, with brands such as Hummel, U-Home and Optica establishing their presence while others such as LC Waikiki, Yashika, FB Fashions and Woolworths expanded to other malls.

Fashion retailers and restaurant owners, who were either expanding or establishing their presence, dominated the leasing market. New entrants like Hummel opened stores at the Acacia Mall, while South African retailer, Woolworths expanded into their fourth store at the Village Mall. Century Cinemax, with their first VIP movie hall, opened a third store at the Arena Mall to the excitement of movie revellers. LC Waikiki also expanded into Entebbe with their third store anticipated to open at Victoria Mall in Q1 2023. The Patio Brasserie, one of Kampala's fastest growing bar and restaurant chains and Middle East Restaurant expanded into the Arena mall. This is all testament to the rebounding retail sector, and resilience amidst adversities and uncertain trading conditions after the long lockdown period.

It is still uncertain when the retail performance, as measured by footfall, will fully return to the pre-pandemic numbers, given the high inflation rates and a possible Covid-19 resurgence. Shopping center management and operation, using flexible and agile solutions, continue to underpin the sector's performance.

TMT Atrum - Ntinda, Prime Retail Space To Let.

Average Occupancy in Knight Frank Managed Malls



Source: Knight Frank

Retail Key Take Aways

15% GROWTH IN ANNUAL TURNOVER

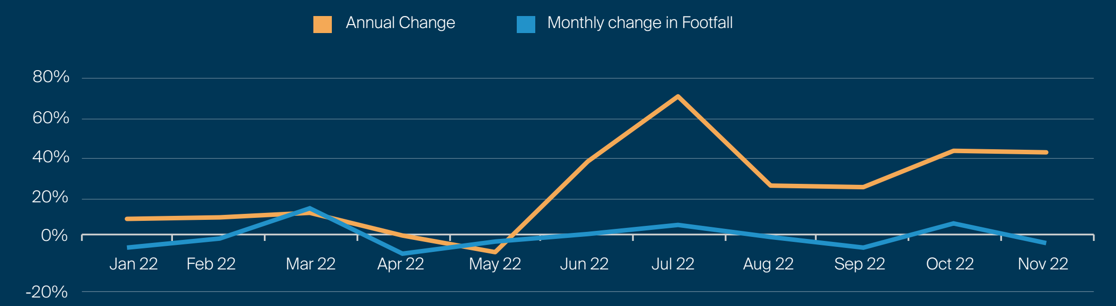
2.66% GROWTH IN OCCUPANCY

40% INCREASE IN ANNUAL FOOTFALL

4,500 SQUARE METERS LEASED OUT IN KF MANAGED MALLS

Source: Knight Frank

Growth in Footfall in Knight Frank Managed Malls



Source: Knight Frank

RESIDENTIAL

Effective demand for middle and affordable housing continues to grow steadily. This is particularly the case in the growth residential nodes in Nakawa Division, Kajjansi town council and Kira municipality.

Residential land price growth in select prime areas slowed down in H2 2022, with the increased supply of re-development plots against low demand. Developers, who typically make up most of the land purchasers in the affluent suburbs, were negotiating or forming joint ventures in an effort to reduce costs associated with redevelopment. This impacted sale prices, resulting in some vendors reconsidering their decisions to sell. As a result, average land prices per acre in affluent suburbs such as Kololo reduced by approximately 10% in H2 2022, as compared to the same period in 2021. This is also causing the market prices to correct and adjust accordingly to match the rental rates being achieved.

Leasing activity proved resilient, with an uptick in inquiries, on the back of the opening of economies globally, and growing activities in the oil and gas sector. This vibrancy however soon tapered off, with growing uncertainties as a result of global geopolitical conflicts. Average prime residential rents remained stable on a y-o-y comparison, while occupancies increased slightly by 2%.

A trend observed over the half year was landlords developing larger more expensively serviced units for sale in Kololo, at price ranges between $500,000 and $700,000 for apartment sizes ranging from 300 to 500 square meters. It is becoming increasingly evident however, that the Ugandan market is yet to realize effective demand for residential units at this price range. The sweet spot for prime residential units is between $250,000 to $350,000 for an apartment in the prime suburbs.

Residential pipeline activity remains high, with apartment units in Naguru/Kololo/Nakasero coming online in the next 2 years estimated at approximately 500 units. The developers are both new and existing players in the market. Most of the new players/ first time developers are coming into the market to try and capitalize on the oil and gas buzz as speculators. Some of the new players are taking longer to complete projects, an aspect that is influencing potential buyers to negotiate prices, and request for better long-term payment methods especially for purchasers who are avoiding loan facilities.

There is still a lack of product selling at between $100,000 - $150,000 in the prime and semi-prime locations in a radius of approximately 10 - 12 kilometers from the city center. These include areas such as Ntinda, Muyenga, Makindye, Mutungo, Luzira, Mbuya, Kyambogo, Mengo, and Rubaga, among others. These locations have effective demand at this price bracket, but not the required quality and availability of product.

