



KAREN REAL ESTATE INVESTMENT OPPORTUNITY 2017/2018

In September 28th 2015, we broke ground on [Amara Ridge](#), our exclusive, gated community in Karen, Nairobi. In line with good market practice, we have been updating the market research for the area and have since released research notes for the Karen Market in [2015](#) and [2017](#). As per the 2017 research note, on average, the Karen market had a total return of 11.4%, with an average rental yield of 4.6% and a price appreciation of 8.0%. The market however had pockets of value with total returns of up to 24.0%, for developments in prime locations, such as Miotoni, with high quality finishes, and amenities such as swimming pools and club houses. This week, we revisit the Karen Market to highlight and identify changes in the market between 2017 and 2018. In this note, we analyze market performance in terms of rental yields, price appreciation and total returns. We begin with an overview of the Karen market, the factors making it attractive for real estate development, the performance of the Karen Market in the first half of 2018 compared to performance in H1' 2017 and conclude with an outlook and hence investment recommendation for the area.

Karen Market Research

Overview

Karen is a high end neighborhood in Nairobi located approximately 12 Km South West of Nairobi CBD. It was a purely residential zone but relaxation of zoning regulations has seen an increase in commercial developments coming up in some areas, the most notable ones being The Hub Mall along Lang'ata Road and Galleria at the junction of Magadi and Lang'ata Road. Driven by the relaxation and increased development activities, the area has seen an increase in land values which have grown with a 6 – year Compounded Annual Growth Rate (CAGR) of 12.9% since 2011, from Kshs 25 mn per acre in 2011 to Kshs 52mn per acre in 2017, hence making it more attractive to investors.

Other factors that have made Karen an attractive zone for real estate development include:

1. **Serene Environment** –Karen is a serene neighborhood located at the foothills of Ngong Hills with numerous forest surrounding it including Oloolua Forest, and Ngong Sanctuary Forest creating plenty of green space attracting high net worth individuals seeking serene and exclusive neighborhoods for settlement,
2. **Improved Infrastructure** – The areas has witnessed an increase in infrastructural development especially roads such as the Southern Bypass and the expansion of Ngong Road which is still underway which have improved accessibility to the area making it more attractive to potential home owners,
3. **Recreational Facilities** – With facilities such as Bomas of Kenya, Karen Blixen Museum, Karen Country Club, the Giraffe Manor, The Hub, and Galleria Mall, Karen has created an ideal environment for residents seeking luxury, convenience and exclusivity,
4. **Relaxation of Zoning Regulations** – 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 with land value increasing from Kshs 25 mn per acre in 2011 to Kshs 52mn per acre in 2017 a 6 – year CAGR of 12.9%.



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 to 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,
5. **Rental Yield:** is a metric that indicates what an investor will generate annually if he rented the unit. A high rental yield shows that the investor will recoup his money faster,
6. **Capital Appreciation:** This is a metric that indicates the rate at which prices are increasing in the development or market. A high price appreciation shows that the prices of the development/ market are increasing quickly,
7. **Total Returns:** This is basically what the percentage of investment investor stands to gain from renting and selling the development. It is usually a summation of the rental yield and price appreciation.

The findings were as follows:

Performance of Karen between 2017 and 2018

In H1' 2018, the total return in Karen Area was 8.5%, with an average rental yield of 4.9% and an average capital appreciation of 3.5%. On average the total return declined by 2.9% points from the 11.4% average as at H1' 2017 and the capital appreciation declined by 4.5% points from the H1' 2017 average of 8.0%. The decline in performance is attributable to the spillover effects of extended electioneering period in 2017, that led to a decline in purchases as investors adopted a wait and see attitude.

In terms of performance by typology, 5 bedroom units had a better performance, recording on average a total return of 9.0%, a marginal 3.9% points decline from the 12.9% recorded in H1' 2017. 4 - bedroom detached units were the worst performing typology, recording on average a total return of 7.9% in H1' 2018, a 1.9% points decline from the 9.8% total return recorded in H1' 2017. The better performance of 5 bedroom units in the market is attributable to the fact that, Karen is mainly a home for high net worth individuals who prefer bigger houses hence more demand for 5 bedroom units.

(All Values in Kshs Unless Stated Otherwise)

Karen Residential Market Performance H1' 2018

Type	Unit Plinth Area (SM)	Price per SQM (2018) Kshs	Rent 2018 Kshs ("000")	Annual Sales 2018	Rental Yield 2018	Price App 2018	Total Return 2018	2017			Y/Y Δ				
								Price Per SQM	Rent	Rental Yield	Price App	Total Return	Rental Yield	Price APP	Total Returns
4 BR	456	174,035	325	22.7%	4.7%	3.2%	7.9%	177,401	284,714	4.7%	6.8%	9.8%	0.0%	(3.6%)	(1.9%)
5 BR	489	206,524	388	30.2%	5.0%	3.7%	9.0%	208,649	353,209	4.4%	9.2%	12.9%	0.6%	(5.5%)	(3.9%)
AVG	473	190,279	356	26.4%	4.9%	3.5%	8.5%	193,025	318,962	4.6%	8.0%	11.4%	0.3%	(4.5%)	(2.9%)

- The Karen Market has average rental yields of 4.9%, price appreciation of 3.5% and a total return of 8.5%, which is a decline of 2.9% points in total return from 11.4% recorded in H1' 2017
- The decline is attributed to the spillover effects of the 2017 double election which led to a decline in purchases as investors adopted a wait and see attitude
- 4 bedroom detached units have an average rental yield of 4.7% and price appreciation 3.2%, with total returns of 7.9%. This is a 1.9% points decline in from the 9.8% total return recorded in H1' 2017
- 5 bedroom apartments are the best performing typology with average rental yields of 5.0%, average price appreciation of 3.7% and average total returns 9.0%. The better performance of 5 bedroom units in the market is attributable to the fact that, Karen is mainly a home for high net worth individuals who prefer bigger houses hence more demand for 5 bedroom units

Source: Cytonn Research 2018

The performance of residential units in Karen is as summarized below;

Conclusion

The market recorded a decline in the performance with returns coming in at 8.5% in H1' 2018 compared to 11.4% in H1' 2017. The decline is largely attributed to the 2017 electioneering period that extended to the first half of 2018 slowing down purchase of units by investors and home owners. 5 bedroom detached recorded the highest returns of 9.0% as opposed to the 4 bedroom which came in at 7.9% total returns. The opportunity in the market therefore lies with 5 bedrooms which attracts high net worth individuals seeking large spaces and willing to pay the extra cost for it in the area. The best performing sub nodes are in Miotoni and areas around Windy Ridge where investor return can go to up to 16.5%, for 5 bed room units, with high quality finishes and amenities such as a club house and swimming pool. Therefore, a good combination of the right product to the right market through pricing and amenities will earn a developer high returns.