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GLOBAL REAL ESTATE INSTITUTE

AFRICA GRI 2015

DISCUSSION SUMMARIES PROVIDED BY

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SOUTHERN AFRICA

Is South Africa saturated and does opportunity knock for neighbours?

OVERVIEW

SOUTH AFRICA

- Moderate growth for development opportunity as the market is not saturated
- However, developers/investors need to focus on particular opportunities within specific areas
- South Africa is a difficult decision from international investor's perspective due to exchange rate controls
- One of the most significant benefits of investment in South Africa is that it is quick to market unlike the rest of Africa

OTHER SOUTHERN AFRICAN COUNTRIES

- Developers and investors would are the pioneers and therefore great opportunity exists
- The region offers high growth potential, especially within Angola, Mozambique, Botswana, Nigeria and Kenya
- Investment / development into Africa is at a risk but reward is there through greater t risk premium
- A great challenge is that Africa is not quick to market

WEST AFRICA

Are long term investors sticking with Western Africa? And is it all about Lagos and Accra?

The moderator started by noting an interest in Africa, South of the Sahara e.g. Nigeria at MIPIM in 2015. The call was for the discussion to tamper the euphoria of African growth with the downsides to achieve a realistic discussion of African real estate markets.

- There is clear interest in real estate activity in Nigeria and Ghana which begged the question, "why not Francophone West Africa?" Francophone West Africa is characterised by
    - Language barriers
    - Political instability especially in Cote d'Ivoire
    - Francophone legal system
    - Outflow of the middle class from Cameroon
    - Land title (a primary barrier)
- This also creates first-mover opportunities in Abidjan, Dakar and Libreville for example. Cameroon, for example, does not have a single mall. However, it is a bilingual country so language might not be such a barrier after all.
- The suggestion was to find a credible local partner as a way of overcoming the barriers to entry outlined above
- There is real diversity in investment strategy and

approach among the players – even though there is interest in Abidjan, that is second to the interest shown in Ghana and Nigeria

- Angola is usually considered as part of the West African investment universe instead of SADC. Portuguese is a relative barrier to entry.
- Both Ghana and Nigeria have housing deficits with Nigeria's deficit even bigger.
- Investors discriminate between countries in terms of the ease of investing and repatriating their earnings and exiting the investment
    - Some investors push for high return markets but are also interested in returns with developmental impacts; so for example, in both Ghana and Nigeria, there is interest in investing in tier-2 cities
    - An ever present problem is business integrity – land title, the reliability of business partners and legal systems
- State of the market in Ghana and Nigeria
    - Ghana less saturated than Nigeria – it is important to know the market and asset class cycles
    - There is a little wariness towards Ghana due to macroeconomic headwinds and a shortage of quality economic opportunities
    - In Nigeria there is a shortage of blue chip tenants who want to commit to long term leases
    - In both Accra and Lagos there are good office developments and a number of global corporate tenants. It is difficult to pre let assets early enough in the development process.
        » This could be due to tenants' experience of significant delays in completing past projects. An improvement in developers' track record could change that. Reputation counts.
        » For office buildings, many projects are coming into the market at once which presents more options for tenants. In addition, tenants have become savvier and are adopting a wait and see attitude.
- Unexpected fiscal developments, e.g. taxation can alter development prospects. Also important is the lack of professionalization of the brokerage profession in a place like Ghana.
- The bulk of sales in Nigeria are to local buyers. Nigerian investors are less risk averse.
    » Attracting international investors is a matter of packaging the investments. The lack of interest could be due to the low level of detail in the investment opportunities presented.
    » Some investors provide funding to refine the level of detail to make the investment bankable in the form of bridge loans, mezzanine loans, etc. to reduce the downside risk
    » The experience of other players is to invest their own equity to get to the point where the feasibilities are done, debt is secured and the project is bankable for investors BUT not everyone has the capacity to do this
    » A concern was raised about investors in Africa expecting an IRR of 30% which is considered too high; the counterargument is that an IRR of 22% is achievable in the US, meaning 30% offers a good risk premium for the additional risk.
- A suggestion was made for governments to invest in infrastructure in the peripheries of the major urban areas to facilitate the demand for space given the dire shortage of space in the inner cities in Ghana and Nigeria.
    » As pointed out during the discussion, the absence of an efficient airport and easy transport access to cities makes a city like Lagos unattractive for e.g. hotel development. It is unrealistic anyone can come close to quality standards in development comparable to what one can attain in Dubai. This was in response to a comment that investors in Lagos expect quality standards comparable to cities such as Dubai.
    » It was also pointed out that the population size and economic base of tier-2 cities in Nigeria means these cities offer attractive investment opportunities.
    » In terms of actual returns in these two markets, A- and B assets currently return between 14-16% total IRR for retail and office space.