Effective demand for middle and affordable housing continues to grow steadily. This is particularly the case in the growth residential nodes in Nakawa Division, Kajjansi town council and Kira municipality. Absorption rates for rental apartment units in these suburbs were high, with average occupancies above 85%. Infrastructural improvements (mainly accessibility and road improvements), easy access to amenities, and other services such as schools, health facilities, banking services and restaurants have boosted demand in these areas. Residential housing developers are now more aware and appreciative of the affordability gap and are making efforts to provide value for money by heeding the price and quality requirements of the population. With the current housing deficit, estimated at 2.4million units, government and major institutional investors' initiatives in providing affordable housing will be crucial to encourage other developers to invest in the sector.

Windsor Apartments, Windsor Crescent Kololo, For Sale on Condominium Basis.

NEXT NEIGBORHOOD HIGHLIGHTS

NAJJERA

Income Yields (%)

8%-12%

Median Rents (UGX)

UGX 600,000

UGX 850,000

UGX 1,200,000

DISCOVER MORE

KYANJA

Income Yields (%)

8%-12%

Median Rents (UGX)

UGX 650,000

UGX 900,000

UGX 1,200,000

DISCOVER MORE

Residential Key Take Aways

2% ANNUAL INCREASE IN OCCUPANCIES

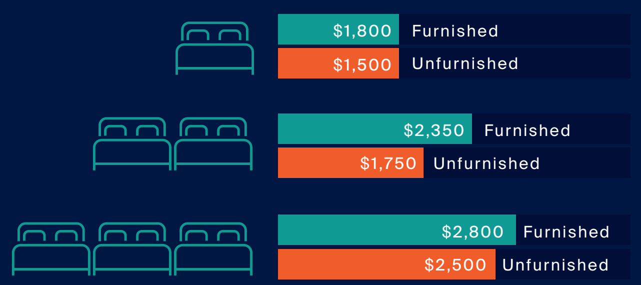
INCREASED SUPPLY OF REDEVELOPMENT PLOTS

500 UNITS EXPECTED IN THE NEXT 12 TO 24 MONTHS

RENTS REMAINED STABLE

Source: Knight Frank

Average Net Monthly Rent ($) and Occupancy (%) in Kampala's Prime Residential Suburbs



78%

OCCUPANCY

H2 2022

Source: Knight Frank

INDUSTRIAL

A rise in demand for warehouses for rent was observed, from logistics, cold storage, and agricultural processing

Industrial space requirements remained relatively stable in H2 2022, despite the high inflation, dry weather conditions, currency depreciation, and rising costs of finance. Warehouse leasing dominated the inquiries, at approximately 70%, while sales inquiries accounted for 30%. Of the sales inquiries, 97% were for land, with size requirements ranging between 5-15 acres, predominantly in the Kampala Industrial Business Park (KIBP)-Namanve, which offers suitably sized industrial land options for greenfield projects. This demand, especially in the KIBP- Namanve has been largely attributed to the park's strategic location and proximity to Uganda's main business hub (approximately 15Km from Kampala's City Center), location along the corridor to the Kenya border, government incentives to boost industrialization as well as the strategic future added advantage like connectivity to the planned Southern by-pass, Bukasa Port, and the Standard Gauge Railway.

A rise in demand for warehouses for rent was observed, with demand from logistics, cold storage, and agricultural processing. Warehouse occupier requirements were mostly for large spaces, between 500-2,000 square meters, dominated by Fast Moving Consumer Goods (FMCG) suppliers, cold storage and distributors.

Average rents for warehouses remained relatively stable throughout the year, ranging between US$3 to US$5.5 per square meter in the Kampala Industrial Business park -Namanve (KIBP), while warehouses in the traditional Kampala Industrial area were between US$5- US$7 per square meter.

Emerging opportunities were evident for SME businesses, cold storage, agribusiness and industrial research given the increased government initiatives to invest in infrastructure, innovation and business incubation centers.

RENT PER SQM PER MONTH

$3.0 - $5.5

KAMPALA INDUSTRIAL BUSINESS PARK NAMANVE

RENT PER SQM PER MONTH

$5.0 - $7.0

TRADITIONAL KAMPALA INDUSTRIAL AREA

VALUATION

A slight improvement in the commercial banks' asset quality was recorded in September 2022. The ratio of non-performing loans to total gross loans decreased from 5.3% in June 2022 to 5.2% in September 2022.

Following the government's lifting of COVID restrictions in January 2022, the year was off to an upbeat start in terms of valuation inquiries. According to data from the Bank of Uganda, commercial banks advanced 8.5% more mortgages during Q1 2022 than they did in the same period the previous year. A cocktail of factors, including supply chain disruptions as a result of global tensions, and effects of adverse weather conditions, culminated in high inflation in H2 2022, resulting in stringent monetary control measures by the central bank and subsequently a rise in mortgage lending rates. As lending rates increased, the number of non-performing loans (NPLs) to total gross loans increased from 4.79% in FY 20/21 to 5.32% in FY 21/22 according to Bank of Uganda. This shows that even though more mortgages were advanced, the ability of mortgagers to repay was relatively low, partly due to the increase in interest rates. This was further evidenced by the rise in foreclosures and the increased number of properties on the market for sale. This may prompt lenders to take a more cautious stance when advancing mortgages, taking into account the credit worthiness of borrowers.

