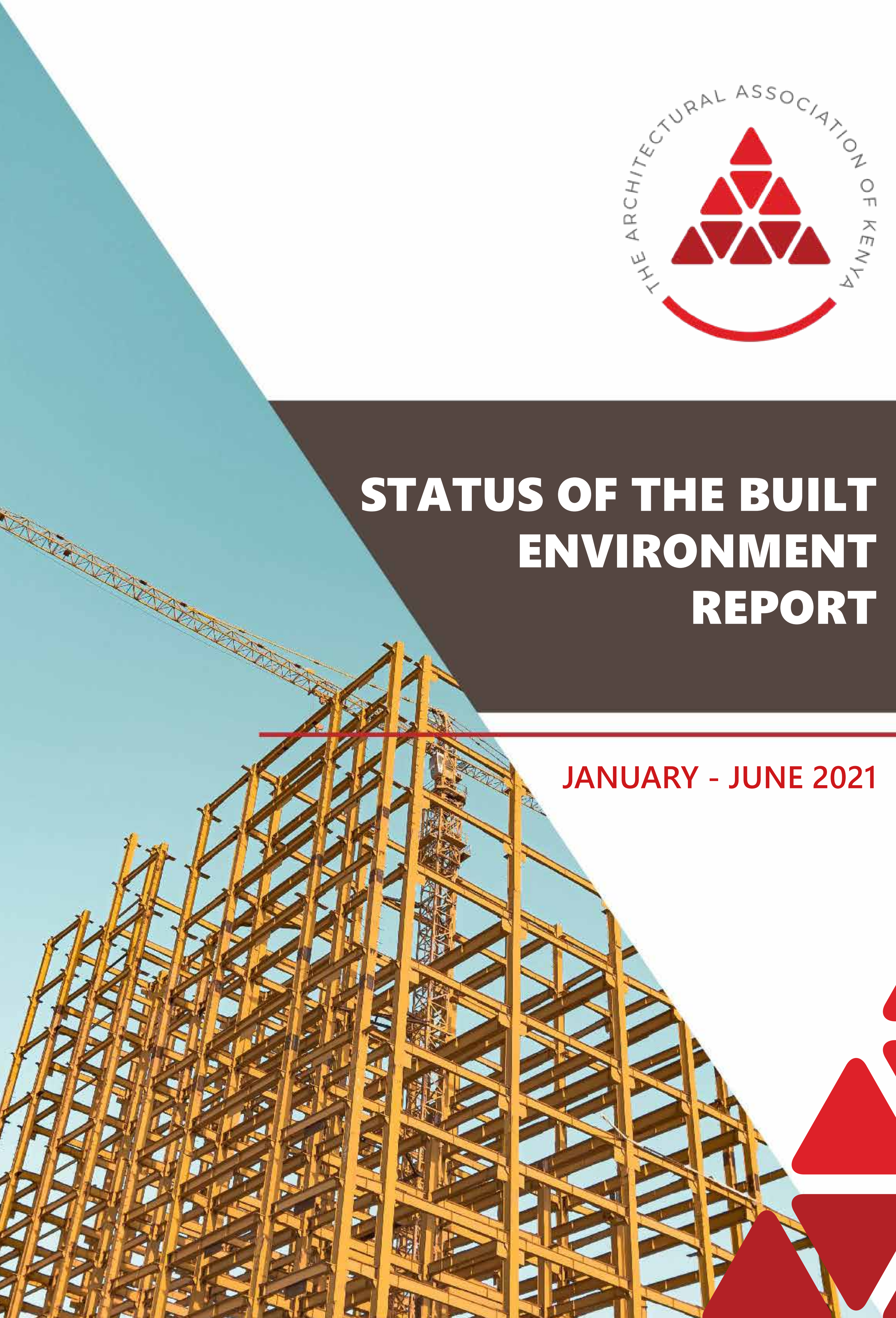
THE ARCHITECTURAL ASSOCIATION OF KENYA



STATUS OF THE BUILT ENVIRONMENT REPORT

JANUARY - JUNE 2021

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Introduction

The Covid-19 pandemic has made the underlying structure and resilience of African financial markets a more important matter for domestic and international investors, as the continent copes with the challenges of returning to sustainable growth.

In Kenya, the Kenya National Bureau of Statistics (KNBS) reported that the country's economy had contracted by 1.1% in the third quarter of 2020 compared to a 5.8% growth over the same period in 2019. The drastic decline was mainly attributed to the on-going impact of the COVID-19 pandemic and various mitigation measures put in place which affected activities across majority of sectors of the economy. These included accommodation and food services; tourism; transport and storage and education. Consequently, the economy was projected to contract to -1% for 2020 but rebound to 6.9% in 2021.

In 2021, the construction industry is expected to improve, assuming a slowdown in COVID-19 cases and recovery in the global economy.

The AAK believes that the construction industry may grow by up to 3.9% this year. This growth will be driven by a sharp recovery in output levels compared to periods when works were not permitted or were severely restricted in 2020, with Q2 2021 in particular recording high growth Year-on-Year, assuming there is no repeat of the strict lockdown similar to last year. Importantly, we project that the growth will particularly propelled by huge infrastructural investments by the Government of Kenya. More noticeably, the on-going construction of the Nairobi Expressway, the Lamu Port under LAPSSET and the dueling of the Nairobi-Mombasa Highway as well as the implementation of the affordable housing agenda will play a critical role in the recovery of the sector. Important to however is that the growth of the real estate and construction sectors will be pegged on the overall performance of the economy. The contraction in the country's economy was also felt in the built environment. Presently, the Treasury has projected that Kenya's GDP will grow by 7% in 2021.

economy contracted by

1.1%

construction industry may grow by

3.9%

Treasury has project GDP growth of

7%

01

Real Estate

Residential

The residential sector in real estate has continued to record improved performance, as the retail and commercial spaces continues to record a decline, if the Cytonn Q1'2021 markets review is anything to go by. According to the report, the residential sector recorded an improvement in performance with average total returns to investors coming in at 5.1% year on year, up from 4.7% recorded in FY'2020.

The improved performance was also realized in the apartments market which recorded average total returns of 5.3% year on year compared to the detached units which recorded average total returns of 4.8%. Detached units in areas such as Rosslyn, Ruiru and Kitisuru recorded the highest average year on year returns at 6.7%, 6.3% and 5.9 %, respectively. Apartments in Westlands, and, South C which traditionally house Nairobi's city's middle income earners, recorded the highest average y/y total returns of 6.8% and 6.5% respectively.

The 2021 Q'1 Market Review by Cytonn revelaed that Gigiri and Karen were the best performing submarkets recording average rental yields of 8.3% and 8.0 %, respectively. This may be attributed to their superior locations, availability of high quality office spaces charging prime rental prices, relatively good infrastructure, and low supply of commercial office spaces within the markets.