EAST AFRICA

Is Kenya still Africa's success story? And how to move to the next level?

- The Real Estate market in Kenya is more matured than in previous years, its ripe for increased investments
- Global investors want to know what to lookout for in the market prior to investing
- From the discussions, it emerged that it would be better to be based in Kenya than Tanzania.
- Resource companies (i.e. Mining and Oil) prefer Tanzania
- The two biggest retail projects in the region are all taking place in Kenya, further emphasising Kenya's importance to the region, precisely because Kenya's market is more matured, more skilled and has the infrastructure for such projects.
- Tanzania has better growth prospects than Kenya, but their regulatory framework is not as advanced and requires a lot more patience than Kenya.
- There are no "A" grade assets in Kenya, but a lot more "B" Grade assets.
- There is more Real Estate developments in Kenya than any country in the region, thus the market is more competitive, with returns hovering below 10% on average, whereas Uganda and Tanzania offer returns that are mid to higher teens.
- However, there is higher business risk in Tanzania than Kenya, because of the underdeveloped regulatory framework.
- There are land rights issues in Tanzania and foreign land ownership is often very complex and difficult.
- However, in Kenya, Nairobi seems to be the only town with a structured regulatory framework
- Kenya has done very well by digitising of the title deeds and other documents, making it easier to acquire the correct papers on land parcels.
- The quality of labour force in Kenya is more educated, and better trained than the other countries in the region, thus making it the ideal gateway into the region for any investor looking to enter the market in the region.
- Kenya is more unionised than the rest of the region.
- There are more capital buyers in Kenya than the rest of the region.
- A lot of prime land in Tanzania, more so Dar es Salaam, is government owned (National Housing Council), thus making it difficult to do business because of the bureaucracy.
- It is easier and faster to do business with private businesses than to do it with government in Tanzania.
- There are issues with duplication of title deeds in Nairobi (and Kenya in general), thus placing huge importance on proper due diligence prior to doing any business.
- Choosing the right local partner is very important as the wrong partner may result in huge losses.
- Construction costs are on average 10% higher in Dar es Salaam than in Nairobi Kenya, and a further 10% away from the city of Dar es Salaam.
- The East Africa region has high yields/returns thus attracting more capital into the region.
- There is a question of why South African brands/ companies fail in Kenya and seem to do relatively well in Tanzania
- The suggestion is that South African brands need to align their brands and models to suit the individual countries in the region.
- There are historical relations between Tanzania and South Africa, thus ensuring smooth business relations and enabling SA brands to thrive in Tanzania.
- Statistics show that Dar es Salaam is the fastest growing city in Africa, at a rate of 6% annually, and

doubling in size every 12 years.

- The average price in dollars for land in Nairobi, Sandton and Dar es Salaam is around $6 million.
- Uganda has classical issues of political instability, Kenya has security issues (terrorist threats), whereas Tanzania is more stable than the rest of the region.
- Yields in Rwanda are about 10%, 12-14% for developments in Nairobi (Kenya) and15-20% for developments in Dar es Salaam (Tanzania).
- Investors in the room, collectively indicated that they will be investing in the region of $1,4 Billion by way of property developments in the region.

LUSOPHONE AFRICA

Are Angola and Mozambique the new jewels in Africa's crown?

