

Karen Investment Opportunity

[Amara Ridge](#), our exclusive development in Karen is nearly complete and the 10 houses are fully sold out. This week we thus revisit the Karen market to take note of any changes in the market and update the research note released in June 2015, [Karen Real Estate Investment Opportunity 2015](#). According to the research note, Karen offered an attractive investment opportunity for 4-5 bedroom bungalows with a price point of Kshs 75-115 mn and a rental yield of 5%. In this note, in addition to the rental yields covered then, we will include price appreciation, total returns and annualized uptake to give a better understanding of the performance of the market. We start with a brief introduction of Karen, the factors making it attractive for development, the performance of the residential real estate sector in the market and conclude with an investment recommendation for the Karen market.

Karen Market Research

Overview

Situated 12 km South West of the Nairobi CBD, Karen is one of the oldest and most affluent neighbourhoods in Nairobi. It was initially a purely residential zone and largely a white settler farm, but relaxation of zoning regulations has resulted in more commercial developments coming up in the area, the most notable ones being The Hub and Galleria Mall. Consequently, the real estate values have appreciated in the area making it attractive for developers and hence the area has witnessed increased development activity in the last 5-years. In addition to increased commercialisation, other factors that have made Karen an attractive area for real estate development include:

1. **Serene Environment** – With the continued relaxation of zoning regulations and increased development activity most high end areas are losing their appeal to high net worth individuals. Karen, located at the foothills of Ngong Hills and in close proximity to a number of forests including Ngong Sanctuary Forest and Ololua Forest has managed to maintain its serenity with plenty of green space and a country feeling attracting high net worth individuals.
2. **Improved Infrastructure** - such as roads which have greatly improved the accessibility of Karen. - The Southern Bypass opened in the second half of 2016 and Ngong Road currently in its second phase of its development that will see some feeder roads in Karen, such as Karen Road, also expanded,
3. **Relaxation of Zoning Regulations** – Initially a 5-acre zone, zoning regulations have been relaxed in Karen to allow for development on half acre land parcels thus increasing real estate activity and increasing property values. From our research, land prices in Karen have grown by a 5-year CAGR of 13.3% between 2011 and 2016,
4. **Recreational Facilities** – Karen has a unique historical heritage preserved in museums such as the Karen Blixen Museum. It also hosts the Bomas of Kenya, the Giraffe Manor, Karen Country Club and malls including The Hub and Galleria, making the place an ideal home for individuals seeking exclusivity, luxury and convenience.

Market Performance

In evaluating Karen Market performance, we will look at the following key metrics:

1. **Plinth Area:** Research on the size of the units found in the market allows us to gauge the current offering, and put into consideration the home buyer's preferences for sizes of houses

2. **Prices:** Research on prices will be used in comparison of the products in the market over a given time period and allow us to demonstrate capital appreciation
3. **Rental Rates:** Research on rental income allows us to inform potential investors on the current rental rates in other developments and also inform the investors on the rental yield they can gain from buying houses in Karen
4. **Annual Uptake:** This allows the investor to appreciate the rate at which available homes are sold over a specific period of time. This helps him or her gauge on whether it is profitable to invest in a given area.

The findings were as follows:

(all values in Kshs unless stated otherwise)

4 Bedroom Units Karen Performance Summary								
Name Of Development	Size of Unit (SQM)	Monthly Rent (Kshs.)	Current Selling Price (Kshs.)	Price per SQM	Annualized Uptake (%)	Rental Yield	Price Appreciation (%) y/y	Total Return
Bogani Park-type A	452	340,356	94m	207,964.6	24.0%	4.3%		4.3%
Belair	415	280,000	75m	180,722.9	35.0%	4.5%	7.1%	11.6%
Miotoni Heights	418	320,000	68m	162,679.4	100.0%	5.6%	4.6%	10.2%
Dik Dik Gardens	430	275,000	72m	167,441.9	7.7%	4.6%	15.2%	19.8%
Ivy Creek	409	300,000	57m	139,364.3	20.0%	6.3%	8.7%	15.0%
Bogani Park-type B	382	292,230	88m	230,366.5	13.0%	4.0%		4.0%
Eve's Garden	500	220,000	68m	136,000.0		3.9%	4.6%	8.5%
Fair Acres	375	250,125	73m	194,666.7	47.5%	4.1%	0.7%	4.8%
Average	423	284,714	74m	177,400.8	35.3%	4.7%	6.8%	9.8%
High	500	340356	94m	230,366.5	100.0%	6.3%	15.2%	19.8%
<i>Four bedroom units in Karen have an average rental yield of 4.7% with an average annual price appreciation of 6.8% and a total return to investor of on average 9.8%. The highest returns in achieved in the market are rental yields of 6.3% and a total return of 19.8% indicating that with the right product, the market has very attractive returns</i>								

