Cytonn Monthly – August 2017, & Nairobi Metropolitan Area Residential Report 2017

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Executive Summary

Fixed Income and Macroeconomic Review: During the month of August, the yield on the 91-day paper declined to 8.1% from 8.2% at the end of July, whereas yields on the 182 and 364-day papers remained unchanged at 10.3% and 10.9%, respectively. Kenya's inflation rate for the month of August rose to 8.0% from 7.5% in July, primarily driven by a rise in food prices as there was limited food supply to Nairobi and other urban centres;

Equities: During the month of August, the equities market was on an upward trend, with NSE 20, NASI and NSE 25 gaining 6.0%, 4.8% and 3.8%, respectively, taking their YTD performance as at the end of August to 26.9%, 26.4% and 25.6% for NASI, NSE 20 and NSE 25, respectively. The financial services sector (Banks and Insurance companies) have released their H1'2017 results, with the listed banking sector recording a 10.0% decline in the average core earnings per share, compared to the average growth of 13.3% registered for H1'2016, while the listed insurance sector recorded an average decline of 12.5% in core earnings per share, from an average growth of 69.4% in H1'2016;

Private Equity: During the month of August, we witnessed investments in major sectors including financial services, manufacturing, and the energy sector, with the highlight transaction being the completion of the acquisition of a 90.0% stake in Kenyan paint and coating manufacturer, Sadolin Group, by Kansai Plascon Africa Limited, a subsidiary of Japanese paint maker Kansai Paint Co. Ltd;

Real Estate: There was reduced activity witnessed in the real estate sector as a result of a tough economic environment, occasioned by the electioneering period and low credit supply due to the enactment of the Banking Amendment Act 2015, as the value of buildings approved declined by 16.3% from Kshs 126.3 bn in 2016 to Kshs 105.7 bn in 2017, with the number of mortgages in the country declining by 1.5% from 24,485 mortgages in 2015 to 24,085 mortgages in 2016;

Focus of the Week: In an update to our Nairobi Mortgage and Rental Affordability Report - 2016, we conducted research on 35 sub-markets in the Nairobi Metropolitan area to determine the investment opportunity for residential developments in 2017. This report shows the performance of both apartments and detached units in the 35 sub-markets, and the full report can be accessed here - Nairobi Metropolitan Area Residential Report 2017;

Company Updates

- On Saturday, September 23rd, 2017 we shall host the Cytonn Investments Golf Competition at Muthaiga Golf Club. If interested in playing, email clientservices@cytonn.com. Priority will be given to our clients.
- This week, our Investments Analyst, John Ndua, discussed the subdued performance of Standard Chartered Bank Kenya and Deacons in the first half of 2017, following a challenging operating environment. Watch John Ndua on CNBC here
- Cytonn Investments released H1'2017 financials, posting a 140.4% increase in revenue to Kshs 638.8 mn, from Kshs 265.8 mn in June 2016, with Group profit rising by 415.8% to Kshs 299.2 mn, from Kshs 58.0 mn over the same period. Investment in our deal pipeline, worth Kshs 82.0 bn recorded gains of Kshs 430.3 mn over the first half of the year, coupled with revenue growth of 140.4%, highlights the attractive investment opportunity in real estate and the financial services sector in Kenya, and the region at large. For more information and details, see the press release here and the financials here
- The corporate scene has witnessed heightened oversight through regulations seeking better governance for both public and private institutions. On Monday, August 28th 2017, Cytonn

Investments hosted the Cytonn Corporate Governance Workshop, in a bid to get the market participants to provide additional input and critique the methodology applied in the Cytonn Corporate Governance Report, and build an industry wide initiative to strengthen corporate governance. The event was attended by key governance brands and organs such as the Institute of Certified Public Accountants of Kenya (ICPAK), the Institute of Directors (IOD-K), the Institute of Internal Auditors (IIA), the Centre for Corporate Governance (CCG) and the Office of the Auditor General. See event note

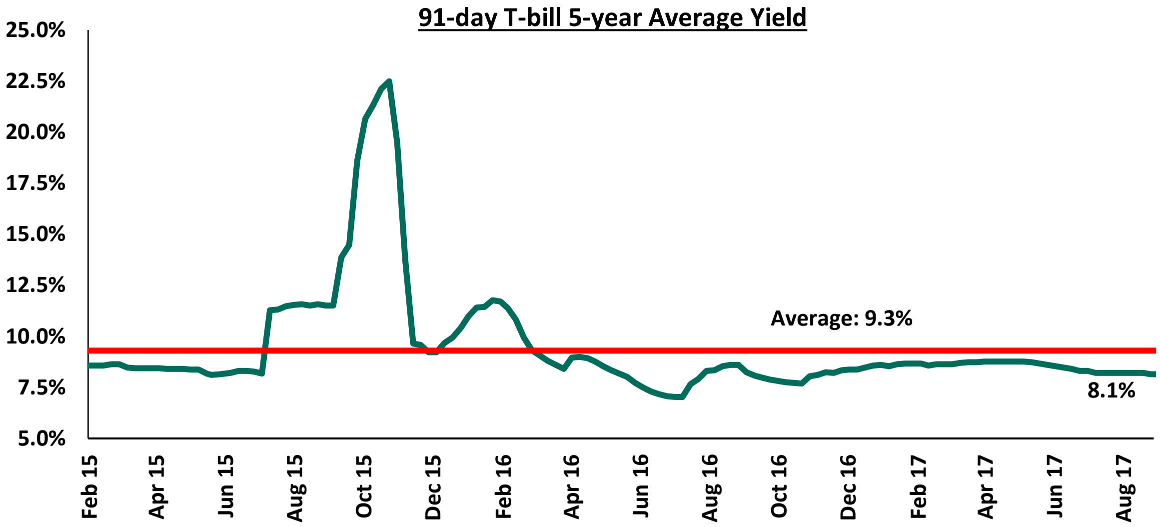
- We continue to showcase real estate developments by our real estate development affiliate, Cytonn Real Estate, through weekly site visits. Watch progress videos and pictures on The Alma, Amara, The Ridge and Taraji Heights. The site visits target both investors looking to invest in real estate directly, and also those interested in high yield investment products to familiarize themselves with how we support the high yield returns. To deliver high yield returns, our cost of capital is priced off the loan markets where all-in pricing ranges from 16.0% to 21.0% and our yield on real estate developments ranges from 23.0% to 25.0%, hence our top-line gross spread is about 6%. If interested in attending the site visits, kindly register here
- We continue to see very strong interest in our Private Wealth Management training, which is at no cost, and is held bi-weekly, but is open only to pre-screened participants. The training can also be offered to institutions that would like their employees trained on Financial Planning. To get further details contact our Client Services team at clientservices@cytonn.com
- For recent news about the company, see our news section here
- We have 10 investment-ready projects, offering attractive development and buyer targeted returns of around 23.0% to 25.0% p.a. See further details here: Summary of investment-ready projects
- To invest in any of our current or upcoming real estate projects, please visit Cytonn Real Estate
    - The Alma, which is over 55.0% sold, has delivered an annualized return of 55.0% p.a. for investors who bought off-plan. See The Alma
    - Amara Ridge is currently 100.0% sold and has delivered over 20.0% p.a. returns to investors. See Amara Ridge
    - Situ Village is currently 15.0% sold. See Situ Village
    - The Ridge (Phase One) is currently 31.0% sold. See The Ridge
    - Taraji Heights is currently 10.0% sold. See Taraji Heights
    - RiverRun Estates (Phase One) is currently 8.7% sold after the recent launch. See RiverRun Estates
- We continue to beef up the team with ongoing hires: Careers at Cytonn

Fixed Income and Macroeconomic Review

T-bills subscription rates improved during the month of August, as subscription rates rose to an average of 113.3%, compared to 63.8% experienced in July due to improved liquidity in the market. The subscription rates for the 91, 182 and 364-day papers came in at 74.5%, 122.3% and 119.7% from 59.9%, 76.5% and 52.6% the previous month, respectively. The yield on the 91-day paper decreased to 8.1% from 8.2% in July, whereas yields on the 182 and 364-day papers remained unchanged at 10.3% and 10.9%, respectively. The Central Bank of Kenya (CBK) remained disciplined in stabilizing interest rates in the auction market by rejecting aggressive bids that were priced above market, and the market responded, leading to a rise in the overall bids acceptance rate for T-bills to 95.9% during the month, compared to 87.4% in July, with the government accepting Kshs 104.3 bn of the Kshs 108.7 bn worth of bids received, against the Kshs 120.0 bn on offer, indicating bids are largely within ranges CBK deems acceptable.

For this week, T-bills were oversubscribed, with the overall subscription rate rising to 136.1% from 94.7% recorded the previous week. The subscription rates for the 91, 182 and 364-day papers came in at 69.3%, 145.4%, and 153.4% compared to 105.0%, 59.8% and 125.3%, respectively, the previous week. Yields on the 91, 182 and 364-day papers remained unchanged from the previous week at 8.1%, 10.3% and 10.9%, respectively. The overall acceptance rate came in at 91.1% compared to 98.0% the previous week, with the government accepting a total of Kshs 29.7 bn of the Kshs 32.7 bn worth of bids received, against the Kshs 24.0 bn on offer in this auction.

The 91-day T-bill is currently trading below its 5-year average of 9.3%. The lower yield on the 91-day paper is mainly attributed to the low interest rates environment we have been experiencing, and we expect this to continue in the short-term, given (i) the government is expected to meet its domestic borrowing target for the 2017/18 fiscal year, as reduced credit to the private sector will see institutions channel funds more actively towards government securities, and (ii) the government is expected to meet its foreign borrowing target in the 2017/18 fiscal year, which was set downwards to Kshs 206.0 bn from Kshs 462.3 bn in the previous financial year.



During the month, the Kenyan Government issued a new 5-year bond (FXD 1/2017/5), with a market determined coupon, and re-opened a 10-year fixed-coupon bond (FXD 1/2017/10) with an effective tenor to maturity of 9.9 years and a coupon rate of 13.0%, in a bid to raise Kshs 30.0 bn for budgetary support. The bonds were undersubscribed, with the overall subscription rate at 88.9%, with Kshs 26.7 bn worth of bids received compared to Kshs 30.0 bn on offer. The average market bid rates came in at 12.5% and 13.2%, while the average yields of the accepted bids came in at 12.5% and 13.1%, for the 5-year and 10-year bonds, respectively. The acceptance rate for the bids received came in at 66.0%, which was higher than the average acceptance rate from previous auctions during the year which averages at 59.5%, with the government accepting Kshs 17.6 bn out of the Kshs 26.7 bn worth of bids received. The government consequently issued a tap sale for the new 5-year bond (FXD 1/2017/5) at the accepted weighted average yield of 12.5% to raise Kshs 13.0 bn, with the government managing to collect the full Kshs 13.0 bn.

During the month, the average interbank rate closed at 5.5%, compared to 7.2% at the end of July, due to better distribution of liquidity in the market, with liquidity having previously been skewed towards larger banks. There was a net liquidity injection of Kshs 24.9 bn in the money market, compared to the net liquidity injection of Kshs 61.8 bn experienced in July, with the bulk of it coming from Government Payments at Kshs 111.5 bn, and T-bill Redemptions of Kshs 108.7 bn.