ANGOLA

- The economy needs to diversify which is an indication of existing opportunities
- Residential markets:
- There is demand for housing among low and middle income group
- Prices range from $ 60 000 to $100 000
- There is a limited mortgage market
- People lease to own their properties with a lease term of 15 years
- Office markets
- Demand is generated from the gas and oil companies, and financial services
- Limited quality options of office space
- Property companies expect to have good yields in the future: this point was highly contested
- Vacancy rates might grow to 10% in the next year
- The lease period is 5 years
- Office stock supply is one million m2 and current demand is weak
- There is a lot of speculative developments
- Most projects are completed without leases
- 60% are sold before completion with 30% probability of lease agreement signed in the last six months before completion
- Opportunities exist in the retail and logistics, and industries
- Retail development is not speculative

MOZAMBIQUE

- Residential market
- Mass housing is oversupplied
- Transactions are on cash bases
- The mortgage market is weak with interest rate averaging 20%
- Investors must understand the culture of the communities they operate in
- The extraction companies buy properties for functional purposes only
- There is the challenge of lack of information

PAN AFRICAN EQUITY MARKETS

Are foreign investors still window shopping? And what are the most immediate opportunities?

EVOLUTION OF FUND RAISING EFFORTS:

- General sense of apprehension amongst international institutions when raising funds for African investment
- However, there has been a growing trend of global investors looking into Africa.
  - This may be due to the fact that the African market has become more sophisticated
- Historically, South Africa has not committed to fund investment in Africa.
  - However, a shift has been noted in recent times with South African pension funds and listed real estate funds showing interest

RETURNS

- Generally the target yield for investment is around 18% on a gross basis
- The ability to achieve 25-35% is unrealistic
- Factors influencing returns, include:
  - Tax leakage
  - Currency risk
  - Geography – differs from market to market
- Sub-Saharan Africa is attractive in absolute returns compared to Turkey and the Middle Eat

FACTORS FOR SUCCESSFUL INVESTMENT / FUND RAISING

- Experience of the fund management team is key in trying to access investment equity
- Furthermore, companies / fund managers must have the following:
  - Local presence
  - Deep knowledge of the local market
  - Ability to match the development opportunity to the investor (and the investors risk profile)
- Africa is highly fragmented and therefore the investment management team must understand all influencing factors

DIFFICULTIES IN AFRICAN INVESTMENT / FUND RAISING

- The real issue is not in trying to identify the stock for investment purposes but rather ease of gaining access to investment equity
  - However, investors have noted that funds are chasing the same opportunities
- The cost of equity is extremely high for African investment and therefore following a strategy of buying land to hold it's too expensive
- Investors primary concern for African investment is political and exchange rate risk
- Traditional PE models do not work within Africa
- Difficult to find long term tenants

FUTURE OUTLOOK FOR AFRICA

- High yielding returns are unsustainable and will need to come down
- Africa's market will become more efficient
  - The more efficient the market the lower the expected return
  - However, this will allow for growth in other sectors

SOUTH AFRICA

- Fundamentals are getting weaker in South Africa
  - Stock is just moving around
  - Capital is not being reinvested in growth
  - In the future, local funds will need to move abroad given limited growth

RETAIL AND LOGISTICS

Bricks, Clicks and Economics – how is the retail sector evolving in Southern Africa?

- The South African retail market is saturated and opportunities lay on the distribution and efficient supply chain
- In other country 5000 m2 malls are successful and yield in return
- There is growth on the online trading and retailers are using their stores as collection point
- Big malls must be developed gradually in order to yield higher returns
- The compression of yields is assisting the development of mall of SA
- There opportunities for future developments as urbanisation is growing and there is more wealth distribution
- Permit risks are low on the continent
- Africa needs technological advancements and if the economy drops, there will be capital flight from the continent

RESIDENTIAL AND MIXED USE DEVELOPMENTS

Where are the next opportunities in West Africa?

