

REITS ASSOCIATION OF KENYA (RAK)
NEWSLETTER
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Welcome Note from the **RAK** Chairman

A warm welcome to the 15th edition of the RAK's Newsletter.

As I take up this role our mission to advance and elevate the REITs market in our country and beyond, I am delighted to share the strides we have made and the impact of our ongoing efforts. From new initiatives to significant achievements, this edition showcases our commitment to driving growth and innovation within the REIT's sector.

The REIT Toolkit and Incubator program has streamlined the complexities of launching REITs, making it increasingly feasible for emerging players to turn their investment ideas into reality. To date, the initiative has made substantial progress, with six prospective REITs actively pursuing approval to enlist. Additionally, the program has garnered interest from several other companies seeking to join. Among the key events hosted by the program were the REIT Toolkit & Incubator Workshops 3A and 3B, themed the REIT Masterclass. These workshops are meticulously designed to provide delegates with the advanced knowledge and practical tools needed to excel in the complex world of REITs.

The association had the opportunity to participate as industry partners at the 11th annual East Africa Property Investment (EAPI) Summit. We were privileged to delve into the topic of 'REIT Investment & Returns in Kenya' and actively engaged in discussions centered around 'Enabling Affordability with Finance.' The event took place at the Radisson Blu in Upper Hill, Nairobi, on April 17th and 18th, 2024. Additionally, we participated in the 7th East African Summit held on May 9th and 10th at Adwa Museum in Addis Ababa, Ethiopia. Our former Chairman, Mr. Kenneth Masika, contributed to a panel discussion titled 'Ethiopia's Evolving Capital Market Ecosystem & Opportunities' (Innovative products and the role of stockbrokers, investment bankers, and investment trusts). Furthermore, we were honored to participate in Nareit's REITweek: 2024 Investor Conference in New York City, USA, as part of Nareit's guests and RAK's global strategic alliances for benchmarking and capacity building. We were pleased to bring on board 15 RAK members, including Acorn Holdings Limited, Nairobi Securities Exchange PLC, ILAM Fahari, Co-operative Bank of Kenya, and Sterling Real Estate Advisory.

A favorable regulatory environment and strategic tax incentives are critical drivers for the robust growth and sustained success of REITs. The association remains steadfast in its advocacy

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for the reinstatement of essential tax benefits for REITs, particularly focusing on stamp duty and capital gains tax. Our recent submission was to the Departmental Committee on Finance and National Planning on the 3rd of June 2024. Although our request for an exemption was not granted, we remain committed to our cause. We have initiated discussions with other associations, such as NAREIT, to bolster our ongoing efforts in advocating for tax exemptions from the government.

The Association is spearheading the establishment of a Pan-African Real Estate Investment Trust (REIT) Consultative Forum. This consultative forum aims to foster knowledge sharing among key REIT stakeholders across the African continent with the aim of developing the market and promoting the growth of the REIT industry in Africa. We are looking to actively engage with several key stock exchanges across Africa on this initiative.

Recognizing the need for guidance in understanding and implementing market practices related to REITs, the Association has assumed a leadership role; and formed the Standards Working Group tasked with developing a comprehensive reference document encompassing valuation methodologies, performance metrics, and financial reporting standards specific to the Kenyan REIT market. This document aims to establish clear definitions and precise calculations for performance metrics to foster consistency and comprehension among stakeholders. We envision this document will be pivotal in creating a resource hub for disseminating knowledge and best practices, highlighting its dynamic nature requiring periodic updates to stay current with evolving market dynamics

and regulatory mandates, thereby ensuring its relevance and usefulness over time.

Over the course of the 2023/2024 academic year, we successfully engaged with students from The University of Nairobi through REIT talks. Our sessions covered a wide array of topics from the basics of REITs to advanced investment strategies and market dynamics. We look forward to continuing this collaboration with several other academic institutions for the foreseeable future.

The RAK conference has become an annual staple in the calendar of the real estate industry, serving as a platform for the sector's growth and professionalization. This year's annual conference is scheduled to take place from October 30th to November 1st, 2024, at Enashipai Resort in Naivasha. Building on the success of last year's conference, this year's event aims to be even more impactful under the theme: "Navigating New Frontiers: Unlocking the Potential of Africa's REIT Market". It promises to be a crucial gathering for stakeholders interested in leveraging the extensive opportunities offered by real estate investment trusts across Africa. Attendees will gain actionable insights, network with key players, and be at the forefront of Africa's REIT evolution. We welcome sponsors to be part

of the event, providing them with significant visibility and engagement within the real estate investment community. This is an event you cannot afford to miss! Early Bird Tickets are now available! Visit our website at <https://rak.co.ke/> to secure your spot at this premier industry event.