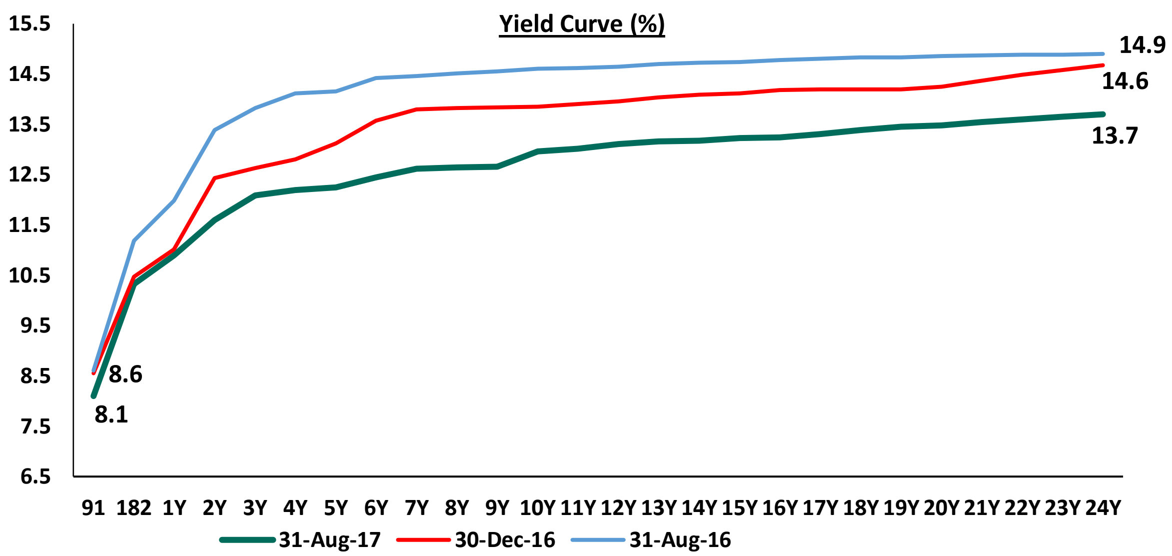
Below is a summary of the money market activity during the month:

all values in Kshs bn, unless stated otherwise

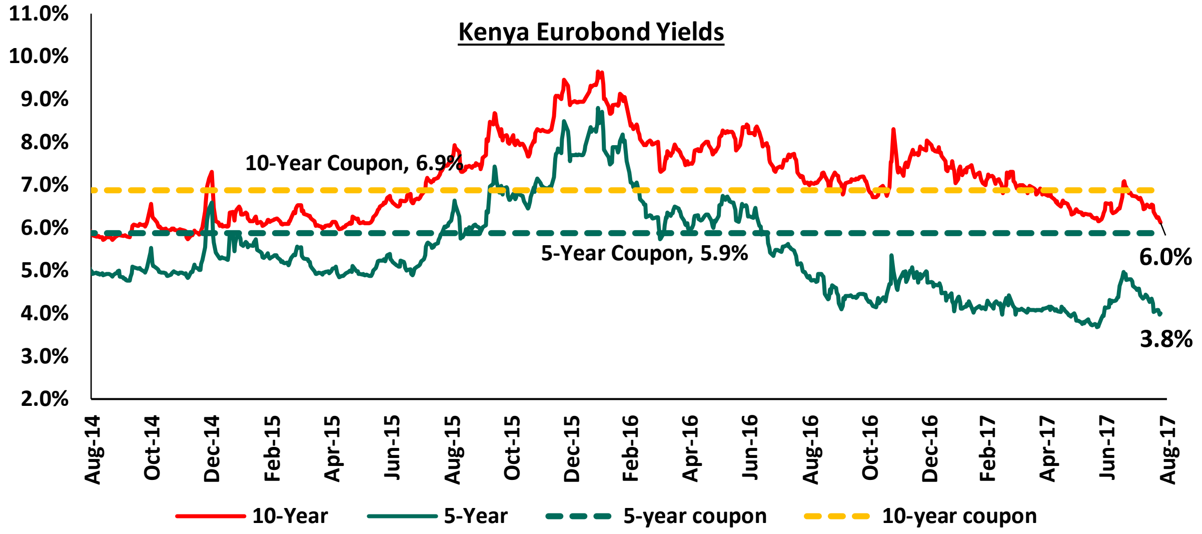
Monthly Liquidity Position – Kenya			
Liquidity Injection		**Liquidity Reduction**	
Term Auction Deposit Maturities	37.2	T-bond sales	17.6
Government Payments	111.5	Transfer from Banks - Taxes	96.4
T-bond Redemptions	5.6	T-bill (Primary issues)	83.8

T-bill Redemption	108.7	Term Auction Deposit	37.2
T-bond Interest	8.3	Reverse Repo Maturities	39.7
T-bill Re-discounts	0.2	OMO Tap Sales	7.0
Repos Maturities	5.0		
Reverse Repo Purchases	30.1		
Total Liquidity Injection	**306.6**	**Total Liquidity Withdrawal**	**281.7**
		Net Liquidity Injection	**24.9**

The yields on government securities have declined since the beginning of the year, as highlighted in the yield curve below. According to the FTSE NSE Bond Index, Treasury bonds listed at the Nairobi Securities Exchange (NSE) gained 1.1% during the month.

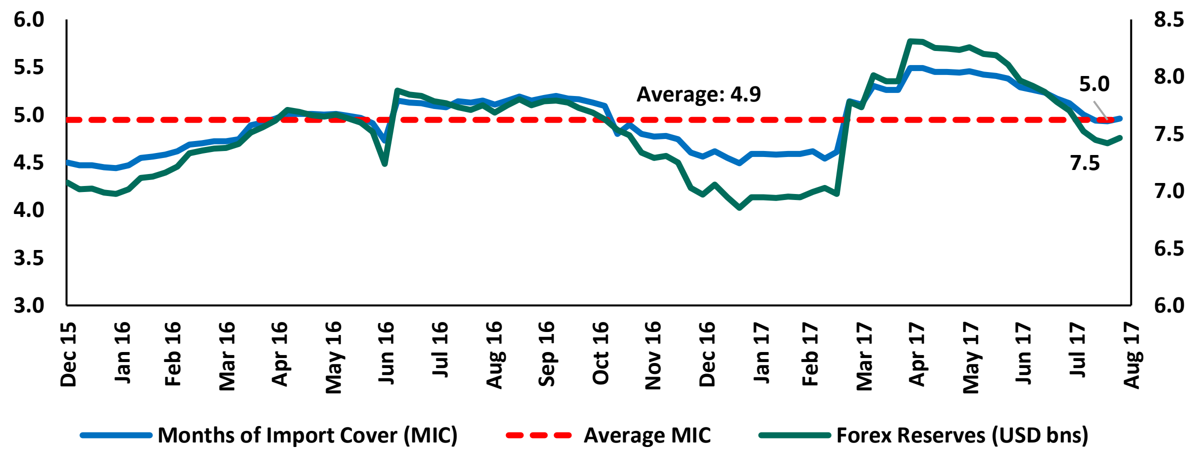


According to Bloomberg, yields on the 5-year and 10-year Eurobonds, with 1.6-years and 6.9-years to maturity, declined by 60 bps and 50 bps, to close at 3.8% and 6.0% from 4.4% and 6.5%, respectively, at the end of July. Since the mid-January 2016 peak, yields on the Kenya Eurobonds have declined by 5.0% points and 3.7% points for the 5-year and 10-year Eurobonds, respectively, due to stable macroeconomic conditions in the country. The declining Eurobond yields and stable rating (Fitch Ratings having affirmed Kenya's long-term foreign and local currency issuer default ratings (IDRs) at "B+"), are indications that Kenya's macro-economic environment remains stable and hence an attractive investment destination.



The Kenya Shilling appreciated by 1.0% to the USD during the month of August to close at Kshs 102.9, from Kshs 103.9 in July. The strengthening of the shilling during the month was primarily driven by dollar inflows from investors abroad into the local debt and equity markets, amid cheap market valuations and a relatively stable business environment, brought about by a non-violent election. On a year to date basis, the shilling has depreciated against the dollar by 0.4%, while according to the International Monetary Fund (IMF), the dollar is overvalued by between 10.0% and 20.0%, based on near-term economic fundamentals. In our view, the shilling should remain relatively stable to the dollar in the short term, supported by CBK's activity as they have sufficient support through forex reserves, currently at USD 7.5 bn (equivalent to 5.0 months of import cover), but we have seen forex reserves decline significantly from USD 8.3 bn at the peak in April this year, but not to a worrying level, as import cover is still at 5.0 months.

Kenya Months of Import Cover and Forex Reserves



The inflation rate for the month of August rose by 0.5% points to 8.0%, from 7.5% in July. The increase was primarily driven by (i) a rise in food prices, which rose by 1.0% m/m, due to limited food supply to Nairobi and other urban centres in the month, and (ii) a rise of 0.5% m/m in housing, water, electricity, gas and other fuels, brought about by increased cost of electricity and kerosene, that increased 24.1% and 1.5% y/y, respectively. See below a summary on key changes on the Consumer Price Index (CPI) in August;

Key Changes on the Consumer Price Index (CPI) during the month of August			
Broad Commodity Group	Price change m/m	Price change y/y	Reason

Food & Non-Alcoholic Beverages	1.0%	13.6%	Rise in food prices, attributable to limited food supply in Nairobi and other urban centers in the month, following depressed rainfall witnessed during the long rains period
Housing, Water, Electricity, Gas and other Fuels	0.5%	3.5%	Increased cost of electricity and kerosene, due to a rise in the pump prices of fuel

Going forward, we expect reduced inflationary pressures, supported by (i) stabilization in food prices, with improved weather conditions in some parts of the country, and (ii) a decline in fuel prices, as a result of rising US oil production, which has suppressed the global recovery of oil prices, countering OPECs decision to extend the deal to cut down on oil production. However, we expect inflation to average 8.0% over the course of the year, which is above the upper bound of the government target range of 2.5% - 7.5%.

The country held its general election this month, which was relatively peaceful, and within expectation, as highlighted in our focus note on the Post-Election Business Environment. This week, the Supreme Court nullified President Uhuru Kenyatta's re-election, a first not just for Kenya but also for Africa, ordering a fresh presidential poll, due to irregularities in the way the Independent and Electoral Boundaries Commission (IEBC) carried out the general election. Following the annulment, we expect businesses to go about their normal activities with caution and thus subdued activity is expected over the coming few weeks. Despite this, we expect the market to normalise once the country takes to the polls, the election is concluded, and fears and uncertainty dissipates, with the Kenya growth fundamentals remaining strong and intact.

Fixed Income Conclusion:

Rates in the fixed income market have remained stable, and we expect this to continue in the short-term. However, a budget deficit that is likely to result from depressed revenue collection creates uncertainty in the interest rates environment as any additional borrowing in the domestic market to plug the deficit could lead to upward pressures on interest rates. Our view is that investors should be biased towards short-to medium term fixed income instruments to reduce duration risk.

