

RESEARCH



# UGANDA MARKET UPDATE

H1 2016

ECONOMIC UPDATE

SECTOR BY SECTOR  
ANALYSIS

H2 2016 OUTLOOK

# UGANDA MARKET UPDATE H1 2016

## Economic Update

Uganda's economy continued to grow in the current financial year albeit at a slower pace of 4.6% compared to a 5% growth that was recorded in the financial year 2014/15.

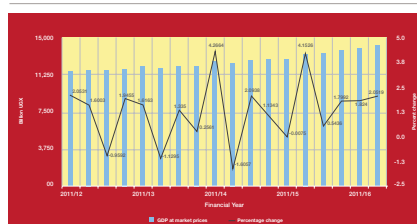
The decline in real GDP growth is attributed to volatilities experienced by the economy, which in turn affected various economic activities leading to low foreign direct investments in the country.

These volatilities include strengthening of the United States dollar that affected the Ugandan shilling, leading to depreciation pressure which subsequently fed into increased domestic prices, restricted lending as a result of high commercial bank lending rates (in response to inflationary pressures that had a negative impact on private demand and investment) as well as negative speculation and uncertainty in the run-up to the 2016 general elections which affected investment decisions.

Data from Uganda Bureau of Statistics revealed that in real terms, the size of the economy has grown by approximately UGX 2.5 trillion from UGX 53.2 trillion last financial year to UGX 55.7 trillion in the current financial year. Drivers of growth include strong performance of the services sector which grew by 6.6 % from 4.5% recorded last financial year.

The main contributors to this sector's growth were transport and storage as well as accommodation and food services sub sectors that grew to 7.7% and 6.9% from 6.2% and -0.1% respectively. The construction sector grew from 2.5% to 5.7%. Despite a slow-down in growth for FY 2015/16, this represents a credible performance which is significantly higher than the 3.2% and 3.4% growth projected for the world and Sub-Saharan Africa economies respectively in 2016.

Figure 1.0  
QGDP at Constant 2009/10 Prices As Well as the Percentage Change in QGDP Estimates.



Source: Uganda Bureau Of Statistics (UBOS)  
QGDP = Quarterly Gross Domestic Product

### Exchange rate

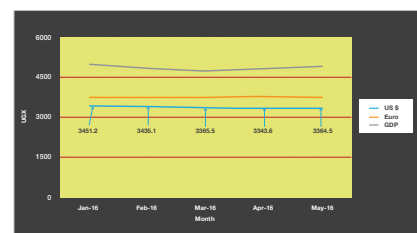
The Ugandan shilling depreciated against the US dollar by 2.6% to an average of UGX 3,451.2 to the \$1.00USD in January 2016 from an average of UGX 3,362.5 to 1:00 USD in December 2015. The Shilling depreciated in January mainly due to a rise in demand for the US dollar as businesses resumed in earnest after the December 2015 Christmas break, and speculation on the outcome of the general elections in February 2016.

The shilling appreciated by 0.5% to an average of UGX 3,435.1 to \$1.00 USD in February owing to sluggish demand for the dollar characterised by low import activity as well as the fact that the election period caused economic uncertainty with companies cutting back on travel as well as tourists staying away due to travel advisories.

Overall, the shilling has been stable against the US dollar due to tightening of the monetary policy by the Central Bank which in turn constrained domestic demand and consequently has impacted on demand for foreign exchange for imports.

As of June 6<sup>th</sup>, 2016, the shilling had appreciated by 2.4% to an average of 3370 per USD from an average of UGX 3,451.2 per USD at the end of January 2016.

Figure 2  
Trends in the Monthly Average Exchange Rates for the Period January-May, 2016.



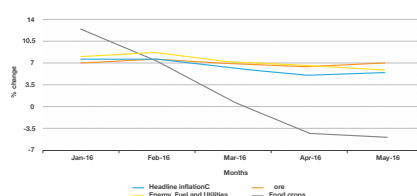
Source: Bank Of Uganda and Uganda Revenue Authority

### Inflation

Annual Headline inflation during the first half of 2016 remained within single digits, although slightly above the 5% policy target due to fluctuating food and fuel prices. The downward risk on inflation still remains the uncertainty of food prices which are heavily influenced by natural conditions such as heavy rains and drought.

Annual headline inflation for the year ending May 2016 increased for the first time since the start of the calendar year 2016 to 5.4 percent from 5.1% recorded in April 2016. This increment was largely on account of an increase in Annual Core Inflation due to a rise in other goods Inflation of 7.4% for the year ending May 2016 compared to the 6.7% increase recorded during the year ended April 2016.