5.5% Average Total Returns Year on Year

Best Performing Submarkets:

Gigiri & Karen

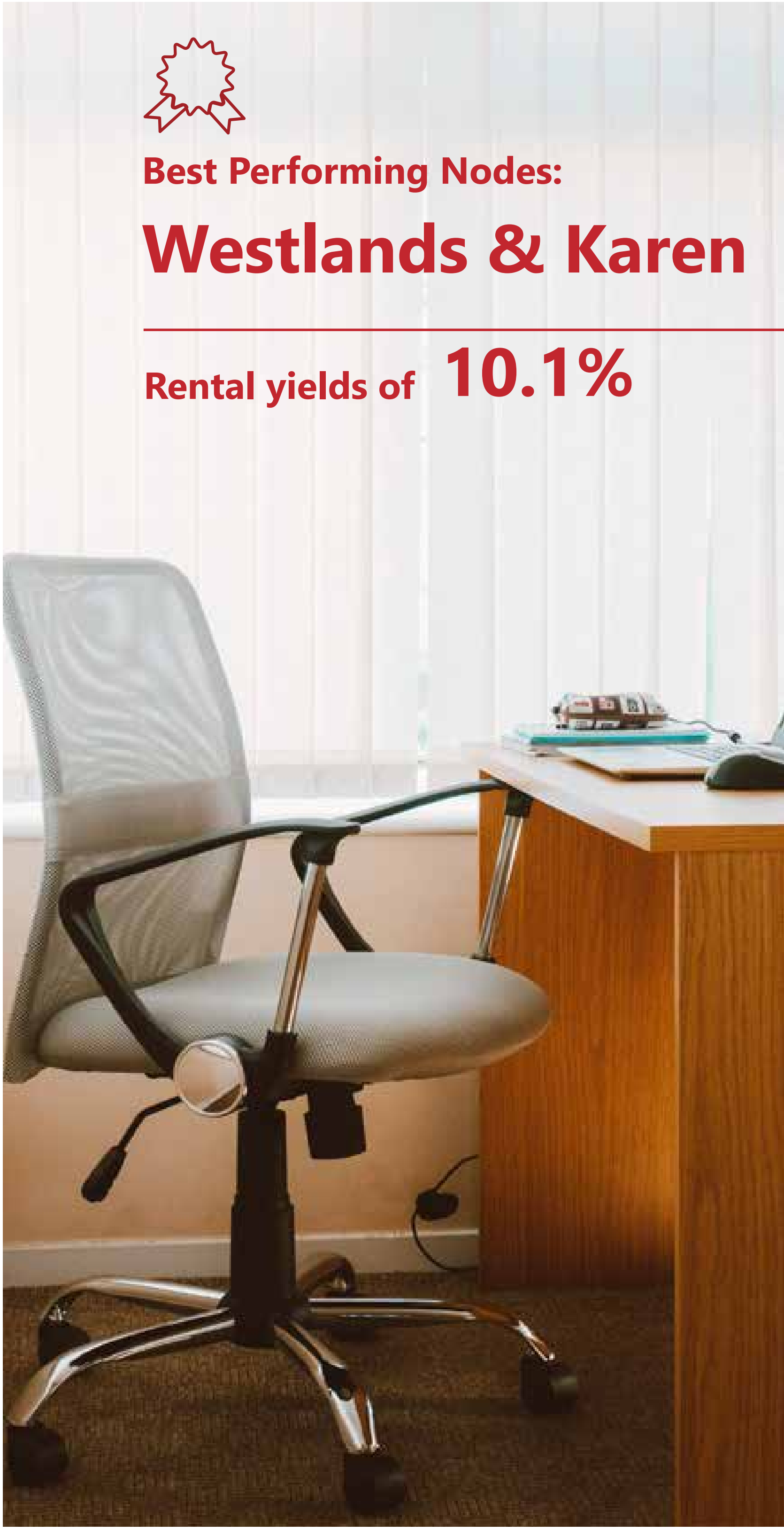
Commercial

In the retail sector, Westlands and Karen were the best performing nodes in the first Quarter of 2021 recording average rental yields of 10.1 % compared to the overall market average of 7.4 %. The performance is attributed to presence of affluent residents who have a high consumer purchasing power with the areas hosting high end income earners, the ease of access to the areas, and, relatively high occupancy rates of above 81% against the market average of 74.9 %.

On the other hand, the average rental yield in the commercial office sector is expected to decline to 6.8% from 7.0% in 2020, attributable to the oversupply, with the average occupancy rates expected to decline by 2.7 percentage points from 77.7 % to 75.0 %. The subdued performance comes with reduced demand in the office spaces as businesses scale down due to financial constrains while others adopt the working from home strategy.

Listed real estate is also expected continue performing poorly in 2021 with the Fahari I-Reit having opened the year at a relatively low trading price of Sh5.8 per share. This is coupled with the expected negative performance of the office sector and lack of investor appetite in the instrument due to negative investor sentiments.

All in all, there are still viable investment opportunities in areas such as Karen, Gigiri and Westlands, which continue to have relatively high returns compared to the market averages.



Industrial

The industrial market is the cream of the crop due to its few speculative developments, low vacancies and recovering rental growth. In the first quarter of 2021 nominal rentals for prime space of 500 m^2 on a national level grew by 1% year on year. This is better than the 0.5% growth achieved in 2020, but still well below the 5% rental growth of 2019. The slow rental growth shows that the industrial market is also feeling the effect of the weak economy, although accompanied by less pain than the office and retail property markets.

The above notwithstanding, an April 2021 report by Cytonn revealed that Kenya's industrial real estate sector is undergoing a transformation with the traditional design of warehouses giving way to modern ones that are located in more convenient locations. Consumer preference has now seen demand increase for industrial places in areas perceived to be more 'serene' as compared to the 'congested' Industrial Area, Baba Dogo and Mombasa Road areas in Nairobi where most of the country's old warehouses are located.

To meet the changing demand, developers of industrial parks are now moving to areas within Nairobi's periphery such as Kiambu and Machakos counties where they are easily accessible and are still in close proximity to key airport and railway termini as well as the Nairobi CBD. Some of the modern industrial parks include the Tatu Industrial Park which is located in Ruiru and Infinity located along the Eastern Bypass as well as Tilisi is located in Limuru, Kiambu County.

The said trends are further corroborated by findings in the Knight Frank Africa Report 2021/22 which indicated that a continued steady supply of grade A warehousing will push prices downwards in the poorly located grade B warehouses which still make up a majority of the stock in the country.

Hospitality

Kenya's hospitality industry has continued to experience low performance with business in the hotel industry reporting lower than normal forward bookings for instance. Traffic from international visitors also went down due to resurgence in Covid-19 infections in Europe and the United Kingdom during the Quarter 1 of 2021.