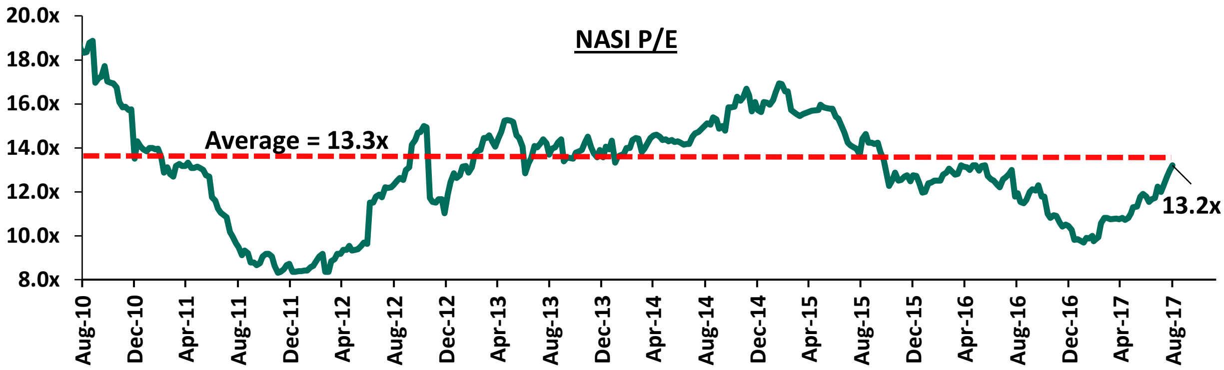
Equities

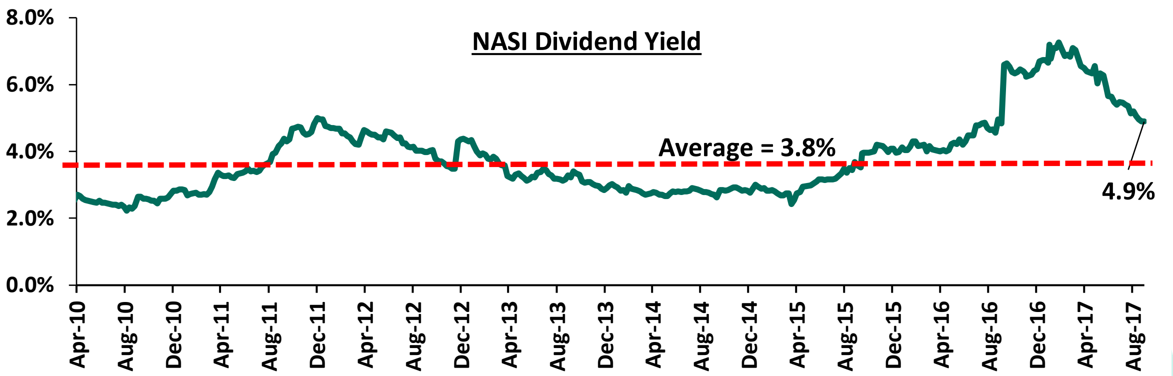
During the month of August, the equities market was on an upward trend with NSE 20, NASI and NSE 25 gaining 6.0%, 4.8% and 3.8%, respectively, taking their YTD performance as at the end of August to 26.9%, 26.4% and 25.6% for NASI, NSE 20 and NSE 25, respectively. For this week, the equities market was on a downward trend with NASI, NSE 25 and NSE 20 losing 5.5%, 4.6% and 4.5%, respectively, taking their YTD performance to 22.2%, 22.6% and 22.0%, respectively. The downward trend is attributed to uncertainty due to nullification of the presidential results resulting to losses by stocks on Friday with NASI, NSE 20 and NSE 25 losing 3.6%, 3.4% and 2.4%, respectively. The equities market performance during the month was driven by gains in large caps, led by KCB Group, Coop Bank and Equity Group, which gained 10.4%, 8.9% and 7.4%, respectively. Since the February 2015 peak, the market has lost 4.7% and 26.8% for NASI and NSE 20, respectively.

Equities turnover declined by 17.1% during the month to USD 170.1 mn from USD 205.0 mn in July 2017, taking the YTD turnover to USD 1,166.8 mn. Foreign investors remained net sellers for this month with net outflows of USD 35.7 mn, compared to net outflows of USD 19.7 mn witnessed in July 2017. YTD, foreign investors are net sellers with net outflows of USD 60.4 mn. We expect the market to record subdued activity over the coming few weeks with reduced volumes as market players are cautious of the renewed uncertainty. Despite this, we expect the market to remain supported by improved investor sentiment once the country takes to the polls for the presidential elections within 60-days, and fears and uncertainty dissipates, and as investors take advantage of the attractive stock valuations. For a comprehensive analysis on the impact of the election ruling on the business environment, see the Note.

The market is currently trading at a price to earnings (PE) ratio of 13.2x, versus a historical average of 13.3x, with a dividend yield of 4.9% versus a historical average of 3.8%. The current 13.2x valuation is 36.1% above the most recent trough valuation of 9.7x experienced in the first week of February of 2017, and 58.8%

above the previous trough valuation of 8.3x experienced in December of 2011. The charts below indicate the historical P/E and dividend yields of the market.





According to the Capital Markets Soundness Report for the second quarter of 2017 by the Capital Markets Authority (CMA), CMA is in the process of developing a framework to ensure that all private offer transactions are made known to the authority. As highlighted in our Cytonn Weekly #32/2017, this implies that companies seeking to raise cash through sale of shares or short-term debt through private placements will be required to notify the regulator. CMA indicated in the report that the level of activity from private offerings market has been limited despite its significant potential for funding cash-strapped firms. This framework will see CMA enforce provisions in Section 30c of the Act, which require that the Authority is notified through information notices by issuers raising funds through private offers. As such CMA will be able to track the level of activity in the private space, and monitor trends driving the market. In our view, the impact of this framework will only be clear with time. As highlighted in our Cytonn Weekly #28/2017, the Capital Markets Authority (CMA) has done a fantastic job spearheading the introduction of new products such as Global Depositary Receipts and Global Depositary Notes thus providing faster and more convenient link to the market hence enabling market participants to exercise freedom of choice, which will in turn increase turnover. The market would also like to see more emphasis in expanding existing products.

During the month, we had a number of earnings releases and detailed below are the earnings' releases for this past week:

I&M Holdings released H1'2017 results

I&M Holdings released H1'2017 results, recording a 16.8% decline in core earnings per share to Kshs 7.9 from Kshs 9.5 in H1'2016, attributed to an 18.3% increase in operating expenses from H1'2016 with the operating income remaining flat. Key highlights for the performance from H1'2016 to H1'2017 include:

- Total operating income remained flat at Kshs 9.6 bn from H1'2016, despite a growth of 12.3% in Non-Funded Income (NFI), which was offset by a decline of 4.4% in the Net Interest Income (NII),
- NII dropped by 4.4% to Kshs 6.8 bn from Kshs 7.1 bn in H1'2016, following a 6.2% decline in interest income to Kshs 11.1 bn from Kshs 11.8 bn on account of the interest rate cap, despite a 9.0%

decline in interest expense to Kshs 4.2 bn from Kshs 4.6 bn in H1’2016. The Net Interest Margin (NIM) maintained at 7.7% same as in H1’2016,

- NFI improved by 12.3% to Kshs 2.7 bn from Kshs 2.4 bn in H1’2016, attributed to a 16.7% rise in fees and commissions on loans and advances to Kshs 1.4 bn from Kshs 1.2 bn in H1’2016. The current revenue mix shifted to 72:28 from 75:25 funded to non-funded income,
- Total operating expenses increased by 21.1% to Kshs 4.8 bn, from Kshs 4.0 bn in H1’2016, which was driven by an increase of 34.2% in loan loss provision (LLP) to Kshs 1.0 bn from Kshs 0.7 bn in H1’2016, and an 11.4% growth in staff costs to Kshs 1.9 bn from Kshs 1.7 bn in H1’2016,
- Cost to income ratio worsened to 50.7% from 41.7% in H1’2016. Without LLP, cost to income ratio stood at 40.6% from 34.2% in H1’2016,
- Profit before tax declined by 14.8% to Kshs 5.0 bn from Kshs 5.8 bn in H1’2016, while profit after tax declined by 16.8% to Kshs 3.4 bn from Kshs 4.2 bn in H1’2016,
- The balance sheet recorded an expansion in H1’2017, with total assets increasing by 9.0% to Kshs 229.2 bn from Kshs 210.3 bn in H1’2016, driven by a rise of 9.1% in the loan book to Kshs 144.5 bn from Kshs 132.5 bn in H1'2016,
- Total liabilities increased by 6.4% to Kshs 184.9 bn from Kshs 173.8 bn in H1’2016, driven by a 10.3% growth in customer deposits, while shareholders’ funds increased by 22.6% to Kshs 41.9 bn, from Kshs 34.2 bn in H1’2016,
- Customer deposits grew by 10.3% to Kshs 161.5 bn from Kshs 146.4 bn in H1’2016. Consequently, the faster growth in deposits compared to loans resulted in the loan to deposit ratio (LDR) declining marginally to 89.5% from 90.0% in H1’2016,
- I&M Bank is currently sufficiently capitalized with a core capital to risk weighted assets ratio of 16.1%, 5.6% above the statutory requirement, with total capital to total risk weighted assets exceeding statutory requirement by 2.8% to close the period at 17.3%,
- The Board did not recommend payment of an interim dividend.

Going forward, we expect I&M Holdings growth to be propelled by;

a) Continued investment in the innovation and digitization of systems, processes and solutions in a bid enhance efficiency as well as to provide their customers with convenient access to products and solutions

b) Revenue diversification with new business lines such as the acquired Giro Bank and Burbidge Capital, which the bank will leverage on to spur growth

c) Expansion and increased growth in regional subsidiaries across Uganda, Tanzania, Mauritius and Rwanda

For a more comprehensive analysis, see our I&M Holdings H1’2017 Earnings Note.

Standard Chartered Bank Kenya released H1’2017 results

Standard Chartered Bank Kenya released H1’2017 results, recording a 34.4% decline in core earnings per share to Kshs 10.0 from Kshs 15.2 in H1’2016, driven by a 7.2% decline in operating income and a 20.7% increase in operating expenses. Key highlights for the performance from H1’2016 to H1’2017 include:

- Total operating income declined by 7.2% to Kshs 13.5 bn from Kshs 14.5 bn in H1’2016, attributed to an 8.1% and a 5.3% decline in Net Interest Income (NII) and Non-Funded Income (NFI), respectively,
- NII dropped by 8.1% to Kshs 9.2 bn from Kshs 10.0 bn in H1’2016, following a 2.3% decline in interest income to Kshs 12.7 bn from Kshs 13.0 bn, coupled with a 16.1% increase in interest expense to Kshs 3.6 bn from Kshs 3.1 bn in H1’2016 as a result of increased interest expense for their deposits, with the cost of funding remaining unchanged at 3.2% from last year due to the 17.6% growth in customer deposits. Standard Chartered Bank and DTB, which recorded a 2.7% increase, are the only two banks to have experienced an increase in interest expense. This resulted in the Net Interest Margin (NIM) declining to 8.4% from 9.5% in H1’2016.