In conclusion, I would like to express my gratitude to all the members and stakeholders who have contributed to the progress of RAK. Together, we are fostering the growth of the REIT industry in Kenya and East Africa. I encourage you all to stay engaged, participate in upcoming events, and continue collaborating to unlock the full potential of REITs.

Thank you.

Enjoy the read!

Geoffrey Odundo
RAK CHAIRMAN



CASE STUDY: ILAM Fahari I-REIT Unquoted Securities Platform (USP)

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Background

ILAM Fahari I-REIT (IFIR) was the first listed REIT at the Nairobi Securities Exchange (NSE) having been listed on the Main Investment Market Segment in 2015. This came after the REIT regulations were published by the Capital Markets Authority (CMA) and the Income Tax Act was amended to allow for tax exemption of REITs.

The REIT acquired 3 seed properties in its portfolio including Greenspan Mall, a mixed-use shopping mall in Donholm, and two light industrial properties, Bay Holdings and Highway House, both located in the Industrial Area of Nairobi. The REIT later acquired 67 Gitanga Road, a commercial office property.

In 2019, STANLIB disposed the role of Promoter and REIT Manager to ICEA Lion Asset Management (ILAM) and in 2020, thus ILAM officially took over the role of manager and promoter of the REIT, effectively changing the name of the REIT to ILAM Fahari I-REIT.

Challenges

The REIT faced challenges including underperforming assets which were either vacant or facing significant vacancy risk arising from major tenants. Additionally, the Covid-19 pandemic, which resulted in tenants whose businesses were affected by lockdown restrictions negotiating for rent concessions.

All these had an impact on the REITs market perception and subsequently its pricing. Also, the small size of the property portfolio was problematic due to the high fixed costs of the REIT, which further dampened the returns to unitholders.

Additionally, the REIT had not been able to raise capital to acquire additional assets and the small size of the portfolio, and high fixed costs had an impact on returns to the unit holders.

As a result of this, the REIT traded at a discount to Net Asset Value (NAV). A REIT's NAV is the estimated direct property market value of its total assets minus the value of total liabilities. NAV can be expressed on a per share basis and compared to the stock price, which gives the ratio, price/NAV. It is used to measure the relative value of the REIT's real estate priced in the public market relative to similar assets in the private market.

Interventions

In the face of these challenges, the REIT took several measures to preserve value of the REIT including signing a lease with new anchor tenant at Greenspan mall, commissioning capital works to elevate the mall, and beginning to dispose off non-performing assets of the REIT.

The REIT therefore decided to undertake an in-depth review of its operations, with the aim of increasing its size, efficiency and returns.

In 2022, the REIT issued a cautionary statement announcing a strategic review that would involve an operational restructuring. Following in-depth research and consultations with key market stakeholders, the REIT decided to delist from the main market and subsequently quote its units on the USP. This would enable the REIT to reset itself with a smaller unit holder base. It would trade as a restricted REIT, only open to professional investors in line with the REIT regulations.

Following this, the REIT aims at optimizing the existing assets, potential disposal of non-core assets, capital raising, acquisitions and aligning service provider fees.

The NSE Unquoted Securities Platform (USP)

In 2020, NSE Plc identified the need for an unquoted platform which could be used for value discovery, capital raising, and an enhanced trading experience supported by the efficient trading, clearing and settlement of financial market transactions of unquoted companies.

The USP offers issuers shorter listing timelines, lower admission costs, enhanced liquidity due to the automated trading process, flexible listing requirements and capital raising opportunities. ILAM Fahari I-REIT enjoys these benefits following its admission to the USP in July 2024.

The conversion of the REIT from un-restricted to a restricted I-REIT, was the initial step in the process of moving the listing of the I-REIT from the Unrestricted Main Investment Segment (MIMS) of the NSE to the USP where it will trade.

On the USP, trading of the REIT will be mainly open to professional investors, defined as having a minimum outlay of Ksh.5Mn (The REIT regulation puts this at a minimum of Ksh.100,000). The REIT has bundled non-professional unit holders into a nominee account to enable them to still trade, governed by trading rules given the restricted nature.