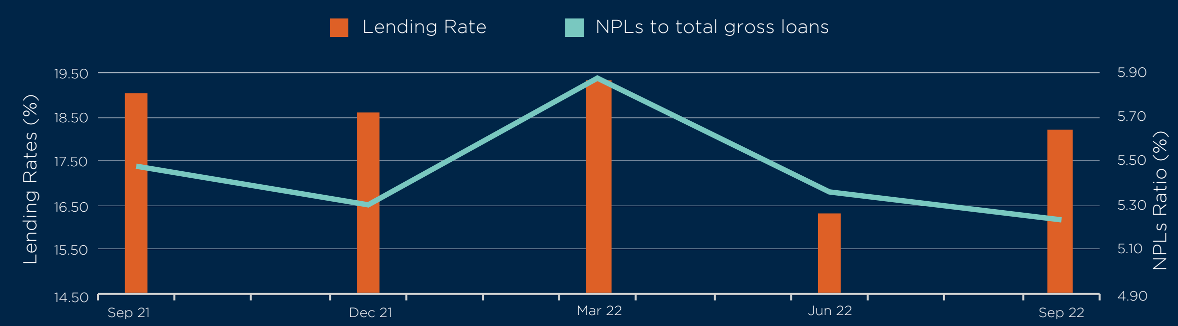
A slight improvement in the commercial banks' asset quality was recorded in September 2022. The ratio of non-performing loans to total gross loans decreased from 5.3% in June 2022 to 5.2% in September 2022. NPLs levels dropped in the sectors of transport, building, construction & real estate, community, and social and personal & household

loans. According to Bank of Uganda, this improvement could reverse, following the expiry of credit relief measures and the disruptions in the economic recovery.

Climate change has become a major global concern and the Sustainable Development Goals (SDGs), particularly SDG 13 advocate for an urgent course of action by the global community. The COP 27 conference held in Egypt sought to address the issues with a focus on reduction of carbon emissions by 45% by 2030 and reach net zero emissions by 2050 in order to keep the 1.5-degree Celsius temperature goal set by the Paris agreement within reach.

The Paris agreement also focusses on strengthening global response to the threat of climate change. Urban sprawl, and city growth are on the rise, and by 2050, it is expected that there will be 9.8 billion people on the planet. The carbon footprint is anticipated to increase in the absence of immediate action. In property valuation, the concept of sustainability has become a global requirement and valuers in Uganda are becoming cognizant of incorporating Environmental, Social and Governance (ESG) aspects into valuation assessments. This will be dependent on availability of transaction evidence that puts into account ESG factors. With the increase in ESG and demand for green buildings, valuers need to remain knowledgeable on the matter and develop inspection checklists incorporating ESG aspects observed in properties.

Lending Rates Vs NPLs to Total Gross Loans



Source: Bank of Uganda

2023 OUTLOOK

BOU projects that inflation will average between 6- 8 % in 2023, before returning to the medium-term target of 5% by the end of the year

According to the Bank of Uganda (BOU) State of the Economy report, the domestic economy remains largely resilient to the current external shocks and is expected to grow in the range of 5.0% to 5.3% in the FY 2022/23 from 4.6% in FY 2021/22, driven by improvement in agricultural productivity as a result of government intervention, investments in the oil sector and a rebound in industrial activity.

BOU further projects that inflation will average between 6- 8 % in 2023, before returning to the medium-term target of 5% by the end of the year. The downward revision of the inflation outlook is as a result of the waning impact of the earlier increase in global energy and nonenergy prices, reduced domestic and external demand, lower exchange rate depreciation, current monetary policy stance, and the anticipated decrease in global inflation and international commodity prices.

In the residential property market, demand for housing in secondary markets, away from the prime suburbs, will continue. Investment opportunities in the secondary residential suburbs will increase, given the growing young population and potential for good absorption rates. It will be upon investors to strategize and capitalize on this opportunity.

The growing demand for smaller unit types (1-and 2-bed units), observed over the half year in the prime suburbs will also persist.

The general outlook for the office market remains positive, albeit hinged on demand from players in the oil and gas sector, financial services, and professional services. The post-pandemic office recovery has proved resilience in the sector, with increased occupancies and stable rentals.

The current deficit in the supply of grade A office space is projected to persist in the short term, given that most office buildings (for rent), currently under construction are expected on the market towards the end of 2023 or 2024.

Industrial activity is expected to remain stable in 2023 supported by the anticipated economic recovery and government initiatives to boost industrialisation.

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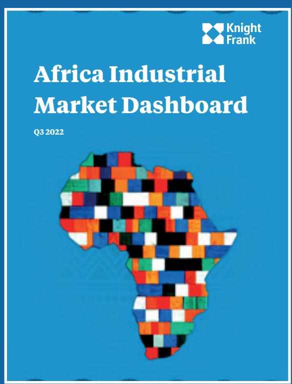

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