In a January 2021 study commissioned by the Central Bank of Kenya's MPC, 36 % of respondents noted that the resurgence in infections in Europe and UK had affected their business operations since they form a significant part of their clientele. Only 19% of those interviewed, particularly the small hotels, indicated that the rising infections in Europe have no impact on their hotel operations.

From the study, it was recommended that the government being a key consumer of the hospitality industry services in terms of conferences and should augment the same by offering subsidies, tax holidays (waivers), and suspension of levies during the period of the pandemic.

02

Infrastructure

Lamu Port-South Sudan Ethiopia Transport Corridor (Lapsset) Project

As the region looks forward to the commencement of works on proposed joint Uganda, Tanzania East African Crude Oil Pipeline (EACOP), Kenya's $1.5 billion Lokichar to Lamu Crude Oil Pipeline under the Lamu Port-South Sudan Ethiopia Transport Corridor (Lapsset) project is in progress and currently, the environmental social impact assessment report on the project is undergoing public participation.

Further, Kenya's long-awaited Lamu Port which is also part of LAPSSET is set to become operational between June and July 2021. While there is optimism that the port will bring about the renewal of Lamu, there are concerns about the degree of connectivity between the county and the rest of the country. The corridor itself is expected to have roads, rail and pipelines connecting the port to the hinterland, going as deep into the region as South Sudan and Addis Ababa.

Nairobi Expressway

Construction of the 27.1km highway dubbed the Nairobi Expressway starting from Mlolongo through Uhuru Highway and terminating at the James Gichuru in Westlands is expected be completed in December 2021. Construction of the expressway began in October 2019 and was expected to be completed and opened for traffic early next year.

According to the Ministry of Transport, Housing and Urban Development, the Nairobi Expressway will provide a critical link with the Northern Corridor which is the main gateway for exports and imports to and from the port of Mombasa to the landlocked neighbours of Uganda, Rwanda, Burundi, South and eastern DRC. The Ministry also projects that the new highway which is currently over 40% complete will also carry about 85%of all cargo and commuter traffic for the highly built areas of Athi River, Kitengela, Mlolongo, Syokimau, Utawala, Embakasi, South B and South C, and surrounding areas.

The concessionaire, China Roads and Bridge Corporation (CRBC), is responsible for designing, financing and building the expressway, and will maintain and operate it during the concession period. During this period, CRBC will also collect toll charges from motorists who choose to use the elevated highway.The concessionaire will then transfer the road to the Government at the end of the30-year concession period.

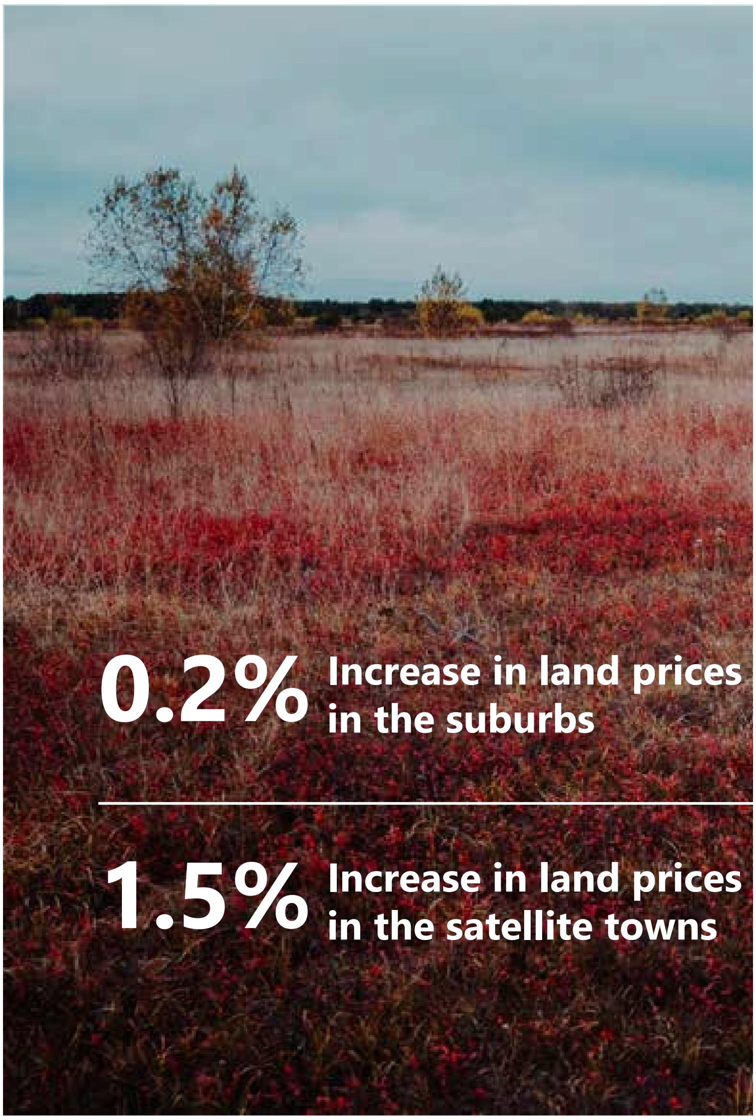
An off-the-cuff calculation indicates that CRBC is set to pocket Sh106.8 billion as profit during the said period.

Once complete, the Nairobi Expressway is expected to have a four-lane dual carriageway from Mlolongo to the Eastern Bypass and a six-lane dual carriageway from the Eastern Bypass to the Southern Bypass. The highway will also comprise of a four-lane dual carriageway from the Southern Bypass to St Mark's Church in Westlands and a four-lane dual carriageway from St Mark's Church to James Gichuru Road. With a total of nine stations spread aross the 27.1km stretch, the expressway will also have interchanges at Mlolongo, Syokimau, JKIA, Eastern Bypass, Southern Bypass, Capital Centre, Haile Selassie, Museum Hill, Westlands, and the Mainline station at the endpoint—St Mark's/Lion Place. There will also be a roundabout at the junction of Enterprise Road and Mombasa Road, and another at the junction of James Gichuru and Red Hill Link Road.

03

Land

Despite the ravaging effects of the COVID-19 Pandemic, the overall land prices in the suburbs posted a modest 0.2% increase over the first quarter of 2021 while the satellite towns saw a 1.5% rise. In Nairobi's commercial zones a report by Hass Consult revealed that prices of land in the areas dampened as low offices space demand has added to an already existing glut. Similarly, Riverside suburb which is characterized by a high density of office space recorded the biggest drops in land prices at 1.68% over the first quarter of 2021 and is expected to decline by up to 7.1 % over the year. Ngong led the satellite towns with prices of land increasing by 6.07% over the first quarter of the year and 16.04% annually. In Kiambu land prices recorded a 2% drop over the quarter with the annual decline expected to be 12.6 %. Nyari was the best performing suburb over the first quarter with land prices increasing by 2.2% while annually Donholm topped at 3.7%.