Figure 3  
Uganda Headline and Annual inflation rates for 3 major components, Jan-May, (2009/10=100)



Source: Uganda Bureau Of Statistics

### Inflation across the East African Region

Annual headline inflation remained with in single digit figures across all countries in the East African region.

Table 1  
Annual Headline Inflation Rates for Selected EAC Countries.

	Jan-16	Feb-16	Mar-16	Apr-16	May-16
Uganda	7.70	7.70	6.20	5.10	5.4
Kenya	7.78	6.84	6.45	5.27	5.0
Tanzania	6.50	5.60	5.40	5.10	5.2
Rwanda	4.50	4.40	4.63	4.70	4.6
Burundi	4.30	6.70	4.30	2.6	2.7

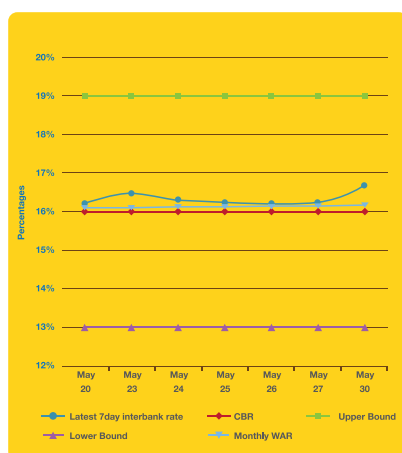
Source: Respective National Statistics Bureaus

## Interest Rates

Bank of Uganda maintained the Central Bank Rate (CBR) at 17% during Q1 of 2016, given the inflationary forecast and accompanying risks. In April 2016, Bank of Uganda reduced the CBR to 16% and maintained this through to May as a result of the improvement in the inflationary outlook. The same rate was maintained for the month of May 2016.

The impact of the high CBR has also been reflected through higher domestic lending rates that fluctuated between 24% - 25%. Interest rates remained high but relatively stable, with short term (6 months) Treasury Bills at 16.08% and commercial bank lending rates at 24.29% during the first half of 2016.

Figure 4  
Central Bank (Lending) Rate and the Seven Day Interbank Rate as at June 1<sup>st</sup>, 2016



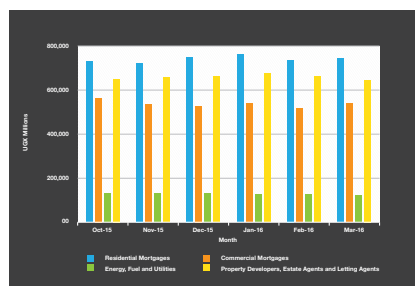
Source: Bank Of Uganda

## Private Sector Credit to the Real Estate Sector

Commercial Bank lending rates remained high, ranging from 18% - 24% on Uganda Shilling mortgages, which has slowed down private sector borrowing, and crowded out private investments.

This turn of events can neither shield the economy from shocks nor accelerate its rate of economic growth to higher levels of prosperity. It also stifles home ownership and property development.

Figure 5  
Commercial Banks Credit to the Mortgage, Land and Real Estate Sectors in million UGX



Source: Bank Of Uganda

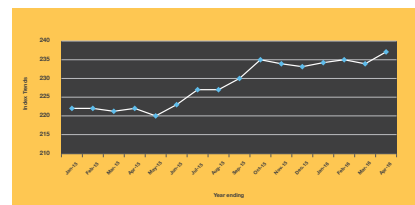
At the end of March 2016, the outstanding stock of Private Sector Credit (PSC) from commercial banks towards Real Estate activities amounted to UGX 2.6 trillion. This is a 0.5% increment compared to February 2016. This marginal growth is mainly attributed to a 1.65% increase in amounts borrowed for commercial mortgages. Majority of the lending from commercial banks is for home loans and property development.

## The Construction Sector

Annual changes reveal that the input prices for the whole construction sector that includes material prices, wage rates and equipment hire rates increased by 6.7 % in the year ending April 2016 compared to the year ended April 2015 as shown in Figure 6 below. This increase was attributed to a 16.4% rise in prices of inputs for residential buildings and a 6.8 % rise in input prices for non-residential buildings.

On the other hand, monthly changes in input prices for the whole construction sector showed that there was an increase of 1.3 % in April 2016 compared to a 0.2 % reduction in March 2016. The increase in April was due to increases in prices of cement, PVC pipes, burnt clay bricks, steel bars and wage rates.