- NFI declined by 5.3% to Kshs 4.3 bn from Kshs 4.5 bn in H1'2016, attributed to a 29.8% drop in fees and commissions on loans and advances to Kshs 0.08 bn from Kshs 0.12 bn in H1'2016. The current revenue mix shifted marginally to 68:32 from 69:31 funded to non-funded income,
- Total operating expenses increased by 20.7% to Kshs 8.5 bn, from Kshs 7.0 bn in H1'2016, which was driven by a 68.5% increase in loan loss provision (LLP) to Kshs 2.3 bn from Kshs 1.4 bn in H1'2016 and an 8.2% increase in staff costs to Kshs 3.3 bn from Kshs 3.1 bn in H1'16,
- Cost to income ratio worsened to 63.0% from 48.4% in H1'2016. Without LLP, cost to income ratio stood at 45.8% from 39.0% in H1'2016,
- Profit before tax declined by 33.4% to Kshs 5.0 bn from Kshs 7.5 bn, while profit after tax declined by 34.4% to Kshs 3.4 bn from Kshs 5.2 bn in H1'2016,
- The balance sheet recorded an expansion in H1'2017, with total assets increasing by 12.9% to Kshs 289.1 bn, from Kshs 255.9 bn in H1'2016, driven by a rise of 23.6% in the government securities despite a 1.1% decline in the loan book to Kshs 113.0 bn from Kshs 114.2 bn in H1'2016,
- Total liabilities increased by 15.6% to Kshs 245.5 bn from Kshs 212.4 bn in H1'2016, while shareholders' funds maintained at Kshs 43.6 bn, the same as in H1'2016,
- Customer deposits grew by 17.6% to Kshs 224.5 bn from Kshs 190.9 bn in H1'2016. Consequently, the faster growth in deposits compared to loans resulted in the loan to deposit ratio declining to 50.4% from 59.9% in H1'2016,
- Standard Chartered Bank Kenya is currently sufficiently capitalized with a core capital to risk weighted assets ratio of 16.7%, 6.2% above the statutory requirement, with total capital to total risk weighted assets exceeding statutory requirement by 5.6% to close the period at 20.1%,
- The Board of Directors approved the payment of an interim dividend of Kshs 4.5 per share, compared to Kshs 6.0 per share approved over the same period last year, with book closure on 21st September 2017 and payment to be made on or after 19th October 2017. The payment translates into a projected full year dividend of Kshs 15.0 and dividend yield of 6.5%, at the current price of Kshs 231.0 per share, as at 1st September 2017. The dividend payment represents an expected full year dividend pay-out of 72.9% in 2017, compared to 75.9% recorded in 2016.

Going forward, we expect Standard Chartered Bank Kenya will thrive on;

a) Continued investment in digital infrastructure through its Digital by Design strategy that aims to migrate over 80% of transactions to non-branch channels by 2020. This is expected to promote efficiency and enhance risk management. In 2016 the bank introduced a mobile app, a revamped online platform, fingerprint log-in technology, video banking and cash deposit machines all aimed at achieving its Digital by Design strategy target,
b) Growth in deposits via revamped mobile and online banking products, particularly targeting SME and retail business.

For a more comprehensive analysis, see our Standard Chartered Bank Kenya H1'2017 Earnings Note.

None of the listed banks, in their H1'2017 results, has recorded a growth in core earnings per share, with the average decline in core earnings across the listed banking sector at 10.0%. This is a significant decrease compared to the average growth of 13.3% registered for H1'2016. The sector has experienced slower loan growth, resulting to reduction in the Net Interest Margins given that in this half year, the full effect of the law capping interest rate was in effect. The loan book growth has declined to 5.0% compared to a growth of 6.6% in H1'2016. The interest rate cap was meant to improve lending to the consumer, but so far the cap has curtailed lending as evidenced by the declining private sector credit growth at 2.1% as at May 2017, which is an 8-year low. We shall be releasing the comprehensive banking sector report by 11th September, 2017.

Listed Banks H1'2017 Earnings and Growth Metrics												
Bank	Core EPS Growth		Deposit Growth		Loan Growth		Net Interest Margin		Loan to Deposit Ratio		Exposure to Government Securities	
	H1'2017	H1'2016	H1'2017	H1'2016	H1'2017	H1'2016	H1'2017	H1'2016	H1'2017	H1'2016	H1'2017	H1'2016

KCB Group	**(0.2%)**	11.2%	1.3%	(2.2%)	16.7%	8.4%	8.7%	8.1%	84.3%	73.2%	24.0%	21.1%
DTB Kenya	**(5.8%)**	11.3%	18.6%	24.7%	7.2%	10.2%	6.8%	7.6%	74.7%	82.6%	41.1%	36.4%
Equity Group	**(7.8%)**	18.0%	13.6%	6.5%	(1.5%)	13.6%	9.7%	10.8%	73.1%	84.3%	37.2%	24.6%
NIC Bank	**(11.9%)**	2.9%	18.9%	6.5%	4.1%	3.6%	7.1%	7.7%	87.7%	100.1%	33.3%	25.9%
Stanbic	**(12.1%)**	22.2%	12.5%	(2.7%)	8.0%	0.3%	5.3%	5.6%	75.1%	78.2%	38.6%	36.3%
Barclays Bank	**(13.3%)**	(10.2%)	3.2%	11.9%	6.8%	14.8%	10.1%	10.7%	86.8%	83.8%	27.9%	26.0%
I&M Holdings	**(17.9%)**	23.0%	10.3%	13.1%	9.1%	7.6%	7.7%	7.7%	89.5%	90.5%	31.3%	35.5%
Co-op Bank	**(25.4%)**	18.7%	2.7%	12.0%	14.2%	8.0%	8.8%	8.9%	88.4%	79.5%	26.0%	29.2%
StanChart	**(34.4%)**	34.8%	17.6%	16.9%	(1.1%)	(7.3%)	8.4%	9.5%	50.4%	59.9%	47.6%	49.2%
National Bank	**(42.2%)**	(70.0%)	3.4%	(1.6%)	(12.0%)	(9.3%)	6.9%	7.2%	57.7%	67.8%	38.1%	29.5%
HF Group**	**(74.0%)**	26.3%	(6.0%)	6.2%	(1.3%)	7.0%	5.7%	6.7%	89.3%	92.1%	9.2%	9.3%
Weighted Average*	**(10.0%)**	**13.3%**	**8.9%**	**6.8%**	**5.0%**	**6.6%**	**7.3%**	**7.7%**	**65.2%**	**67.7%**	**29.2%**	**25.4%**

The weighted average is based on Market Cap as at 31st August, 2017

****For Housing Finance, given their primary business of mortgage provision, we used the Loans to Loanable funds ratio. The Loan to Deposit ratio is at 141.3%***

Jubilee Holdings released H1'2017 results

Jubilee Holdings released H1'2017 results, recording an increase in Core earnings per share (EPS) by 23.2% coming in at Kshs 26.1, from Kshs 21.2 in H1'2016, attributed to a 30.1% growth in total income to Kshs 14.9 bn from Kshs 11.4 bn in H1'2016 despite a 31.0% growth in total expenses to Kshs 13.1 bn from Kshs 10.0 in H1'2016, with the increased profitability partly attributed to other comprehensive income at Kshs 0.3 bn, having been recorded at Kshs (0.4) bn the same time last year.

- The 30.1% rise in total income was driven by a 14.5% growth in gross earned premium to Kshs 15.6 bn from Kshs 13.6 bn in H1'2016 and a 7.3% increase in commissions earned to Kshs 1.1 bn from Kshs 0.9 bn in H1'2016,
- Investment income declined marginally by 1.6% to Kshs 3.4 bn from Kshs 3.5 bn in H1'2016, while investment in equities returned fair value gains amounting to Kshs 1.3 bn compared to a loss of Kshs 0.4 mn in H1'2016, driven by the stock price rally at the Nairobi Securities Exchange (NSE),
- The 31.0% growth in total expenses is attributable to a 38.7% rise in net insurance benefits and claims to Kshs 10.4 bn from Kshs 7.5 bn in H1'2016,
- The loss ratio worsened to 101.8% from 89.6%, while the expense ratio worsened to 50.4% from 42.9% in H1'2016, owing to a faster increase in operating expenses as compared to net premiums. The combined ratio thus worsened to 139.1% from 132.5%,
- Profit before tax (PBT) increased by 18.6% to Kshs 2.3 bn from Kshs 2.0 bn in H1'2016, while profit after tax (PAT) improved by 18.9% to Kshs 1.9 bn from Kshs 1.6 bn in H1'2016. However, adjusted for other comprehensive income, PAT rose by 23.2%,
- The Board of Directors recommended the payment of an interim dividend of Kshs 1.0 per share, the same recommended over the same period last year. The dividend translates into a projected full year dividend of Kshs 7.5 and dividend yield of 1.6%, at the current price of Kshs 468.0 per share, as at 1st September 2017.

Going forward, Jubilee's growth will be driven by: (i) new and growing market segments such as provision of maritime insurance, (ii) continued product development, pricing efficiency and adaptability to the evolving market trends, and (iii) expansion into new regions that will drive growth, e.g. DRC,

For a more comprehensive analysis, see our Jubilee Holdings Earnings Note H1'2017.

Sanlam Kenya released H1'2017 results

Sanlam Kenya released H1'2017 results, recording an increase in Core Earnings per Share (EPS) to Kshs 0.6 from Kshs (0.9) in H1'2016, against our expectations of an EPS growth to Kshs 0.1. The increase in EPS is attributed to an 18.8% increase in total income to Kshs 4.3 bn from Kshs 3.6 bn in H1'2016 outpacing a 10.2% increase in total expenses to Kshs 4.1 bn from Kshs 3.8 bn,

- The 18.8% rise in total revenue was driven by a 27.4% growth in gross earned premium to Kshs 3.4 bn from Kshs 2.6 bn in H1'2016,

- Gross earned premiums rose by 27.4% to Kshs 3.4 bn from Kshs 2.6 bn mainly attributed to strong growth in the general insurance business with significant gains being recorded in corporate client engagement. Gross written premiums in the general business grew by 225.0% to Kshs 1.3 bn from Kshs 0.4 bn in H1’2016,
- Investment income declined by 3.6% to Kshs 1.20 bn from Kshs 1.25 bn mainly attributable to a 19.3% increase in expenses in their investments arm to Kshs 57.9 bn from Kshs 48.5 bn in H1’2016. Investment income currently accounts for 28.1% of the total income, compared to 34.6% in H1’2016,
- Total expenses grew by 10.2% to Kshs 4.1 bn from Kshs 3.8 bn attributed to an increase in claims and policyholders’ benefits expense by 5.0% to Kshs 2.8 bn from Kshs 2.6 bn, and a 33.2% increase in operating and other expenses to Kshs 1.0 bn from Kshs 0.7 bn, which represents a steep rise. However, the detailed breakdown of the expenses was not disclosed by Sanlam,
- The loss ratio improved to 101.0% from 107.4%, while the expense ratio worsened to 51.1% from 46.8% in H1’2016, owing to a faster increase in operating expenses as compared to net premiums. The combined ratio thus worsened to 162.1% from 154.2%,
- Profit before tax (PBT) increased to Kshs 0.2 bn from a loss before tax of Kshs 0.1 bn, while profit after tax (PAT) increased to Kshs 0.1 bn from a loss after tax of Kshs 0.1 bn in H1’2016,
- The Board did not recommend payment of an interim dividend, same as in H1’2016.