National Land Information Management System (NLIMS)

In line with the Vision 2030 Agenda, the President of Kenya Uhuru Kenyatta on 27th April 2021 launched the National Land Information Management System (NLIMS) dubbed ArdhiSasa under an initiative by the Ministry of Lands and Physical Planning, with support from the Food and Agriculture Organization and the European Union. From 2018, the initiative embarked on a comprehensive programme to digitize all the land records in the country and establish the land management system. The launch is founded on the provisions of the Land Act, 2012 and the Land Registration (Electronic Transactions) Regulations, 2020, which provide for the development and implementation of an electronic National Land Information System in collaboration with the National Land Commission.

This intervention will focus in establishing a transparent, decentralized, affordable and efficient GIS based Land Information Management System. This will contribute to poverty reduction, good governance and improved security of tenure. In addition, the system will enhance efficiency and effectiveness in the delivery of services for all Kenyans, especially the poor. Further, the system will enable the capture, management and analysis of geographically referenced land-related data in order to produce land information for decision-making in land administration and management. The platform provides complete details of the parcel of land from the original owner, period of ownership, year of purchase to number of transactions to the current status of land, the revenue officials need to collect as well as the image of the land/property. For records on land availability, a fresh survey of lands was conducted and every parcel of land counted and details noted. The digitization process began. Digitization of land records ensured requisite details - map of the land, mutation and photo ID, among others – a step towards conclusive ownership.

04

Financing

The Central Bank of Kenya acting as a fiscal agent for the Kenyan republic recently invited bids for an 18-Year Amortized Bond Issue No.IFB1/2021/18 with a total value of Kshs.60 Billion. The infrastructure Bond whose coupon rate will be market determined is expected to be used for funding of Infrastructure projects in the FY 2020/21 budget estimates. The Bond will be tax free as is the case for infrastructure Bonds as provided for under the income Tax Act. In January, the CBK also invited members of the public to bid on another infrastructure bond amounting to Kshs.50 Billion valid for a period of 16 years with the minimum investment being capped at Kshs.100,000.

In a bid to enhance realization of the Affordable Housing Agenda, the Kenya Mortgage Refinance Company (KMRC) is expected to issue a bond by October 2021 to raise additional financing for low-cost housing. The company will also issue a bond to finance climate-friendly housing projects. For the 2021-22 financial years, the Government of Kenya allocated a total of Kshs. 11.5 B to KMRC for purposes of implementation of the Kenya Affordable Housing Project managed by.

Of this, Sh8 billion will go to the affordable housing project and Sh3.5 to operationalise the company. The KMRC has made significant progress since it was launched given that as at December 2020, KMRC had refinanced 1,400 affordable housing loans worth Ksh2.75 billion.

In seeking to spur increased investements in the Manufacturing Sector, the government set aside Sh20.5 billion for the promotion of local industries through various ministries in its 2021-2022 Financial Budge. The allocation included Sh8.3 billion allocated to the Dongo Kundu SEZ, Sh1.4 billion to the Kenya Industry and Entrepreneurship Project and Sh448 million to the Kenya Industrial Research Laboratories. Others that received cash injections through the budget included the Naivasha Industrial Park, Kisumu SEZ in Miwani, Naivasha Textile Park and Athi River Textile Hub.

05

Affordable Housing

The construction of 600 houses in Nakuru, under the ambitious Affordable Housing Project was recently launched in May 2021. The World Bank last year selected Nakuru as the pioneer county for the realization of the ambitious half a million houses project by 2022. The multilateral lender said Nakuru had most of the critical infrastructure needed for the construction. The construction of the 600 houses comes at a time when demand for housing in Nakuru is rising following its elevation to city status even as local steel and cement manufacturers, animal feeds makers and dairy industries companies continue to set up shop at the Salgaa industrial zone. Several local and foreign investors have also expressed interest in setting up manufacturing concerns at the new industrial zone within Rongai Sub-County.

Naivasha has also attracted both local and foreign investors in the industrial sector. Besides Standard Gauge Railway that is linked to the Meter Gauge Railway at Mai Mahiu, the Inland dry port, a business park being established by Kenya Electricity Generating Company (KenGen) and an Industrial park set up by Oserian Company are also expected to draw firms.

The affordable housing project in Nakuru will be built on a 10 acre-land in Bondeni Estate within Nakuru Town East Sub-County while those within Naivasha are being constructed on a 55-acre parcel of land along the Nairobi-Nakuru highway near GK Prisons.

The United Nations Project Services (Unops) recently released Sh1 Billion to enable urban housing living units to make owning a house – a reality for all. The project is aiming to rope in other development partners who are expected to raise sh6.47 billion into planning 100,000 housing units across Kenya. The initiative advanced by UNOPS aims to reduce the investment risks of development activities, in order to bring about new partnerships between the private and public sectors. The knock-on effect means unlocking new opportunities and providing jobs for local communities, which all helps drive progress towards the SDGs.

The affordable housing agenda also received a boost following the formulation of a joint strategy for the Network in Kenya by FSD Kenya. The strategy which will encompass FSD Kenya, FSD Africa and FSD Africa Investments as developed with the support of the Centre of Affordable Housing Finance in Africa (CAHF).

The strategy was developed using the Housing Value Chain framework – and critically evaluated the failures experienced at each component from land, title, infrastructure, construction, off take, maintenance, and social and economic infrastructure for four housing typologies namely: incremental housing, informal settlements, small landlord and formal housing – which are generic to most of Africa. In preparation of the strategy, it was reported that while the Kenyan housing landscape offers a breadth of opportunities, the potential for scale is not being realized. The success of the "housing unit delivery" is often less than expected, and while important, finance is often not the key limiting factor.

Accordingly, there is recognition from all stakeholders that more attention needs to be given to the length and complexity of the entire housing value chain, and how finance; on the ground skills and regulatory frameworks need to be brought even closer together at every single component of each value chain, to enable the broader market transformation that is desired.

Shelter Afrique's Strategies on Enhancing Affordable Housing Delivery across Africa

Defining a sustainable and long-term approach remains crucial for business and economic recovery; particularly in the face of the COVID-19 pandemic. For a Pan African Housing Finance Institution such as Shelter Afrique, delivering projects which have an impact remains a crucial goal/measure of performance as it relates to our mandate of 'Delivering Affordable Housing for all Africans'.