Figure 6  
Trends of the whole construction sector index for the period Jan15 - Apr16



Source: Uganda Bureau Of Statistics

Despite a notable construction boom evidenced in the Ugandan economy since 2006, we envisage a negative impact on this sector during the second half of 2016 as a result of the proposed higher taxes on cement.

With an aim to boost revenue in FY 2016/17, Government of Uganda has proposed that excise duty charged on a 50 kilogram bag of cement is to be raised from UGX 500 (\$0.15) to UGX 1,000 (\$0.29), which could raise market prices, depress consumer demand and slow down the pace of private property development.

## Residential

We registered an increase in the number of properties which came onto our books for sale in Q1 & Q2 2016. These properties are mainly in the greater Kampala Metropolitan areas of Kira, Naalya, and Najjera which are becoming increasingly popular for middle income home owners.

Land tenure in these suburbs also tends to be "Private Mailo" which is considered an advantage for many home buyers who believe mailo tenure is in perpetuity, and is generally considered a "safer" tenure to have, as opposed to leasehold titles.

There has been a noticeable decline in sales activity in the high end residential sales market during Q1 & Q2 2016. Marketing periods for prime property are taking much longer to register interest from potential buyers, and there are few buyers with the capacity to close deals at asking prices. This has led to a downward correction in the market prices of approximately 10%– 15% being achieved in sales prices.



The reduction in sales activity was mainly due to uncertainty and speculation during the pre and post general election period. That said however, sales that have been concluded, were at discounted prices, as buyers take advantage of the ‘bearish’ market performance over the past 24 months.

There has been a noticeable increase in inquiries for commercial and residential investment properties to buy from both the local and expatriate community. This is a sign of recovering investor confidence as the perceived immediate threats or aftermath of the election violence are considered to have passed.

In addition, the period of March-May 2016 saw an increase in demand for short stay accommodation as opposed to the long leases. Over 80% of the inquiries received during this period were from clients who were looking to stay for a period of 2 – 4 months.

Table 2  
Prime residential rentals

Description	Rental Charge
5 bed furnished detached houses on 1.00 acre plots	\$4,000 - \$5,000
4 bed furnished detached houses on between 0.50 – 1.00acre plots.	\$3,000 - \$4,000
3 bed furnished town houses (in a gated community)	\$2,500 - \$3,000
3 bed serviced apartments	\$2,500 - \$3,000
2 bed serviced apartments	\$1,850 - \$2,500

Source: Knight Frank Uganda

## Office

The office sector has been the hardest hit of all the property sectors over the past 24 months, and saw prime rents falling to as low as \$12.00 per sq.m in some properties. The Kampala outer CBD locations of Kololo and Nakasero, and other prime suburban office locations of Naguru, Bugolobi, Nakawa and Bukoto have been the focal points of office development over the past 2 years, and this trend is likely to continue as key demand drivers of commercial office space look for premises out of the congested CBD area, where land prices are also considered extortionate.

During the first half of 2016, yields for office space remained stable ranging between 9% and 10% for prime offices (grade A) and 8% for grade B Offices.

Asking rentals were between USD 11– 15 per square metre per month while grade B offices fetched an average of between USD 8 - 10 per square metre per month. The average selling price per sq.m for prime office space was between USD 1,400 – 1,600 per sq.m.

Table 3  
Prime commercial rentals

Property Type	Yield	Rate per sq.m
Grade A	10%	\$15 – \$16.5
Grade B	8%	\$8 – \$10

Source: Knight Frank Uganda

Grade A buildings maintained an average occupancy rate of approximately 80% while Grade B buildings had lower occupancy levels averaging at 60% over the past 6 months. These occupancy rates are slightly higher than those recorded during the same period last year. Demand for Grade A space has continued to be driven by Government agencies, financial services sector, especially the insurance sector and credit finance companies that are growing and need more space as a result.

New office stock in prime secondary commercial locations of Bugolobi, Nakawa, Bukoto and Nakasero, have exerted downward pressure on core CBD office properties. The latter sector has not been performing well because most of the stock is old, with limited and expensive parking, and traffic congestion in these locations. Rents have stagnated, or in most cases, are being negotiated downwards.

As observed in the last quarter of 2015, the demand for smaller office spaces .i.e. (50–70 m<sup>2</sup>) by firms who do not need big space (i.e consultancy and logistics firms,) yet need proximity to their clients in the corporate sector, continued to gather momentum in the prime office locations of Nakasero, Kololo, Naguru and Bugolobi.