- IFC looking to bring full supply chain for affordable housing in the region.
- Senegal and Ivory Coast are projected to be the next in line, as far as development and investment goes. However the housing Gap in Senegal stands at 170 000 units compared to 17 million units in Nigeria.
- Capital seems to follow where there are opportunities for high returns, in this case, Nigeria and Ghana.
- Senegal is very stable politically and has a high investor confidence.
- In French speaking African countries in the region, information is centralised and therefore makes it difficult for investors to access it.
- Cameroon's economy is largely informal and cash rich, because of the heavy regulatory framework.
- 24 million people live in Cameroon and there is no single shopping centre in the country.
- The following are key things that would be investors look at before deciding to invest in a country:
    - Land rights
    - Political stability
    - completion risk
    - Property rights
    - Financial transparency
- Tenants are reluctant to sign leases before projects commence construction, but once the building is underway the uptake seems to accelerate

- Affordable housing in Nigeria is slowly picking up.
- What is affordable housing: Kenya $40 - 60k ; Nigeria $ 150k
- The challenge for projects/development in this region is the lack of infrastructure.
- The problem in Nigeria is that the law is not strong enough to support foreclosure.
- It is also difficult to evict defaulters when renting out your property.
- In Ghana, housing developers build shells and put in the infrastructure and allow the individual owners to finish the houses however they please, thus reducing house costs.

HOTELS & TOURISM

Where are the next hotel development opportunities in East Africa?

- The focus in this sector is on budget-midrange markets.
- From a developer's perspective, Dar Es Salaam is in the spotlight, with Addis Ababa a future target, followed by Kampala
- From an operator's perspective, there are lots of opportunities in Rwanda and Uganda for budget business hotels.
- There is also a degree of openness towards franchising by the big brands
- From a user's point of view – the big brands hold an advantage because there is clarity in what the quality standards are.
- The owner-operator relationship is contentious most of the time.
- The strategy towards emerging markets is to develop the asset and bring the operator along.
- There is general alignment where recurrent issues can be discussed between owners and developers.
- The difference between East and West Africa:
    - East Africa is more ready for resorts than West Africa is
    - West Africa lacks infrastructural links that make access to resort and recreational areas easy especially outside the big cities
    - The owners are different as are the nature of contract negotiations
    - East African owners are mostly Asians who have had a long track record in the business.
    - Time to market in East Africa is also shorter.
    - In East Africa,
        - » Kenya has security issues that do not look like they can be resolved quickly
        - » Tanzania has natural beauty but not enough infrastructure yet; however, growing air traffic increases the attractiveness of future hotel developments
        - » A 5-star hotel is doable in Nairobi but secondary cities need budget hotels such as the IBIS franchise
    - Rent setting – there are a number of alternatives preferred by different owners:
        - » Fixed rentals
        - » Variable rentals
        - » Hybrid rentals
- The investment approach is on an asset by asset basis
    - Some assets need renovation
    - Some assets are ready to be operated right away

- Regardless of asset type the rental model must make investment sense
- Secondary cities
  - Southern Tanzania or Northern Mozambique with mining activities
  - The risk is going in too early before all the requisite infrastructure is in place
  - There is therefore a need to be cautious about these cities
    - » Clearly establish demand for hospitality services
    - » Make sure there is ready infrastructure in terms of road access, energy, connectivity, etc.
- The approach of some of the big brands is to target capital cities first; secondary cities are approached with caution for lack of depth with the exception of Nigeria due to the sheer size of that country
- There was a question about the prospect of extended stay and hotel apartments either as stand-alone or mixed developments. The consensus is that extended stay has a huge potential in Africa.

PAN-AFRICAN DEBT MARKETS

Which banks are lending? And what do they want to see from developers?

- The South African debt market is mature
- The cost of borrowing is high on the continent and there is a need for more lenders
- There is a need for development funds for small to large capital projects
- There is a huge demand for commercial properties
- It is getting easier to participate in the market, e.g. Nigerian banks are now able and willing to lend money
- The equity level is between 40% to 50% and banks are willing to refinance projects
- Bridge lending in Nigeria with interest rate of 12% but the applicant must produce pre-lease agreement and the projects must have a yield of 15%
- It is not easy to get interest only loans on the continent. One must provide guarantees
- The risk of default is high as there is a disparity between the country's currency and the international currency used in the loan agreement
- It is better to borrow from the local banks than the international banks

RESIDENTIAL AND MIXED USE

What are the best opportunities in Southern and Eastern Africa?