Going forward, Sanlam Kenya's growth is likely to be driven by the general insurance unit and continued implementation of its 5-year growth strategy headlined by restructuring of the rest of the business to grow the non-premium income, which now contributes 36.6% to total income. The continued integration of the Sanlam Emerging Markets asset management business in the region is expected to be concluded within the year.

For a more comprehensive analysis, see our Sanlam Kenya Earnings Note H1’2017

Liberty Holdings released H1’2017 results

Liberty Holdings released H1’2017 results, recording an increase in Core earnings per share (EPS) by 18.9% coming in at Kshs 0.8, from Kshs 0.7 in H1'2016, attributed to a 7.2% growth in total income to Kshs 5.0 bn from Kshs 4.7 bn in H1’2016 despite a 6.7% growth in total expenses and commissions to Kshs 4.5 bn from Kshs 4.2 in H1’2016

- The 7.2% rise in total income was driven by a 2.5% growth in gross earned premium to Kshs 4.9 bn from Kshs 4.8 bn in H1'2016 and a 23.9% increase in commissions earned to Kshs 0.5 bn from Kshs 0.4 bn in H1’2016,
- Investment income rose by 16.1% to Kshs 1.7 bn from Kshs 1.5 bn in H1’2016, supported by the performance of their equities portfolio following the price rally at the Nairobi Securities Exchange (NSE),
- The 6.7% growth in total expenses is attributable to a 9.0% rise in net insurance benefits and claims to Kshs 2.3 bn from Kshs 2.1 bn in H1’2016,
- The loss ratio worsened to 83.4% from 74.9%, while the expense ratio worsened to 44.9% from 42.9% in H1’2016, owing to a faster increase in operating expenses, as compared to a 2.2% decline in net premiums to Kshs 2.76 bn from Kshs 2.82 bn in H1’2016. The combined ratio thus worsened to 107.2% from 93.9%,
- Profit before tax (PBT) increased by 11.6% to Kshs 0.55 bn from Kshs 0.49 bn in H1’2016, while profit after tax (PAT) improved by 18.9% to Kshs 0.42 bn from Kshs 0.36 bn in H1’2016.
- The Board of Directors did not recommend an interim dividend, same as in H1’2016.

For a more comprehensive analysis, see our Liberty Holdings Earnings Note H1’2017

The listed insurance firms have released their H1’2017 results, recording an average decline of 12.5% in core earnings per share, from an average gain of 69.4% in H1’2016. Jubilee Holdings and Liberty Holdings recorded impressive growth while Britam Holdings was the worst hit driving the weighted market average core EPS downwards due to change in valuation methodology on the long-term insurance claims. The sector experienced marginal improvement in operational efficiency with the expense ratio declining to 54.3% from 55.5% in H1'2016 despite the loss ratio rose to 72.7% from 66.5% indicating increased claims in the industry. This resulted to the industry average combined ratio increasing to 127.0% from 122.0% in H1'2016. On average, the insurance sector has delivered a Return on Average Equity of 10.9% a marginal improvement from 9.0% in H1'2016.

Listed Insurance Companies HY'2017 Earnings and Growth Metrics

Insurance Company	Core EPS Growth		Net Premium growth		Net Claims Growth		Loss Ratio		Expense Ratio		ROaA		ROaE	
	H1'17	H1'16	H1'17	H1'16	H1'17	H1'16	H1'17	H1'16	H1'17	H1'16	H1'17	H1'16	H1'17	H1'16
Jubilee	**23.2%**	7.5%	22.0%	12.6%	38.7%	21.4%	101.8%	89.6%	37.3%	42.9%	4.3%	3.8%	18.0%	16.8%
Liberty	**18.9%**	15.4%	(2.2%)	(4.4%)	9.0%	20.0%	83.4%	74.9%	79.6%	74.7%	1.2%	1.0%	6.3%	5.5%
Kenya Re	**3.7%**	4.1%	7.1%	6.5%	1.6%	30.8%	51.0%	54.9%	41.0%	38.0%	8.5%	10.0%	13.6%	16.2%
CIC	**(3.5%)**	104.2%	16.9%	(10.6%)	27.2%	(25.8%)	65.0%	63.5%	57.2%	53.1%	0.3%	2.6%	1.2%	9.0%
Britam	**(44.1%)**	184.8%	8.8%	6.4%	84.8%	(29.4%)	54.7%	48.0%	70.0%	73.3%	2.0%	0.2%	8.9%	0.7%
Sanlam*	**N/A**	(148.6%)	11.7%	2.2%	5.0%	25.8%	83.9%	77.3%	51.1%	46.8%	0.3%	(0.5%)	2.4%	(3.3%)
Weighted Average**	**(12.5%)**	**69.4%**	**12.8%**	**5.1%**	**42.8%**	**0.8%**	**72.7%**	**66.5%**	**54.3%**	**55.5%**	**3.3%**	**3.0%**	**10.9%**	**9.0%**

*** Sanlam's EPS cannot be calculated since it registered a loss in 2016***

**** The weighted average is based on Market Cap as at 31st August, 2017**

In an effort to keep our rankings of companies on the Cytonn Corporate Governance Ranking (Cytonn CGR) Report up-to-date, we continually update the rankings whenever there are changes on any of the 24 metrics that we track, and how this affects the company ranking. During the week, Safaricom Limited Board appointed Mr Mohamed Shameel Aziz Joosub and Ms Linda Watiri Muriuki as Directors of the company. The Board also approved resignation of Mr. Gianluca Ventura as a substantive Director of the company. Safaricom's score has improved to 83.3% from 81.3% due to an improvement in the board size from an even number 10 to an odd number 11. It's ranking has therefore improved to position 3 from position 5.

Below is our Equities Universe of Coverage:

all prices in Kshs unless stated otherwise

No.	Company	Price as at 31/07/17	Price as at 31/08/17	m/m Change	YTD Change	Target Price*	Dividend Yield	Upside/ (Downside)**
1.	DTBK	184.0	185.0	0.5%	56.8%	241.1	1.7%	32.0%
2.	NIC***	33.8	40.5	20.0%	55.8%	51.2	3.1%	29.5%
3.	HF Group***	10.5	11.6	11.0%	36.8%	13.9	8.4%	28.3%
4.	KCB Group***	40.8	45.0	10.4%	56.5%	54.0	6.7%	26.7%
5.	I&M Holdings	114.0	125.0	9.6%	38.9%	147.5	2.9%	20.9%
6.	Barclays	9.9	10.7	8.1%	(23.9%)	12.1	3.5%	17.1%
7.	Co-op Bank	15.7	17.1	8.9%	29.2%	18.5	4.5%	13.0%
8.	Jubilee	430.0	484.0	12.6%	(1.2%)	490.5	1.8%	3.1%
9.	Stanbic	80.0	81.0	1.3%	14.9%	77.0	5.8%	0.8%
10.	Kenya Re	21.3	21.8	2.4%	(3.3%)	20.5	3.4%	(2.3%)
11.	Liberty	12.8	13.9	9.0%	5.3%	13.0	0.0%	(6.6%)
12.	StanChart	221.0	237.0	7.2%	25.4%	209.3	4.3%	(7.4%)
13.	Equity Group	40.8	43.8	7.4%	45.8%	38.4	4.6%	(7.7%)
14.	Britam	14.5	15.0	3.8%	50.0%	13.2	1.8%	(10.2%)
15.	Safaricom	24.5	25.5	4.1%	33.2%	19.8	4.7%	(17.8%)
16.	Sanlam Kenya	27.0	29.5	9.3%	7.3%	21.1	1.0%	(27.6%)
17.	CIC Group	4.9	6.0	22.7%	56.6%	3.7	1.7%	(36.0%)
18.	NBK	9.6	11.9	24.6%	65.3%	4.0	0.0%	(66.2%)

**Target Price as per Cytonn Analyst estimates*

***Upside / (Downside) is adjusted for Dividend Yield*
****Banks in which Cytonn and/or its affiliates holds a stake*
For full disclosure, Cytonn and/or its affiliates holds a significant stake in KCB Group, ranking as the 5th largest local institutional investor

We remain "neutral with a bias to positive" for investors with short to medium-term investments horizon and are "positive" for investors with a long-term investment horizon.

Private Equity

During the month, we witnessed investment activity in the financial services, manufacturing and the energy sectors with fundraising activities focused on the technology, and energy sectors.

Acquisitions:

Kansai Plascon Africa Limited, a subsidiary of Japanese paint maker Kansai Paint Co. Ltd, completed the acquisition of a 90.0% stake in Kenyan paint and coating manufacturer, Sadolin Group. The transaction was valued at USD 100.0 mn hence valuing the company at USD 111.1 mn (Kshs 14.5 bn). The remaining 10.0% stake is held by undisclosed local investors. For more information, see our Cytonn Weekly #34/2017.

South African based Sanlam Investments has committed to acquire a 30.0% stake at USD 7.6 mn in South African based EasyEquities, a subsidiary of Purple Group a South African based financial services provider, subject to regulatory approval in South Africa. This effectively values EasyEquities at USD 25.3 mn (Kshs 2.6 bn). EasyEquities is a fintech company that offers a platform for low cost investment solutions by offering users an opportunity to invest in securities which include whole shares and fractional share rights. For more information, see our Cytonn Weekly #34/2017.

UK based private equity firm, Enko Capital, acquired an undisclosed significant minority stake in Agence Maritime Internationale (AMI) Logistics, a Dubai-headquartered logistics business with significant operations in East and Southern Africa for USD 7.0 mn. In Kenya, AMI operates from the port of Mombasa offering freight forwarding services and handling transit containers bound for Kampala. The deal marks the second investment for the Enko Africa Private Equity Fund (EAPEF), which held its final close in February 2016 at USD 83.5 mn. For more information, see our Cytonn Weekly #33/2017.

French oil giant Total has acquired 100% stake of Maersk Oil, the oil and gas unit of Danish shipping giant A.P. Moller Maersk, for USD 7.5 bn. The transaction is structured in that (i) Maersk will receive USD 5.0 bn worth of Total shares, and (ii) Total will acquire USD 2.5 bn of Maersk Oil's debt. The acquisition effectively transfers Kenya's Maersk Oil assets to Total which gives Total a stake in the Kenyan oil reserves in, South Lokichar, Turkana, estimated at 750 mn barrels. Maersk Oil currently has 25.0% ownership in the exploration licenses of blocks 10BA, 10BB and 13T in South Lokichar alongside Tullow Oil and Africa Oil who have 50.0% and 25.0% ownership respectively. The acquisition is expected to be completed in the first quarter of 2018 and will make Total the second largest International Oil Corporation in Algeria by production and will complement Total's leading oil distributor position in East Africa.