Approximately 20,000 m<sup>2</sup> of prime commercial (Grade A / AB and B) office space was leased during the first half of 2016. Most of this take up was derived from Government Ministries and Parastatals. We are of the opinion that the office sector will start to show

signs of tangible and actual recovery with demand from private sector tenants towards the end of 2016. However, take up is still slow, occupancy rates are still above the desired level, and renewed rents are below passing rents in current running leases.

The prime office pipeline is active with developments like Rume Towers along Lumumba Avenue, and Lotis Towers along Mackinnon Road, to name but a few. The impact of the recent change in the tax regime with regards to prices of construction inputs such as cement is likely to have some sort of impact on construction costs moving on.

We are hoping that once oil production and pipeline construction dates are certain, there will be increased demand for office accommodation from the oil and gas sector and related services which will reduce vacancy rates, and stabilise rentals somewhat.

## Retail

The retail sector has been rather subdued compared to the same period last year. We have witnessed a number of retail tenants (particularly in secondary locations) requesting to have their rents paid in local currency in order to curb the dollar fluctuations. Retail tenants have also generally registered slow sales during the first quarter of 2016 compared to the same period last year.

In addition, retailers are putting pressure on the property owners to give them capped rentals to enable them forecast actual sales with a degree of certainty. This is obviously not ideal for landlords whose financial obligations are in foreign currency (US\$).

However the ministry of Finance issued a directive on the 15<sup>th</sup> January 2016 warning accounting officers against awarding government contracts in foreign currencies, in a bid to help stabilize the Shilling against the dollar. This will result in more predictable prices on contracts instead of the price changes that occur with the dollar fluctuations.

Eventually, landlords will have to take a stand on this matter, although it may

be beyond their control since their development finance is in US dollars.

On the contrary however, the banking sector which is usually a big demand driver for retail units, has witnessed slow activity in the first half of 2016. Banks expansion efforts have been slow, concentrating more on growing their ATM outlets. Banks are also leaning towards having the existing branches operating out of standalone units and instead having their ATMs in the shopping centres. Likewise, branches are also being opened and maintained in the shopping centres, for example Standard Chartered Bank who opened a wholly automated branch on 12th February 2016 with special features like the Cash Deposit Machine (CDM).

Table 4  
Prime retail rentals

Description	Rental Charge
<10m <sup>2</sup>	\$180
<50m <sup>2</sup>	\$35
<100m <sup>2</sup>	\$25
<500m <sup>2</sup>	\$22.5
>500m <sup>2</sup>	\$18.5
Anchors	\$9

Source: Knight Frank Uganda

The 18<sup>th</sup> February presidential and parliamentary elections had a minimal impact on the retail sector. Overall, there was an average decline of 1% in the footfall to malls managed by Knight Frank Uganda from January to February 2016. This is attributed to the post and pre-election negative speculation that was experienced before and after the elections. The average daily traffic reduced by 2.1%, compared to Q2 and Q1 2016 figures due to the fact that Easter fell in the month March which accounts for the higher traffic instead of April as is usually the case.

The retail sector will continue to we realise more line shops expanding their business alongside the emergence of startups especially in the fashion industry. There are also a number of retail developments being built in and around the city suburbs. The Arena Mall, Nsambya is expected to break ground in the second half of 2016. East Africa's leading retailer Nakumatt

has expansion plans to penetrate the Ntinda market in the second half of 2016, the branch located at Ntinda Complex expected to be opened is targeting the catchment area of Ntinda, and secondary catchment areas of Kiwatule, Nakawa, Bukoto, Kisasi and Naalya.

Sportswear Company Adidas commenced fit-outs at the end of April at Acacia mall with a target opening date in Q3 of 2016. The fact that one of the world's biggest manufacturers, retailers and brands, Adidas is set to open a store in Kampala shows the confidence that the international brands have developed in our market which will be a catalyst in boosting the confidence of other affiliate brands to venture into the East African and Ugandan market.

And last but not least, Pizza Hut, a Multinational fast-food chain store officially opened in Uganda at Village mall in Bugolobi on May 23<sup>rd</sup>, 2016. The Imperial Mall in Entebbe is also set to open for business in the second half of the year.