DEVELOPMENT PLANNING

- Planning and infrastructure is a necessity within major African cities
- A common vision is required to successfully execute development projects
- The biggest issue facing most countries is the lack of bulk infrastructure and poor transport / road system
- Specifically:
  - In Angola, cities have been planned for a third of the population it currently has
  - In Kenya, a spatial development Plan for Nairobi exists. However, Nairobi misses a credible development vision and therefore there is no leadership to support and execute projects in line with a common vision. Furthermore, due to traffic congestion and road infrastructure related issues there has been an increase in demand for mixed use development.

LEGAL

- Primary threats include
  - Corruption
  - Land expropriation
- The private sector needs to be ensured that such legal issues have been resolved
- Kenya's legal system regarding land ownership has improved - the system has been 'cleaned-up'

CHALLENGES

- Primary challenge is that the mortgage market in non-existent within Africa
  - African banks are apprehensive to do broad based lending
  - A few banks have started to grant mortgage bonds however interest rates charged are excessive and unsustainable
  - Therefore, developers target market are cash buyers (for now)
- African market does not take kind to purchasing off plan – the market wants to see top structure before purchasing
  - This is problematic for developers who are required to meet presales targets in order to gain access to development debt finance
- Kenyan market
  - Big market of speculators within Kenya
  - Developers need to ensure 90% of funding has been secured when end users purchase as there is a trend for investors to pay a deposit and then default on their payments in the event of the market turning

RENTAL MODELS

- Rental models require the appropriate legal infrastructure to support it which is lacking in most African countries
- Furthermore there is a lack of management companies in Africa to manage rental stock

OPPORTUNITIES

- Significant residential development opportunities exist within Angola, Mozambique and Zambia
  - However, lack of infrastructure (roads) is a significant problem when trying to execute on the opportunity
- Opportunity for property management companies exists with a specific focus in the residential market segment

HOTELS AND TOURISM

Nigeria vs. Ghana: New Frontier or close to saturation?

- There is room for growth in the hotel industry in Accra, Abuja and Lagos.
- The mid-market is where the potential growth lies in the region.
- In the emerging markets, demand far outstrip supply, thus pushing prices for 5 star hotels above market related prices.
- Abuja has the highest return rates of the two countries, and the cost of building per key in Accra is lower than for the same development in Lagos.
- Utility/running costs are much higher in Nigeria than Ghana.
- Nigeria has more local demand for the hotel space, estimated at around 60% and the remaining 40% is international.
- Accra is a favourite destination for international guests; the market is far from saturation.
- A potential new market would be extended stay hotels
- yields/returns on extended stay is much higher than normal hotel rentals
- The following are reasons for higher construction costs in Lagos Nigeria:
    - Imported material (70% of materials are imported in Nigeria)
    - Concrete is very expensive
    - Running costs are much higher (Electricity, etc)
- 40 hotels in Nigeria are in the pipeline, and if all go ahead could potentially lead to saturation of the market, but the growing Nigerian economy could possibly see the demand continue to grow.
- Lease vs Management contracts is the new debate in the hotel and tourism industry, with more companies opting for management contracts because of shared pain and shared gain.
- Investors believe management contracts are better business models because one is involved with the day to day running of the business and can better predict shifts in the market.
- Equity to debt ratio (funding structure) and construction costs are holding back a lot of projects from breaking grown.
- The biggest risk in hotel developments/ construction is the big initial capital outlay and the non-guaranteed cash flow that follow on operation.
- The Nigerian government set up a department to ensure that there is no capital flight, and that the money leaving the country is equivalent to the value of the projects on the ground.
- TAX Incentives:
    - The Ghana government encourages capital inflows by relaxing some of the import duties on certain products.
    - There are areas declared as free zones in Nigeria that offer tax relief for certain projects.
- In the hotel industry, specifically in emerging market, the right professionals are not always hired to do the job.

RETAIL AND LOGISTICS

Is a retail revolution happening in East Africa?