Fundraising:

Kenya's Twiga Foods Ltd, a mobile based business to business food supply platform successfully raised USD 12.8 mn (Kshs 1.3 bn) during their Series A funding. The investment which is made up of USD 6.3 mn in equity, USD 4.0 mn in debt and USD 2.8 mn in grant funding from United States Agency for International Development (USAID), will go toward expansion of the business by enabling it to increase the number of vendors, diversify its product portfolio, and introduce advanced supplier services. For more information, see our Cytonn Weekly #31/2017.

Three Danish Pension Funds; Pension Danmark, PKA and Medical Doctors' Pension Fund, together with A.P. Moller Holding, a holding company of Danish Based shipping company, A.P. Moller-Maersk, have set up a fund that will invest in infrastructure development in Africa, focused in the transport and energy sector. The fund has received USD 550.0 mn in commitments from the partners and targets to achieve a total of

USD 1.0 bn in commitments in the next 12 months. For more information, see our Cytonn Weekly #32/2017.

The successful fundraising activity by private equity firms indicates a positive outlook by investors in the Sub-Saharan Africa private equity space, motivated by the continued growth in the sector and an increasing number of successful exits, with a 9.1% increase in the number of successful exits recorded in 2016.

Private equity investments in Africa remains robust as evidenced by the increased deal flow in a number of sectors that support growth in the Continent. The increasing investor interest is attributed to (i) rapid urbanization, a resilient and adapting middle class and increased consumerism, (ii) the attractive valuations in Sub Saharan Africa's private markets compared to its public markets, (iii) the attractive valuations in Sub Saharan Africa's markets compared to global markets, and (iv) better economic projections in Sub Sahara Africa compared to global markets. We remain bullish on PE as an asset class in Sub-Sahara Africa. Going forward, the increasing investor interest and stable macro-economic environment will continue to boost deal flow into African markets.

Real Estate

During the month of August, the Kenya National Bureau of Statistics (KNBS) released its annual Leading Economic Indicators Survey, which indicated that the value of approved buildings declined by 16.3% in between January and May from Kshs 126.3 bn in 2016 to Kshs 105.7 bn in 2017. Residential building approvals declined by 28.2% from Kshs 74.2 bn in 2016 to Kshs 58.1 bn in 2017 with commercial office building approvals declining by 9.3% from Kshs 52.0 bn in 2016 to Kshs 47.6 bn in 2017. We attribute the decline mainly to the wait and see approach adopted by risk averse investors during the electioneering period and reduced credit supply by banks as a result of the enactment of the Banking Amendment Act 2015. In our opinion, the decline in activity is only temporary, and is expected to stabilize in the near-term and increase in the medium-term, supported by high demand in both the commercial and residential sector due to (i) the huge housing deficit, estimated at 2.0 mn units, (ii) rapid urbanization at 4.4% p.a. compared to a global average of 2.0%, and (iii) entry of multinationals such as Volkswagen and Johnson & Johnson, creating demand for residential, commercial and retail themes.

During the month, the performance and activities of the various themes were as expounded below:

Commercial

During the month, retailers adopted expansionary strategies, with renowned international fashion retailers LC Waikiki and Woolworths, announcing plans to open stores at the Hub, Karen, before the end of 2017. This will be LC Waikiki's second branch in Kenya, in addition to its existing outlet at Two Rivers Mall that was opened in February this year. The retailer also plans to open a store in Nairobi's CBD so as to improve accessibility, especially by their walk in customers in Nairobi. Java House, a coffee chain retailer owned by Dubai-based private equity firm Abraaj Group, announced that it will take up 2,800 sqft of space in Crystal Rivers Mall in Athi River. The mall, developed by Safaricom Investments Pension Scheme, is scheduled to start operations in early 2018, with retailers such as Naivas Supermarket pre-booking the space. These retailers are targeting to reach out to the growing middle class in the country who have higher incomes indicated by the 43.7% growth in GDP per capita from 1,055 USD in 2011 to 1,516 USD in 2016. This middle class population is increasingly seeking a lifestyle and hence demanding prime products. We expect these retailers to boost the retail sector that has been experiencing a slowdown as a result of declined supply and poor performance of the local retail chains such as Nakumatt and Uchumi.

Residential

In the residential theme, the key highlights during the month were:

1. The Central Bank of Kenya (CBK), released their Bank Supervision Annual Report 2016, which indicated that there was a drop in the uptake of home loans, despite the increased demand for mortgages in Kenya, with the reduced interest rates. According to the report, the number of

mortgages declined by 1.5% to 24,085 in 2016 from 24,453 in 2015. The decline was attributed to increased underwriting standards by banks thus locking out potential borrowers. This was despite increased demand for mortgages in the country due to (i) increased affordability as the enactment of the Banking Amendment Act 2015 resulted in the average interest rate charged on mortgages falling to 13.5% in 2016 from 18.7% in 2015, and (ii) increased appetite for mortgages due to belief by buyers that they could qualify for higher mortgage amounts. However, according to the report, commercial banks have introduced higher credit standards thus actual mortgage disbursements have been lower despite the increased demand.

5 Year Mortgage KPI Trends in Kenya

Year	Outstanding Mortgages	Non Performing Mortgages	Number of Mortgages	Average Mortgage Size	Annual Change in No of Mortgages
2011	90.4 bn	3.0 bn	16,029	5.6 mn	
2012	119.6 bn	6.8 bn	18,587	6.4 mn	**16.0%**
2013	138.1 bn	8.5 bn	19,879	6.9 mn	**7.0%**
2014	164.0 bn	10.8 bn	22,013	7.5 mn	**10.7%**
2015	203.3 bn	11.7 bn	24,458	8.3 mn	**11.1%**
2016	219.9 bn	22.0 bn	24,085	9.1 mn	**(1.5%)**
The number of outstanding mortgages have been increasing year on year with a 5-year CAGR of 11.1%. 2016 was the first year the number declined attributable to higher credit standards adopted by banks following the implementation of the Banking Amendment Act 2015					

Source: Central Bank of Kenya

With the high demand of 2.0 mn houses, growing by 200,000 p.a., we expect the residential sector to pick up in 2018 as the slowdown witnessed this year will continue due to the extension of the electioneering period as a result of the annulment of the presidential election result. Real estate financing will, however, continue being a challenge and developers ought to come up with creative payment plans such as instalment sales and group purchases to increase the sales rates of their developments.

2. Acorn Holdings Limited, a partnership between local real estate developer Acorn Group and Helios, a London based private equity fund, announced plans to begin construction of 3,800 hostel units in Nairobi at a total cost of Kshs 7.4 bn. The first set of the hostels will be set up in areas near Strathmore University, United States International University Africa (USIU-Africa) and Daystar University. The development is targeting the growing student population in institutions of higher learning in the country, which has grown by a CAGR of 18.0% over the last 5-years, from 251,200 in 2012 to 564,500 in 2016, according to the Economic Survey 2017. In our view the development is a step in the right direction towards curbing the student housing deficit and we expect to see more private companies enter the sector to tap into the demand gap and reap investment returns, supported by (i) steady income from solid rental growth and resilience from tough economic times, (ii) high occupancy backed by strong demand from the student population, growing at a 5-year CAGR of 18.0%, with Jumia House Real Estate Research report estimating that most universities in Kenya can only accommodate 20% – 30% of the students admitted, with the rest being forced to seek housing outside campus, hence student housing shortage accounting for 40.0% of the over 200,000 national housing units p.a. and (iii) relatively low risk profile, given the multi-tenant nature of student housing.

Hospitality

Contrary to market expectations, and unlike the performance of the other themes, the hospitality sector picked up in August, with the Cabinet Secretary for tourism announcing in a tourism stakeholders' forum that the Kenyan tourism sector had experienced an appreciation in arrivals by 18.0% since 2015, with a possibility of a 20.0% increase in tourist arrivals expected by the end of 2017. The Cabinet Secretary noted that the hotels in Diani and Maasai Mara had recorded full occupancies on the eve of the election and this is expected to continue, especially in the Mara due to the wildebeest migration; the migration usually marks the peak season for the sector. This was supported by data from the Kenya National Bureau of Statistics (KNBS), which indicated that between January and May 2017, the number of international visitor arrivals increased by 10.9% and 8.5% at Jomo Kenyatta International Airport from 288,905 to 320,588 and Mombasa's Moi International Airport from 35,388 to 38,397, respectively, compared to the same period in 2016. The Kenya Tourism Board Chairman attributed the growth to aggressive marketing, which has helped restore confidence among key international markets such as Europe and the USA and the new emerging markets in Africa and Asia as well as the domestic market.

Continued infrastructural improvement, increased marketing by the government through the Kenya Tourism Board (KTB), as well as improved security in the country will continue boosting the performance of the hospitality sector.

Land

Land continues to be one of the most valued assets, with recording the highest performance rates, growing with a 5-year CAGR of 19.4% between 2011 and 2016 as per Cytonn Metropolitan Area Land Report. In August, the Johannesburg Stock Exchange listed ADvTECH Ltd, an education, training and placement company based in South Africa, announced the purchase of a land parcel in Tatu City. The parcel will be used to set up a THRASS education system Crawford schools brand, in line with the company's expansion strategy to various countries in Africa.

Statutory Actions

The government has revived the annuity roads financing program that was shelved in May. Under the program, private contractors, will get financing from banks, and they will develop and manage roads for a maximum of 10 years. The government will then work out payment terms evenly with the banks involved. The program had been shelved due to inflated costs by engineers and high costs by banks who were demanding rates higher than the 12-13% proposed by the government. The World Bank however issued a Kshs 150 bn concession loan to the government through local banks at between 5%-6% to the Kenya Shilling, hence facilitating the commencement of the first phase of the project, expected to cost a total of Kshs 260 bn for the 10,000km of roads earmarked for refurbishment. If successful the program will have several advantages, including faster expansion of infrastructure, as the treasury is not able to disburse all the requisite funds at a go, and assured maintenance of roads by the contractors, therefore increasing the lifespan of the roads. The flagship project by Intex Construction Company, for the 91.0 km Ngong – Kiserian – Isinya and Kajiado – Imaroro road, at a cost of Kshs 11.0 bn, broke ground and the expansion of the Nairobi – Mombasa Highway by American Construction giant Bechtel will operate using the same model. Infrastructure, and especially roads, support real estate by opening up areas for development as has been the case in Nairobi's Satellite Towns and the Bypasses, and with more roads, we expect real estate activity to pick up in various parts of the country.