Source: Cytonn Research June 2017

(all values in Kshs unless stated otherwise)

5 Bedroom Units Karen Performance Summary								
Name Of Development	Size of Unit (SQM)	Monthly Rent (Kshs)	Current Selling Price (Kshs)	Price per SQM	Annualized Uptake (%)	Rental Yield (%)	Price Appreciation (%) Y/Y	Total Returns
Amara Ridge	500	350,000	105m	210,000.0	33.3%	4.0%	10.5%	14.5%
Larkspur Villas	609	420,000	140m	229,885.1	100.0%	3.6%	16.7%	20.3%
Deer park	497	380,000	115m	231,388.3	50.0%	4.0%	20.0%	24.0%
Bogani Palms	743	400,000	130m	174,966.4	33.3%	3.7%	15.4%	19.1%
Bogani Park	515	350,000	100m	194,174.8	67.0%	4.2%	0.0%	4.2%
Muhugu Park	418	350,000	75m	179,425.8	22.5%	5.6%	9.0%	14.6%
SandalWood Waterfront	520	450,000	98m	188,461.5	16.7%	5.5%	10.8%	16.3%
Pergolla villas	250	250,000	85m	340,000.0	20.0%	3.5%	9.4%	12.9%
Tai Woods	250	320,000	64m	256,000.0	7.7%	6.0%	8.6%	14.6%
Marula Gardens	450	342,000	90m	200,000.0	4.6%	4.6%		4.6%
Windy Ridge	630	279,720	75m	119,047.6	29.7%	4.5%	0.9%	5.4%
The Paddocks	550	350,000	115m	209,090.9	20.0%	3.7%	0.0%	3.7%
Tipuana Gardens	500	350,000	90m	180,000.0	25.0%	4.7%	9.5%	14.2%
Average	495	353,209	99m	208,649.3	33.1%	4.4%	9.2%	12.9%
High	743	450,000	140m	340,000.0	100.0%	6.0%	20.0%	24.0%

5 bedroom residential units are the most common development type in Karen. They also have higher total returns of on average 12.9% compared to 4 bedroom units with total returns of on average 9.8%. This is attributable to the fact that most residents in Karen are high net worth individuals seeking larger spaces for convenience and are willing to pay a premium for the space. On average a 5-bedroom unit in Karen is 495 SQM large with an absolute selling price of Kshs 99mn and a high uptake rate of 33.1%. The highest returns achievable in the market are rental yields of 6.0%, a price appreciation of 20.0% and a total return of 24.0% and hence the market is still viable for real estate development

Source: Cytonn Research June 2017

Performance Summary and Recommendation;

Karen Market Performance Summary							
Typology	Size in SQM	Absolute Price	Monthly Rent	Price Per SQM	Rental Yield	Price Appreciation	Total Return
4 Bedroom Units	423	74m	284,713.9	177,400.8	4.7%	6.8%	9.8%
5 Bedroom Units	495	99m	353,209.2	208,649.3	4.4%	9.2%	12.9%
Average				193,025.0	4.5%	8.0%	11.4%
High				340,000.0	6.3%	20.0%	24.0%

On average the rental yield in Karen is 4.5%, 1.1% points lower than the market average of 5.6% and the price appreciation is 8.0%, 4.2% points higher than the market average of 3.8%. The above indicate that Karen is a buyers' market unlike the rest of the market with prices appreciating in 2017, higher than the market average and rental rates still remaining below the market average. Matching the right product to the right market and differentiating it through provision of amenities such as swimming pools and high quality finishes can result in high returns of up to 24.0%

Source: Cytonn Research June 2017



Conclusion

Despite the political headwinds that have affected the Kenyan real estate market, the performance of the Karen Market has been fairly stable recording above market returns. This can be attributed to the high property prices in this market and thus purchases are made with long term considerations and not for flipping typical in more affordable markets which witnessed reduced demand and thus significantly lower price appreciations. Karen is thus a viable market for development with the 5-bedroom unit being the ideal typology for development owing to the higher returns it offers. To get the highest returns however, the developer should differentiate their concept through provision of amenities such as swimming pools, club house and high quality finishes.