- Nairobi has seen a lot of growth in the retail space (from about 3.3 to 6m square feet of mall space)
- Carrefour is setting up two developments in Nairobi. They only enter a country if they can get manage 2 hypermarkets successfully
- There are a number of international players from Botswana and South Africa looking to come into East Africa
- Many of the existing centres are dysfunctional – poor design, no anchor tenants etc
- Outlet malls are decades away from coming into being
- Food franchises are expanding rapidly
- The conclusion is that maybe there is not a revolution but rather an evolution
- Barriers to entry
    - Fragmented market that inhibits scale
    - Import duties
- Growing middle class a potential source of demand (unrealised sales potential in Dar Es Salaam, for example)
    - Kampala less attractive than Dar Es Salaam because of scarcity of well-located space
- Lease length – 6 years with the option to renew
    - Turnover lease clauses difficult for small retailers because of the difficulty of verifying sales records
- Logistics – there is growing demand and the existence of 3rd party operators
    - Existing facilities are not up to the required quality standards in Kenya
    - In Tanzania there is growing demand, site and service model
    - Future demand will be driven by growth in the retail sector in both Kenya and Tanzania
    - Yields are around 10%; it is cheaper to build for basic types – the interior tends to be sophisticated because of IT requirements.
    - The tipping point will be the first successful pre-let facility.

PAN AFRICA OFFICE AND CORPORATE TENANTS

Can returns be maintained amidst the relentless expansion?

RENTAL RATES, DEVELOPMENT COST AND RETURNS

- General
    - Rental levels within many African economies are unsustainable (excessively high) and therefore reductions in rental rates are expected.
    - This may be due to additional stock coming on line within the market

- However, despite the decrease in rental rates an increase in the demand for space is expected to continue within multiple African economies
- Nigeria
  - A trend of decreasing rental rates for A grade office space has been noted and construction costs have been increasing
  - Given this, the current returns being achieved is unsustainable
- Ghana
  - Demand for space was predominantly driven by companies within the oil sector
  - A decrease in the demand for space has been noted due to the pressure being placed on the oil market
  - This has led to excess supply of space and hence downward pressure on rental rates
- Angola
  - A decrease in achievable rentals has been noted due to excess supply within the market
- Mozambique
  - The recent find of gas brings strong economic potential to the country
  - Given this and given limited availability of stock within the region an increase in rental rates is expected

QUALITY OF STOCK

- The definition of A-grade space amongst African countries differs. This may be due to a lack of general consensus and a common benchmark adopted across the different regions
- However, in grading office space the general consensus is that it is determined by a combination of:
  - Quality of stock
  - Optimisation of space
- Green standards
  - A trend of green building practices is expected to be adopted within African countries
  - However, a national body needs to implement / oversee this

RETAIL AND LOGISTICS

Does a “copy & paste” strategy work in West Africa?

- Definition of Retail - normally refers to a multi-tenant development
- Definition of Logistics (Industrial) - Normally refers to a single tenant development
- Definition of copy & paste - refers to using approaches and methods that have been used in specific developments in different markets to enter new markets, but must be adjusted to suit specific markets.
- The goal in developing a shopping/retail centre is not to localise it too much and thus lose potential shoppers that have international taste.
- Copy and paste, tends to work well with logistics developments because manufacturers have specific needs and specific requirements.
- It is important for would be investors and developers, to invest the time and resources to learn the local market conditions before entering a specific market.
- New tenants/retailers need presence (more than one store) in a new market to establish themselves.

- The following are limiting factors for mega malls in Nigeria:
  - Sizeable land
  - Infrastructure developments
  - Retailers / tenants
  - Inconsistent government policies
- Land assembly in Lagos in near impossible because of the time frames involved, thus making it difficult to build mega malls in built up areas.
- The following are limiting factors for Logistics developments:
  - Land price
  - Construction costs
- The approach with most developers, seems to be the wait and see, where they will wait for the economy to grow and industrialize, thus creating a bigger demand and the possibility of industrial parks.
- Land prices inhibit industrial developments because they are priced at residential or commercial land rates, thus rendering potential industrial developments not commercially viable.
- Specialized zones/demarcated areas by government can unlock the potential development of industrial spaces.
- It has become evidently clear that as much as retail can be spearheaded by the private sector, industrial development requires government to work hand in hand with private sector

DISCUSSION SUMMARIES PROVIDED BY

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