Still in infrastructure, the government announced plans to construct a Kshs 5.5 bn cable car facility along the Likoni Channel, linking Mombasa Island and Diani. Diani, which is a popular destination for holidaymakers, has had transport challenges such as congestion at the Likoni channel where travellers rely on ferries to cross from Mombasa Island to the South Coast. In our opinion, the move is a step in the right direction as it will improve the travel experience of visitors, leading to an increase in tourist arrivals and hence boost the tourism and hospitality sector, especially at the Kenyan Coast.

Nairobi is consistently exceeding expectations, according to an annual survey ranking done by Nestpick, an aggregator website for furnished apartments with operations worldwide. Nairobi was ranked as the 84th best place to work worldwide by the Nestpick Survey and 4th in Africa. In the global list, Nairobi was behind Johannesburg at the 71st position, Cairo at the 80th position and Tunis at the 83rd position. The survey considered five key performance indicators namely: (i) the city's start up ecosystem, (ii) the salaries offered, (iii) social security and benefit of the cities, (iv) cost of living, and (v) the quality of life. These surveys are tools used to guide firms setting up shop in new countries as well as a determinant of a city's ability to attract and retain foreign investments, expatriates and tourists, and with Nairobi getting global exposure, we are likely to witness more companies setting up shop in the city. Currently, Nairobi hosts continental headquarters for multinationals such as International Finance Corporation (IFC), General Electric (GE) and Google, and in 2017, a number of companies have announced plans to start operations in the city including, Johnson & Johnson, Boeing and RICS, among others. These multinationals increase demand for grade A office, retail and prime residential houses, thus boosting the real estate market in the country.

Real estate remains attractive for investment, bolstered by the high returns of 25.8% in 2016, high demand and demographics. The slowdown being witnessed, especially in transaction volumes, has mainly been as a result of the wait and see approach adopted by investors due to the August election, and once the electioneering period comes to an end, we expect the volumes and the market to pick up.

Nairobi Metropolitan Area Residential Report 2017

Last year, we released a report that covered the mortgage and rental affordability of the residential sector, called Nairobi Mortgage and Rental Affordability Report. According to the report, most sub-markets were unaffordable to prospective home-owners with an average mortgage affordability index of 66, whereas most markets were affordable to the renters with an average rental affordability index of 132, where index scores of 100 and above indicate affordability. This year, we conducted research on 35 sub-markets in the Nairobi Metropolitan to determine the investment opportunity for residential developments in 2017. This report shows the performance of both apartments and detached units in the 35 sub-markets. We start with an introduction, then cover the performance summary by sub-markets and conclude by establishing where the investment opportunity lies by ranking the sub-markets using various metrics.

Introduction

The residential real estate sector in Kenya has witnessed increased interest in the last 5-years supported by (i) the accumulated housing deficit of approximately 2 mn units and growing at 206,000 units p.a according to the Africa Development Bank, (ii) the high urbanization rate at 4.4% p.a. compared to a global average of 2.0%, which has created increased demand for residential real estate in urban centers, (iii) population growth at 2.7% p.a. compared to a global average of 1.2%, (iv) improvement in infrastructure, leading to opening up of new areas for development, and (v) the growing middle class demanding attractive real estate. In 2017, however, various reports have been released highlighting a decline in sales of residential units. This can be attributed to investors adopting a wait and see approach ahead of the elections held on August 8th and the trend is likely to continue in the short-term given the cancellation of the presidential results and postponement of the elections to a later date. In addition, the implementation of the Banking Amendment Act 2015 resulted in a decline in credit growth from 25.8% in June 2014 to 2.1% as at May 2017. This is because banks are unable to factor in 'high risk borrowers' within the stipulated margins. According to the Central Bank of Kenya, the number of active mortgage accounts in the year 2016 declined by 1.5% to 24,085 from 24,458 in 2015, showing the impact of the Banking Amendment.

On the supply side, according to the World Bank Kenya Economic Update of 2017, 48.0% of housing supplied is in the upper middle Income segment, 35.0% in the high income segment and only 17.0% in the lower income segments. The main factors affecting supply include

i) increasing cost of land, with prices rising at a 5-year CAGR of 19.4%,
ii) access to funding, which is difficult to get unless you have structuring capabilities and is also expensive,
iii) high construction costs, which constitute approximately 70% of development costs, and,
iv) availability of infrastructural support.

Due to these limitations, private developers have continued to focus on the upper middle and high-end unit types to sustain profit margins. We have however seen various efforts by the government to boost provision of affordable housing including the reduction of corporate tax to 15% from 30% for firms that develop at least 100 affordable housing units annually, and scrapping of title search fees, NCA and NEMA fees. This is likely to enable more developers including Saccos and housing cooperatives provide more affordable housing.

In terms of performance, on average prices increased by 3.8% in 2017 compared to a 7.4% increase in 2016 while rental yields remained fairly stable averaging at 5.6% in 2017 compared to the 2016 average of 5.2%. This indicates sustained demand for rental housing whereas demand for sale houses declined.

The performance of the residential sector is as summarized below:

(all values in Kshs unless stated otherwise)

Year on Year Change in Price Appreciation and Rental Yield							
Unit Typologies	Average Price Appreciation (2017)	Average Rental Yield (2017)	Total Returns (2017)	Average Price Appreciation (2016)	Average Rental Yield (2016)	Total Returns (2016)	Y/Y Change in Total Return (% Points)
Detached	4.2%	5.2%	9.4%	6.5%	5.2%	11.7%	(2.3%)
Apartments	3.5%	6.0%	9.5%	8.3%	5.2%	13.5%	(4.0%)
Average	**3.8%**	**5.6%**	**9.4%**	**7.4%**	**5.2%**	**12.6%**	**(3.2%)**
Prices in 2017 appreciated albeit at a lower rate of 3.8%, which is 3.7% lower than the same in 2016 due to a slow-down in demand attributed to investor anxiety over the 2017 elections. Rental yields remained stable at 5.5% compared to 5.2% yield in 2016 indicating sustained demand for rental housing.							

Source: Cytonn Research

Sub Market Analysis

In our submarket analysis, we classified the various suburbs in the Nairobi Metropolitan Area into three segments

- **High End Segment** – Consists of prime suburbs in Nairobi, such as Karen, Runda and Kitisuru. Most of these zones have been zones for low rise residential developments only and are characterized by palatial villas and bungalows on half acre parcels
- **Upper Middle Income Segment** – Consists of suburbs such as Kilimani, Lavington, Kileleshwa, Loresho and Ridgeways among others. The population in these zones are middle class but with higher incomes than the average characterization of middle class. They are zones for both high rise and low density houses.
- **Lower Middle Income Segment** – Consists of suburbs in Nairobi habited by middle class such as Donholm, Komarock and Imara Daima as well as Satellite Towns such as Ngong, Rongai and Juja

The submarket analysis is as presented below, in the zones above, we analysed detached units and apartments separately:

i) Detached Units - High End Segment

This consists of zones such as Karen, Runda and Kitisuru. Houses are mainly on half acre land parcels. The zone has the highest average price per square meter at Kshs 194,000 and recorded average rental yields of 4.9%. On average prices increased by 2.6% in this zone in 2017 with Lower Kabete recording the highest increase in price of 5.1%.

(all values in Kshs unless stated otherwise)

Detached Units- High End Segment						
Location	Average Price per SQM (2017)	Average Rent per SQM (2017)	Annual Uptake	Rental Yield	Price Appreciation	Total Return

Lower Kabete	165,113.9	562.5	18.0%	4.1%	5.1%	9.2%
Runda	208,621.3	892.0	9.9%	5.2%	3.6%	8.7%
Roselyn	173,513.4	853.5	24.3%	5.8%	2.0%	7.7%
Kitisuru	234,497.6	1,015.3	28.5%	5.4%	0.6%	6.0%
Karen	186,515.4	727.3	35.4%	4.0%	1.7%	5.7%
Average	**193,652.3**	**810.1**	**23.2%**	**4.9%**	**2.6%**	**7.5%**
Lower Kabete and Runda have the highest returns attributed to their prime locations and low supply due to scarcity and high cost of development land.						

Source: Cytonn Research

ii) Detached Units - Upper Middle Segment

These zones consist of areas such as Langata, Runda Mumwe, Redhill and Loresho. Zoning regulations in these areas allow for development of both apartments and single dwelling units. The areas recorded on average a rental yield of 5.0% in 2017 and an average increase in prices of 6.1%, Langata had the highest price increment in the zone of 13.4% attributable to ease of access to the area due to its proximity to the CBD and other business nodes such as Upperhill.

(all values in Kshs unless stated otherwise)

Detached Units- Upper Middle Segment						
Location	Average Price per SQM (2017)	Average Rent per SQM (2017)	Annual Uptake	Rental Yield	Price Appreciation	Total Return
Langata	131,637.0	424.3	21.6%	3.9%	13.4%	17.4%
Runda Mumwe	146,861.5	684.9	21.3%	5.9%	6.1%	12.0%
Redhill	96,640.0	344.1	10.4%	5.0%	6.0%	10.9%
Loresho	147,610.6	613.6	16.8%	5.2%	2.9%	8.0%
Ridgeways	187,083.7	843.0	19.9%	5.1%	1.9%	7.0%
Average	**141,966.6**	**582.0**	**18.0%**	**5.0%**	**6.1%**	**11.1%**
Lang'ata has the highest returns due to its proximity to the Nairobi CBD and other business districts such as Upperhill, thus has high demand						

Source: Cytonn Research

iii) Detached - Lower Middle Segment

This zone consists mainly of Satellite Towns and Nairobi suburbs such as Donholm and Komarock. The area has an average price per square meter of 77,000 and the highest annualized sales rate in Nairobi Metropolitan Area of 28.4%. On average prices increased in these zones by 3.9%, with Juja having the highest increment of 11.0% attributable to high demand from middle classes as a result of lower prices, the area has a price per square meter of 71,000 against a market average of 77,000.

(all values in Kshs unless stated otherwise)

Detached- Lower Middle Segment						
Location	Average Price per SQM (2017)	Average Rent per SQM (2017)	Annual Uptake	Rental Yield	Price Appreciation	Total Return
Juja	70,526.1	308.6	44.4%	6.3%	11.0%	17.3%
Thika	66,253.7	340.5	17.4%	6.9%	7.8%	14.7%
Kitengela	76,716.3	307.6	26.4%	5.1%	9.0%	14.0%
Athi River	87,788.8	301.4	26.1%	4.3%	4.8%	9.0%
Ngong	64,285.8	251.0	24.2%	4.5%	4.4%	8.9%
Komarock	78,876.6	525.3	32.3%	8.0%	0.0%	8.0%
Ruiru	84,821.4	384.6	25.0%	5.7%	0.5%	6.2%
Rongai	72,351.6	289.0	21.2%	4.8%	0.9%	5.7%

Donholm	91,797.6	397.1	38.6%	5.2%	(3.2%)	2.0%
Average	**77,046.4**	**345.0**	**28.4%**	**5.6%**	**3.9%**	**9.5%**

Juja and Thika have the highest returns with relatively high price appreciation driven by demand from the lower middle income population. These markets also have relatively larger unit sizes compared to areas such as Donholm for the same price, thus buyers pay less per square metre

Source: Cytonn Research

iv) Apartments - Upper Middle Segment

This zone consists of areas such as Ridgeways, Kilimani, Westlands and Parklands. They have an average price per square metre of Kshs 128,000 and in 2017, the zone recorded the highest yield in Nairobi Metropolitan Area of 6.2% against a market average of 5.5%. In the Zone, Ridgeways had the highest price increment of 12.2% attributed to high demand in the zone evidenced by the high average uptake of 32.9% recorded.