Cumulatively, Shelter Afrique has delivered an estimated 22,673 units, housing 113, 365 people. Beyond the aforementioned, Shelter Afrique has engaged in a number of initiatives including its partnership with International Finance Corporation (IFC) Excellence in Design for Greater Efficiencies (EDGE) to ensure increased delivery of green housing across Africa. In line with this, Shelter Afrique recently held a joint EDGE Developers Workshop with IFC aimed at increasing awareness and knowledge of the partnership and certification. In the context of Shelter Afrique's commitment to championing the delivery of Green Affordable Housing Delivery in Africa, Shelter Afrique is committed to the delivery of 4,416 EDGE Compliant affordable housing units across Africa, in line with its 2021-2025 corporate strategy.

Every year, Shelter Afrique hosts its Annual General Meetings. The 40th AGM of Shelter Afrique was held in Yaoundé, Cameroon from the 21st to the 25th of June 2021. The AGM included a roundtable of African Housing and Finance Ministers and a symposium, which gathered together policy makers and key actors in the housing and built environment space to discuss relevant and topical issues as they relate to affordable housing delivery across the continent.
The symposium sessions were delivered by top experts from the UN-Habitat, UN Economic Commission for Africa (ECA), World Bank, amongst others. The Shelter Afrique Awards which recognized the contributions of innovative organisations and projects in the built environment across Africa was also held.

The Outgoing AGM Bureau Chair, Hon James Macharia, the Cabinet Secretary for Transport, Infrastructure, Housing, Urban Development and Public Works, Kenya

The theme of this year's AGM Symposium, **'Four Decades of Housing Policies in Africa: Mapping the Next Forty Years'** provided us with the opportunity to review the policy environment in Africa and more importantly, to forecast the next forty years to shape policy for our member states. The COVID-19 pandemic has in many ways brough to the fore, the need for urgency in attending to housing - both in terms of quantity and quality - as well as the need to create more liveable and sustainable communities as indicated in Sustainable Development Goal (SDG)11.

The Incoming AGM Bureau Chair, Hon Celestine Ketcha Courtes, Minister of Housing and Urban Development, Cameroon (second from right on high table)

The Yaoundé Declaration, an outcome of the 40th AGM of Shelter Afrique details the approach of the organization, Shelter Afrique, African Ministers and Heads of Delegation of Ministries in charge of Housing and Urban Development, African Finance Ministers, and other related stakeholders with regards to enhancing the mechanisms of mass production of decent, sustainable and affordable housing in the continent to achieve social and economic development. The Yaoundé declaration rests on the recognition of the importance of the SDGs, the African Union Commission's Agenda 2063, and the need to accelerate the reduction of the deficit of decent affordable housing in Africa.

Managing Director, Shelter Afrique, H.E Andrew Chimphondah at the Opening Ceremony of the 40th AGM

The declaration focuses on enhancing leadership and governance across Africa, as well as policy and legislation with regards to attending to housing and built environment challenges across the continent. Similarly, the need to enhance land reforms and also the role of finance and taxation, capacity building, development practices were also highlighted as focus areas in truly realizing Africa's development goals.

Image of attendees at the 40th AGM Roundtable Session of African Housing and Finance Ministers

06

Investor and Developer Scene

Safari Green Building Index

The Architectural Association of Kenya (AAK) has developed a national green building certification tool which is aimed to assess projects in the local built setting to establish their environmental performance.

Dubbed Safari Green Building Index, the ratings system that will be unveiled in August during the AAK Annual Convention 2021 is expected to improve the number of green buildings in Kenya by encouraging investors to build sustainable structures. The rating tool has been designed by the Environmental Design Consultants (EDC) chapter of AAK in partnership with the University of Nairobi and UN-Habitat.

The Safari Green Building Index is suitable for all kinds of buildings in climatic zones in Kenya and is applicable in other East African countries. The tool is intended to covers several areas among them water conservation, energy conservation, planning areas, design areas, innovation, use of local materials and structures with historical value. Also known as certification, green building rating tools is used to evaluate and recognize buildings that meet certain green standards. The rating tools, which are often voluntary, recognize and reward organizations that build sustainable buildings, thus incentivizing the adoption of green construction.

Fluctuations in Steel Prices Affecting the Construction Industry

The disruptions from the COVID-19 pandemic and related interventions have resulted to the cost of steel prices subsequently affecting the country's construction industry. The construction industry heavily relies on steel production with the same being used for such functions as installation of reinforcing bars, manufacturing of heating and cooling equipment as well as internal fixture and fittings. The rise in cost of steel in Kenya has been attributed to the stringent COVID-19 restrictions measures undertaken for the better part of 2020 with manufacturers being forced to shut down operations. The rise has also been attributed to the high demand for steel amid low global supply thereby resulting to prices of construction metals shooting up by up to 25 per cent in Kenya with a kilogramme currently selling at Ksh.125 up from Ksh.85 in December 2020.

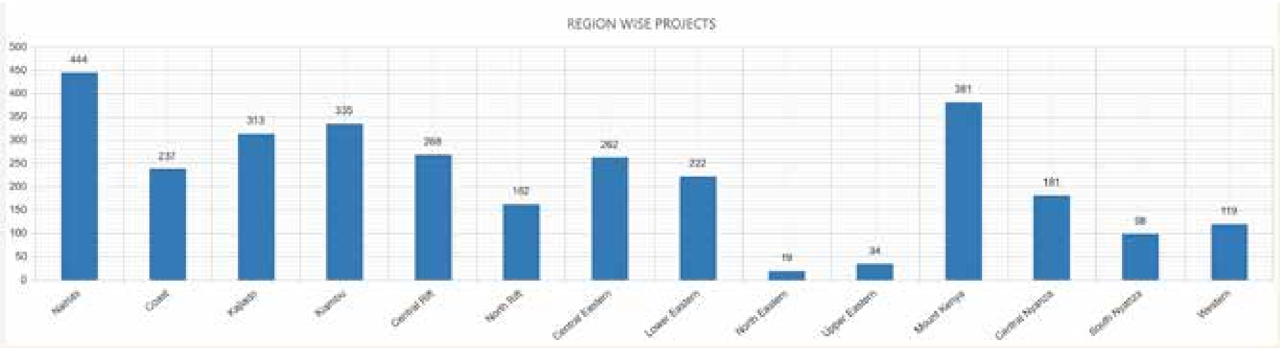
Globally, data from London Metal Exchange, the centre for industrial metals trading, shows that the prices of steel bar escalated from Ksh.40,000 a tonne in April 2020 to over Ksh. 80,000 in May 2021. The price fluctuation is especially expected to affect building contractors with fixed-sum contracts who cannot apply for variation in contract prices under their contracts. In fixed-sum contracts, contractors are expected to adhere to their program of works and cannot apply for any price variations.