## Industrial

Industrial rental property in the traditional industrial areas (1<sup>st</sup> – 8<sup>th</sup> Street) and secondary industrial locations on the outskirts of the CBD like Banda, Ntinda, Nakawa and Kyambogo have also experienced low occupancy rates and take up over the past 6 months. This is partly attributed to supply of warehousing space outstripping demand, and a slowdown in the trading of imported goods and commodities which would require storage space for distribution to neighbouring countries.

We are noticing increasing demand for relatively large warehousing space of late, although decision making process and lead time up to occupation is taking a few months. This demand is being derived from the logistics, transportation, and pharmaceuticals sectors. Development of factories and industrial premises by owner occupiers continues in earnest at the KIBP Namamve, and some of the notable companies who have recently completed their factories and taken occupation are Quality

chemicals Ltd, Roofings (U) Ltd, Hima Cement, Export Trading, Sadolin Paints, and Kyagalanyi Coffee Ltd, to mention but a few. Prime industrial rental rates have stagnated at an average of \$5.00 - \$7.00 per square metre for properties in the core / traditional industrial areas, and \$5.00 - \$6.50 per square metre for newer, more modern warehousing premises in secondary industrial locations of Nakawa, Ntinda, Luzira, Namamve, Banda, and Seeta.

## Valuations

Overall, the Bank lending rates remained high but stable (an average rate of 24.5%) during the first half of 2016. There was a decline in bank lending activity for the first half of the year. However, there is a noticeable increase in valuation instructions and bank lending activity over the past 2 months, albeit for revaluation, as opposed to new loans. There is a correlation between house purchase activity, and volume of valuation instructions / bank lending activity, since most buyers in the market are mortgage purchasers. Prime Property values have corrected in line with comparable prices being achieved on the market, but middle income property values continue to realise capital appreciation of between 2% - 5% per annum or at the very least held their values. Again, this mirrors the increased interest and demand for middle income housing over the first half of the year.

That said, we are also noticing an increase in properties which are being auctioned or repossessed by various lending institutions as a result of "bad" loans. Our research also indicates that prices being achieved for this category of property whereby sales are restricted, and falling far below the expected "restricted" realisation prices.

One of the biggest deterrents of home ownership for mortgage buyers who are the majority of purchasers in Uganda, is unaffordable bank lending rates (22% - 25%). This is also partly the reason why loan repayments are not being met and property repossessions are increasing. Especially where interest rates are not fixed.

## Outlook for Q3 and Q4 of 2016

It is strongly believed that the passing of the amended financial bill that allows banks to engage in agency banking, Islamic banking and bank assurance will be a catalyst for increased economic activity over the next half of the year, through increased access to financing for trade and investment. This initiative is targeted at encouraging or onboarding the unbanked population (only 5 million Ugandans have bank accounts out of 14 million) in addition to providing a unique financial product which is unique to this market.

The supply / demand disequilibrium for middle income and affordable housing remains high, as supply in the prime residential segment runs the risk of becoming saturated with limited demand to match in the short to mid-term. Likewise, this will have downward pressure on prime residential rentals and increased voids.

The local currency remains highly depreciated by stable, and the slight reduction in fuel prices should have downward effect on food prices, but encourage discretionary retail spending. The Central Bank projected that both headline and core inflation would remain in the range of 6.5±% in the period of April - June 2016 before gradually declining to the medium-term target of 5% in the second half of 2017.

However, the property market sentiment remains bearish, with Bank of Uganda revealing that the economy

may deteriorate over the next 12 months due to slowdown in emerging market economies especially due to China's economic slowdown, which has hurt commodity-exporting countries by driving down demand for exports. Consequently, Uganda's balance of payments in the short to medium-term will remain vulnerable to the turbulences in the global economic environment.

The property market is expected to pick up, but with caution since interest rates remain high, the shilling remains weak, and demand for both prime office and residential accommodation is still lagging behind supply. There are various affordable / middle income housing development schemes and satellite towns in the offing, and we believe this will address and alleviate the housing deficit if the right product is built priced correctly.

Furthermore, we also envisage a decline in new investments in the construction sector during the second half of 2016 as a result of the proposed higher taxes on cement. With an aim to boost revenue in FY 2016/17, government of Uganda has proposed that excise duty charged on a 50 kg bag of cement is to be raised from UGX 500 (\$0.15) to UGX 1000 (\$0.29), which could raise market prices, depress consumer demand and discourage new investments.



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The period "HALF 2016" refers to the calendar period 1st January to 30th June 2016 | Q1 refers to 1st January – 31st March and Q2 refers to 1st April – 30th June 2016.