(all values in Kshs unless stated otherwise)

Apartments- Upper Middle Segment						
Location	Average Price per SQM (2017)	Average Rent per SQM (2017)	Annual Uptake	Rental Yield	Price Appreciation	Total Return
Ridgeways	118,482.7	585.0	32.9%	6.1%	12.2%	18.4%
Kilimani	159,201.5	846.0	28.3%	6.6%	8.7%	15.4%
Loresho	106,882.1	531.2	29.8%	6.0%	3.9%	9.9%
Westlands	128,151.3	585.2	22.0%	6.1%	3.5%	9.6%
Parklands	128,650.3	606.3	28.9%	5.6%	3.7%	9.3%
Riverside	159,359.7	734.3	8.8%	7.0%	2.2%	9.2%
Kileleshwa	128,442.6	602.7	26.6%	7.9%	1.1%	8.9%
Mountain View	85,069.1	380.8	28.9%	5.1%	2.8%	7.9%
Upper Hill	141,041.6	668.8	16.0%	5.8%	0.2%	6.0%
Average	**128,364.5**	**615.6**	**24.7%**	**6.2%**	**4.3%**	**10.5%**

Ridgeways has the highest returns at 18.4% driven by high demand as seen through the 32.9% annual uptake compared to other markets with an average annual uptake of 24.7%. The area borders Runda and Muthaiga, attracts ex-patriates working at the United Nations and Government Embassies in Gigiri and Runda. Ridgeways still has low supply compared to Kilimani and Westlands hence less competition between developers.

Source: Cytonn Research

v) Apartments-Lower Middle Income Suburbs

Apartments in the lower middle segment recorded an average rental yield of 5.7% with an average price increment of 3.5%. Like in the detached houses for the same Zone, Langata had the highest increase in price of 13.9% attributed to proximity to the CBD and other business nodes such as Upperhill.

(all values in Kshs unless stated otherwise)

Apartments- Lower Middle Income Suburbs						
Location	Average Price per SQM (2017)	Average Rent per SQM (2017)	Annual Uptake	Rental Yield	Price Appreciation	Total Return
Langata	108,948.8	434.6	23.9%	4.8%	13.9%	18.7%
Komarock	71,071.2	210.5	14.4%	3.6%	9.1%	12.7%
Imara Daima	78,010.8	354.0	22.7%	5.6%	5.2%	10.7%
Dagoretti	98,185.3	516.9	31.9%	6.4%	3.9%	10.3%
Kahawa West	75,956.9	511.9	38.1%	8.6%	(3.8%)	4.8%
Kasarani	115,628.3	413.5	23.0%	4.2%	0.0%	4.2%

Donholm	73,807.0	393.2	18.7%	6.4%	(3.7%)	2.7%
Average	**88,801.2**	**404.9**	**24.7%**	**5.7%**	**3.5%**	**9.2%**

Lang'ata has the highest returns among the lower middle income suburbs at 18.7% attributed to high price appreciation. The area is attractive to both investors and home-buyers due to its proximity to major business districts.

Source: Cytonn Research

vi) Apartments Lower Middle Income Satellite Towns

Nairobi's Satellite Towns recorded an average rental yield of 6.3% with an average price increment of 3.2%. Thindigua had the highest price increment of 13.0% as a result of high by demand for houses in the area. This is as it neighbours prime areas such as Runda and Ridgeways and is easily accessible from the Central Business District compared to other satellite towns.

(all values in Kshs unless stated otherwise)

Apartments- Lower Middle Income Satellite Towns						
Loction	**Average Price per SQM (2017)**	**Average Rent per SQM (2017)**	**Annual Uptake**	**Rental Yield**	**Price Appreciation**	**Total Return**
Thindigua	78,875.0	415.8	32.2%	6.4%	13.0%	19.3%
Uthiru	71,564.8	386.3	37.9%	6.8%	5.5%	12.3%
Kitengela	47,369.2	225.9	22.6%	5.4%	6.4%	11.8%
Ruaka	99,240.3	448.7	25.0%	5.3%	6.4%	11.8%
Kikuyu	77,060.2	353.8	13.0%	5.5%	5.2%	10.7%
Thika	50,974.5	296.9	12.9%	7.6%	1.5%	9.1%
Ruiru	79,435.6	453.5	15.6%	6.5%	1.9%	8.4%
Lower Kabete	81,388.4	469.2	19.4%	6.6%	1.2%	7.8%
Athi River	59,982.1	356.5	23.1%	7.5%	(0.1%)	7.4%
Rongai	57,951.9	322.6	27.3%	6.8%	(1.4%)	5.4%
Ngong	60,760.2	263.5	11.8%	5.1%	(1.1%)	4.1%
Juja	50,728.3	239.1	15.3%	5.6%	0.0%	5.6%
Average	**67,944.2**	**352.7**	**21.3%**	**6.3%**	**3.2%**	**9.5%**

Thindigua is the best performing market with a 19.3% return driven by demand. It neighbours prime areas such as Runda and Ridgeways and is easily accessible from the Central Business District compared to other satellite towns.
Apartments in Juja, Ngong' and Rongai have recorded stagnation in prices indicating low demand compared to other satellite towns. As they are far from the Central Business District, they mostly attract people seeking detached units with an own compound.

Source: Cytonn Research

Investment Opportunity

Whereas the overall market performance has declined, there exists an opportunity in some sub-markets. Thus to identify the investment opportunity in the sector and single out the specific suburbs with the highest returns, we ranked the submarkets based on

- Weighted annual uptake – Refers to how fast developments sell on average per annum, the higher/ faster the sales rate, the higher the points allotted
- Average returns – This is the sum of the rental yield and price appreciation for each suburb. The higher the return the more points allotted
- Price to land multiple – This the number of times the price of a residential unit in a suburb sells above the price of land on which the unit sits, the higher the multiple the more points allotted
- Availability of development land – Areas with higher supply of development land have higher ranking and hence more points
- State of infrastructure – Ranked as poor, average or good, with poor referring to areas that are accessed by earth roads and are not sewered, average referring to areas that are accessed by tarmac but are not sewered and good referring to areas that are both tarmacked and sewered

- Distance from main business nodes- Areas closer to main business nodes such as the Nairobi Central Business District (CBD) have higher ranking due to the ease in commuting for majority of the working adult population

Based on the above metrics, we allotted points to the areas on a scale of 1 to 3 as shown below with 1 being low and 3 being high;

Residential Market Opportunity			
Weighted Annual Uptake	**<1%**	**1-2%**	**>2%**
Points	1	2	3
Average Returns	**<10%**	**10-15%**	**>15%**
Points	1	2	3
Price to Land Multiplier	**<10X**	**10-20X**	**>20X**
Points	1	2	3
Availability of Development Land	**Low**	**Average**	**High**
Points	1	2	3
Infrastructure	**Poor**	**Average**	**Good**
Points	1	2	3
Distance from Main Business Nodes	**>25 km from Nbi CBD**	**16km-25km from Nbi CBD**	**Within 15km radius of Nbi CBD**
Points	1	2	3

Based on the criteria above, for detached units, Juja and Runda Mumwe were the highest ranking due to high uptake, returns and the availability of development land.

Top 5 Areas to Invest in Detached Units								
Location	**Weighted Annual Uptake**	**Returns Points**	**Distance from Main Business Nodes**	**Price to Land Multiple**	**Availability of Development Land**	**Infra-structure**	**Total Points**	**Rank**
Juja	3.0	3.0	1.0	2.0	3.0	1.0	2.3	1
Runda Mumwe	3.0	2.0	3.0	1.0	2.5	1.5	2.2	2
Athi River	3.0	1.0	1.0	2.0	3.0	1.0	2.0	3
Kitengela	2.0	2.0	1.0	2.0	3.0	1.0	1.9	4
Langata	1.5	3.0	3.0	1.0	1.0	2.0	1.8	5
Juja and Runda Mumwe are best areas to invest in detached units mainly due to high uptake, returns and the availability of development land. The main challenge with Juja, however, is infrastructure which may result in high costs for the developer.								

For apartments, Ridgeways and Kilimani were the highest ranked areas due to high uptake, returns and proximity to main business nodes.

Top 5 Areas to invest in Apartments								
Metrics	**Weighted Annual Uptake**	**Returns Points**	**Distance from Main Business Nodes**	**Price to Land Multiple**	**Availability of Development Land**	**Infra-structure**	**Total Points**	**Rank**
Ridgeways	3.0	3.0	3.0	2.0	2.5	2.5	2.7	1
Kilimani	2.0	3.0	3.0	2.0	2.0	3.0	2.6	2
Langata	2.0	3.0	3.0	2.0	1.0	2.5	2.4	3
Dagoretti	3.0	1.0	3.0	2.0	2.5	2.5	2.3	4
Westlands	1.5	2.0	3.0	1.0	2.0	3.5	2.2	5

Ridgeways and Kilimani are the best areas to invest in apartments mainly due to high uptake, returns, and proximity to main business nodes in Nairobi

Residential Sector Conclusion	
Measure	**Sentiment**
Factors influencing residential development	• The key drivers for the residential sector are mainly population growth, urbanisation, improved infrastructure and increased incomes as seen through economic growth with an average GDP growth rate of more than 5.0% over the last five years. New government incentives such as reduced taxes and scrapping of various fees is likely to spur development • The key challenges remain to be high land costs, high construction and infrastructural costs and access to financing hindering provision of affordable housing
Residential Sector Performance	• The average return in the residential sector is 9.4%. However, the best performing markets have returns of up to 19% which is high compared to returns from other asset classes such as the 10-Year treasury bond with a 12.3% yield
Residential Demand	• There is a housing deficit of approximately 1.9 mn units according to Cytonn Research • Residential demand is highest in the lower middle income segment of the market at 70.7%
Outlook	• We expect the market to stabilise from early 2018. However, there will be price stagnation in selected markets with surplus supply. Investors therefore need to invest in proper market research and trend analysis to identify specific market niches.
Opportunity	• For apartments, the best opportunity is investment in areas such as Ridgeways, Kilimani and Lang'ata driven by returns, uptake and state of infrastructure • For detached units, the best opportunity is in areas such as Juja and Runda Mumwe driven by uptake and the market returns to an investor

Conclusion

In conclusion, the residential sector performance in 2017 has been constrained by negative political sentiments as investors' preferred short term investments compared to long term investments such as real estate. In our view, however, the market is likely to recover given the opportunity in the residential segment with returns of up to 20% in the last 5-years. There still exists a huge opportunity in housing given the largest deficit in the market. The returns have remained attractive in some sub-markets and thus investors ought to carry out research to identify specific market niches.

For more on the residential sector market performance, see the full report here.