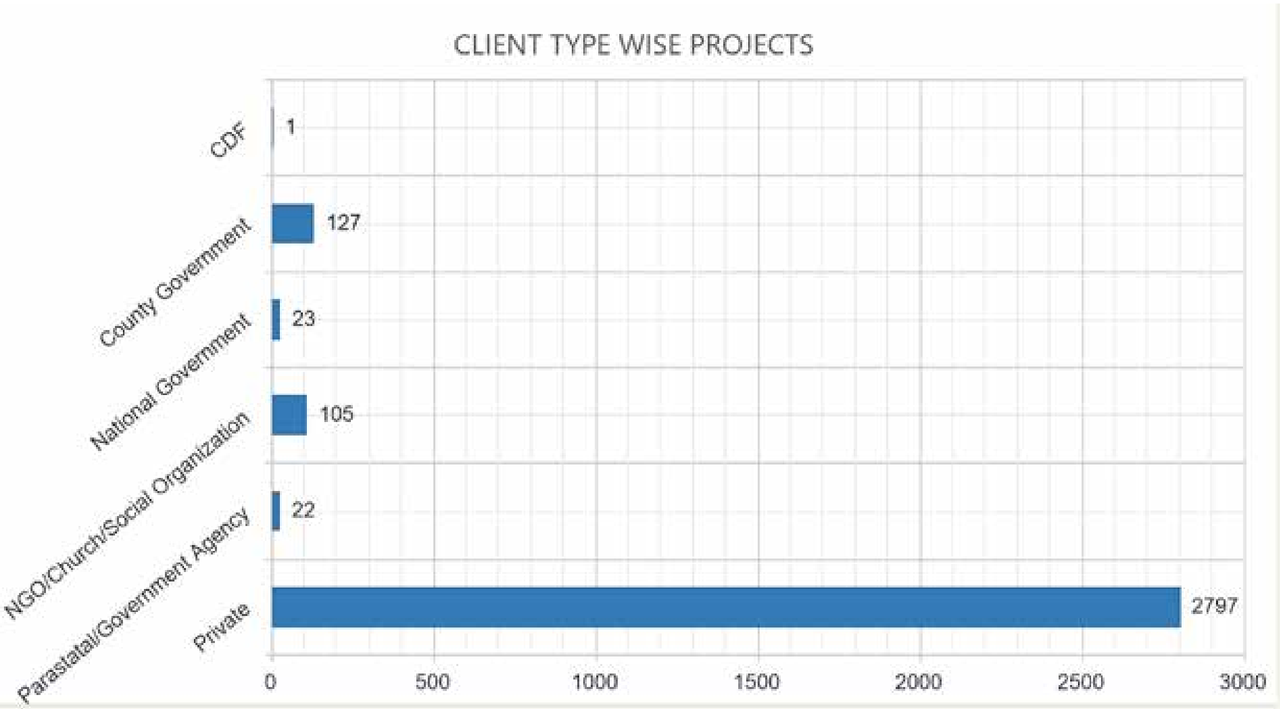
A recent report by Fitch Ratings however indicated that the recent global rise in steel prices will be short-lived, with prices starting to decline towards the end of Q1 2021 as steelmaking production continues to be restarted.

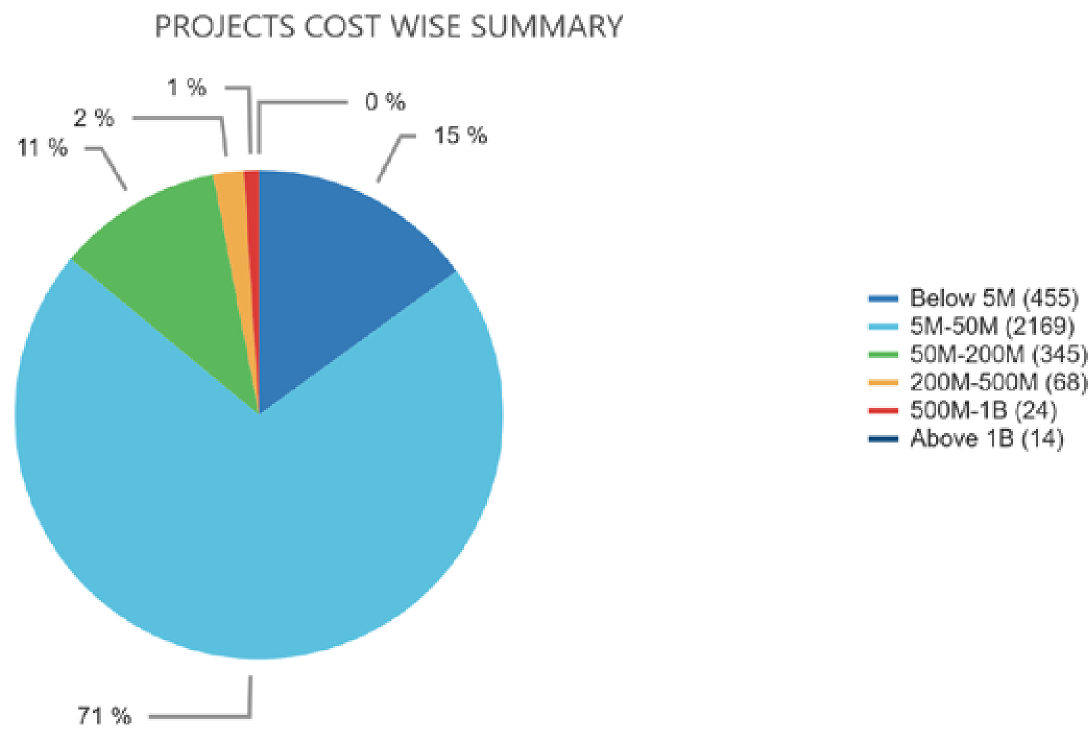
07

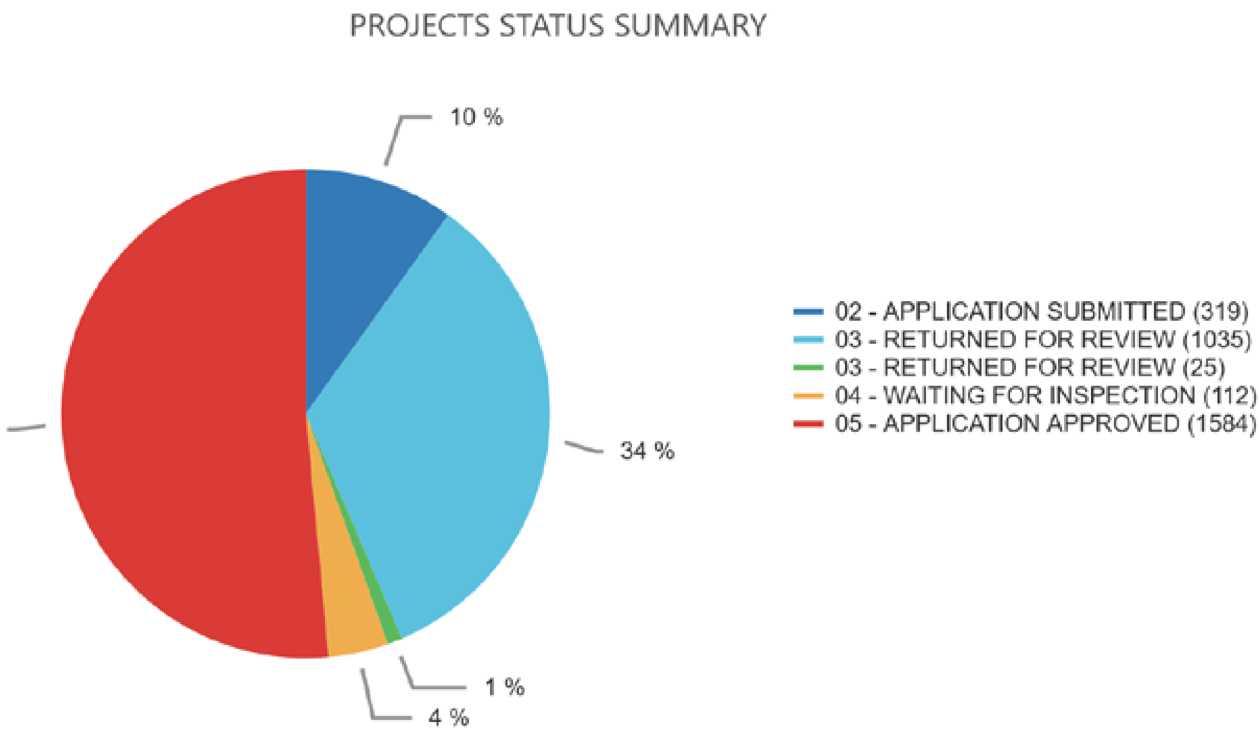
Development Control

National Construction Authority






PROJECTS COST WISE SUMMARY
1 %
0 %
2 %
15 %
11 %
71 %
Below 5M (455)
5M-50M (2169)
50M-200M (345)
200M-500M (68)
500M-1B (24)
Above 1B (14)


PROJECTS STATUS SUMMARY
10 %
34 %
1 %
4 %
02 - APPLICATION SUBMITTED (319)
03 - RETURNED FOR REVIEW (1035)
03 - RETURNED FOR REVIEW (25)
04 - WAITING FOR INSPECTION (112)
05 - APPLICATION APPROVED (1584)

08

Moving Forward

Construction Industry

We forecast Kenya's construction industry growth to accelerate to 4.5% year-on-year (real terms) in 2021 as the sector recovers from the negative impact of the COVID-19 pandemic. While this puts Kenya in line with the 2021 Sub-Saharan African average of 4.4% y-o-y for construction industry growth, the country will not be able to recover its pre-COVID growth rate. Kenya's construction industry's short-term recovery will be supported by a quick return of private investment in the country's residential and non-residential construction sector. In the medium term, we project a gradual acceleration of growth, supported by a number of large-scale road and related infrastructure projects, for which construction is likely to begin in 2022 and which will inject renewed momentum in the Kenyan transport infrastructure sector following the end of works on the Standard Gauge Railway Project in 2020.

Nonetheless, a gradual shift towards more financially sustainable infrastructure projects, contrasting with expensive bilateral debt-funded projects, such as the Standard Gauge Railway, will put downward pressure on long-term growth rates.

Real Estate Market

After the worst economic downturn in decades, further dampened by the recent tightening of lockdown restrictions in response to the second wave of the pandemic and the recommencement of load shedding, economic growth - while admittedly coming off a low base - is still widely expected to show some positive growth of around 6.9% of the Gross Domestic Product (GDP) expected this year.

Coupled with this, a number of factors are expected to continue to underpin current activity in the housing market. These include interest rates which are likely to remain at near-record lows this year, an ongoing large number of potential first-time buyers (many of whom were previously tenants but are now able to afford to purchase a property at current low interest rates) eager to gain a foothold on the property ladder, and financial institutions with a continued appetite to extend mortgages to home buyers.

That said, the continued effects of COVID-19 and the resulting restrictions potentially threaten the strength of the anticipated economic recovery, which is likely to result in an increase in our already high levels of unemployment, while rising oil prices are expected to see a significant increase in the fuel price in the coming days and possibly thereafter - thereby creating likely inflationary impacts.

Realistically, the robust pace of residential property activity seen during the latter part of 2020 and 2021 as lockdown restrictions were eased, while currently ongoing, is unlikely to be sustained throughout 2021. In part this reflects the fact that some of that activity was due to pent-up demand created during the initial lockdown, while other buyers were responding to the aggressive interest rate cuts.

Nonetheless, the structural changes in lifestyle choices triggered by the repeated lockdowns, combined with the stable, low interest rates, suggest there will still be areas of robust activity. We project that the sector will continue to experience consistently busy activity in the price bands not only below but also from Kshs. 10 million upwards, including the luxury market in excess of 100 million. For middle income earners, the investment opportunity for apartments lies in satellite towns such as Thindigua and Syokimau, as well as the upper mid-end segment in areas such as Riverside and Kilimani. For detached units, potential home owners have the opportunity to actualize their dream by investing in areas such as Rosslyn, Ridgeways and Ruiru. Accordingly, our outlook for the Real Estate Sector in 2021 is NEUTRAL with a bias to positive based on the fact that the containment of the COVID-19 pandemic through the expected mass vaccination will spur economic approach and have investors move from the Wait& See Approach that has been the case since 2020.

Residential

Forecasting the likely level of activity in the local residential property market this year is unusually difficult. Areas which offer affordably priced homes - and an appealing lifestyle - are likely to prove most resilient in 2021. The enactment of the Sectional Properties Act 2020 during the course of last year fundamentally altered the apartment housing market in that it made homeownership accessible to many first-time buyers for the first time and also made ownership a viable option for many aspirant buyers who previously thought they could only afford to rent.

This would suggest that sectional title homes in traditionally expensive neighborhoods in Nairobi, as well as freehold homes in the secondary cities will prove to be more resilient and the ones that remain relatively affordable during tough economic times.

Initially, these areas, which include suburbs on the periphery of major towns, should remain resilient. However, if there is a renewed wave of conversions of commercial property to well-located sectional title units in relatively affordable price bands, this could see an influx of homeowners or tenants to business nodes - quite possibly leaning towards younger and less affluent buyers.

Furthermore, since property is an immoveable asset, these structural shifts in lifestyle are likely to result in excess stock supply in some areas and a shortage and development potential in others. In light of the above, our 2021 outlook for the residential market is NEUTRAL with a bias to a positive performance particularly due to the increased appetite for home ownership among the middle class.

Commercial

Our 2021 outlook for the commercial office segment of the real estate sector is NEGATIVE. An office market survey by the Architectural Association of Kenya (AAK) for the first Quarter of 2021 indicates that the worst fears have come true for landlords, with market rentals dropping further due to a swelling oversupply as many organizations and companies continue to have their employees work away from the office. Therefore, in 2021, we expect a continued subdued performance in office sector attributable to the existing oversupply of 6.3 million SQFT as of 2020, the reduced demand of commercial office space as firms downsize and adopt the work from home initiative and reduced rental rates as property managers offer discounts and concessions to retain and attract clients.

Further, we project that in the next few years, the commercial segment of the real estate sector will continue to see low construction of new office spaces and a sharp rise in the conversion of older office spaces-where financially feasible. The same implies that green shoots are likely to emerge from a supply perspective in the near future but strong growth demand but just be the key to helping the sector regenerate.

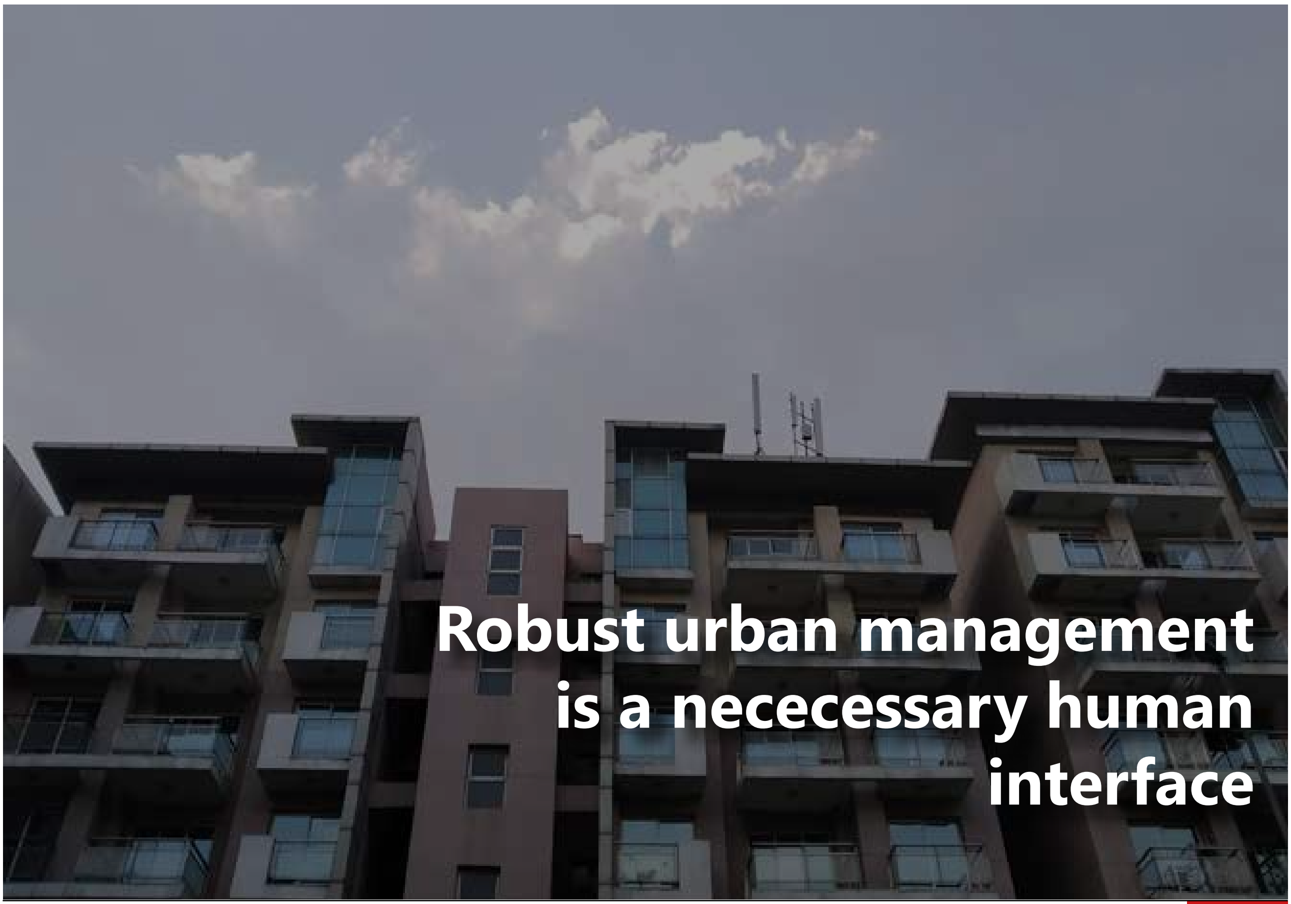
In the retail sector, our outlook is POSITIVE for the remainder of 2021 and the near future. 2021 promises to be promising as we project that the sector will continue to exhibit growth witnessed in 2021 and Q'1 of 2021 with the growth expected to be driven by: the continued expansion of local retailers such as Naivas and Quickmart, and international retailers such as Carrefour taking up prime spaces left by troubled retailers such as Tuskys as well as the continued improvement of infrastructure opening up areas for investment.

Positive demographics and investor confidence due to the ease of doing business in Kenya, having been ranked position #56 by World Bank in the ease of doing business are also some of the factors we believe will propel the performance of the sector. The sector's positive performance may however soften towards the end of 2021, with asking rents, occupancy rates and yields declining by 2.5%, 4.2% points and 0.6% points, respectively, to average at Kshs. 165, 71%, and 6.9%, respectively. This is attributed to the existing oversupply of space estimated at 2.0 million SQFT in the Kenya retail market and 3.1 million SQFT in the Nairobi Metropolitan Area and a possible reduced demand for physical retail space owing to the gradual but steady shift towards e-commerce and the tough economic environment brought about by the COVID-19.

Recommendations

1. We call upon government at both national and county to prioritize planned infrastructure provision for all urban areas and especially areas expectedto experience/accommodate most of the projected growth. The planned infrastructure should include sewerage expansion, storm water drainage, solid waste management, water supply and ICT, to complement the road infrastructure being expanded across the country. Priority should be on areas highlighted as construction 'hotspots' by this report. Additionally, and where possible, the government should explore innovative opportunities for partnerships with private sector to deliver on this mandate. AAK already has viable ideas on this front.

2. We call attention to robust urban management as a necessary human interface to deliver on integrated urban development in all our cities and urban areas. The capacity of our cities and urban areas to plan and implement resulting projects should be improved/enhanced by resourcing the key urban development functions. The start point is to have all development based/or emanating from updated Urban/City Plans done to the local/neighborhood level. Also, ensure the urban management includescapacity to enforce compliance to the plans. This will ameliorate most challenges affecting our urban areas and ensure our urbanization is sustainable.



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