Regulatory Highlights

- i. **Changes to the REITs Trust Deed:** The REIT had to undertake amendments to its Trust Deed to reflect its new Restricted Status and thus amending all clauses that touch on this. The Trust Deed of a REIT is the legal document that establishes the relationship between the REIT, the Trustee and the unitholders and sets out the rules and responsibilities of key parties to the REIT including the promoter and REIT manager. The amended Trust Deed needed to be submitted to the CMA and NSE for approval and later filed with the Business Registration Services.
- ii. **Redemption offer exercise:** The REIT needed to undertake a Redemption offer exercise to redeem the Units from the Non-Professional Investors to enable the conversion of the REIT from an Unrestricted I-REIT into a Restricted I-REIT. The Kshs. 402 million transaction was to allow IFIR's Non-Professional Investors to redeem up to 36,585,134 Units equaling to 20.22% of the issued shares, at a Redemption Offer Price of Ksh. 11 per unit. The offer was oversubscribed by up to 13.08%.

iii. **EGM approval by the unitholders.** Post redemption, remaining Unitholders voted at the EGM for the conversion of the I-REIT and the delisting from the NSE. The proposed conversion was captured as an amendment to the Trust Deed and was voted for at the EGM post closure of the Redemption Offer exercise. Post EGM, the REIT formally applied to the CMA and NSE to delist from the Main Investment Market Segment. Upon approval, the delisting date was communicated to the public as Monday 12th February 2024.

iv. **Application for Quoting on the USP:** The REIT applied to the NSE LLP Management Committee for listing of its units on the NSE USP to facilitate liquidity for both its professional and non-professional investors. To facilitate trading on the USP, the promoter sponsored trading rules to enable liquidity for both professional and non-professional unit holders. Approval for admission to the USP was granted in April 2024, with a bell-ringing ceremony held in July 2024.

v. **Investor education and awareness:** The REIT Manager and lead transaction advisor have undertaken extensive investor awareness workshops to apprise investors of the progress throughout the journey from the initial announcement to restructure the REIT to eventually being admitted to the NSE USP. The REIT has been transparent every step of the way and investors have been able to know which action to take through every step of the re-structuring.

Conclusion

The restructuring of the REIT and quoting of its units on the NSE USP is in line with the REITs strategic plan and objectives. The REIT's conversion to a restricted REIT will enable it to work with a smaller unit holder base while still enabling the unit holders to enjoy liquidity, transparency and price discovery.

Previously, when the REIT was un-restricted, this limited it to being close-ended fund which meant that investment, subscription and exit could only be through secondary market, the value fluctuated with market price, there was a constant number of units and trustee was not entitled to redeem units.

The nature of the REIT being restricted enables it enjoys benefits on both open-ended or close-ended fund features. The open-ended fund means that units may be redeemed by trustee, the value of investment and redemption price determined by NAV of unit and the size of fund may expand or contract.

The USP is open to admit companies and Small and Medium Enterprises (SMEs) who are not ready to list on the main market but can enjoy benefits of well-functioning market infrastructure. The USP also provides value for entities such as REITs and SMEs which are able to discover value through restricted trading on the platform. The platform is open to admission of all types of securities from vanilla equities and bonds instruments to other advanced instruments. The NSE is available and willing to facilitate issuer engagements with interested parties.

REITs Growth Strategies and Progress in Africa

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The past decade has witnessed significant strides in the emergence and growth of the REIT sector in Africa, particularly in South Africa, Kenya, Zambia and Zimbabwe. As stakeholders prepare to convene at RAK's 2024 annual REIT Conference, aptly themed "Navigating New Frontiers: Unlocking the Potential of Africa's REIT Market," this article provides a backdrop for discussions on the growth of REITs in these markets. It also explores the lessons, strategies, and insights gleaned from these countries, setting the stage for deeper discussions at the upcoming REIT Conference in Naivasha, Kenya.

South Africa commands the most robust REIT market in Africa, characterized by a diverse REIT sector with 28 REITs in operation. The REIT framework in South Africa, introduced in 2013, established a conducive environment for REITs, allowing REITs to be structured either as a company or as a trust. Johannesburg Stock Exchange (JSE) plays a crucial role in this ecosystem by facilitating the listing and capital expansion of REITs, enhancing their accessibility and liquidity for both local and international investors. To enhance the REIT regulatory environment, JSE has proposed various amendments to its listing requirements using a phased approach dubbed 'the JSE Simplification Project.' The sixth phase of the Simplification Project broadened inter alia the definition of 'property entity' to include an entity primarily engaged in the holding of property as an investment to earn rental and/or for capital appreciation or the development of property to be held as an investment. The proposed amendments will support the listing of infrastructure REITs and also aim to convert complex language construction of listing regulations into plain language whilst maintaining the regulatory objective.

The performance of South African REITs has had to contend with challenges that negatively impacted occupancy levels

in the REIT properties such as load shedding, slow economic growth, political instability, and fluctuating property values. In response to the challenges posed by the South African economic and political environment, the REITs have resorted to making well-rounded and resilient investment approaches to foster growth. One such strategy has been geographical and sectoral diversification, with REITs investing in a wide range of specialized sectors. This REIT growth strategy has seen specialisations in logistics (Equities Property Fund Limited), self-storage (Stor-Age Property REIT Limited), and multi-let industrials (Industrials REIT and Sirius Real Estate Limited). In 2021, Afine Investment Limited listed a petrol service station REIT on the JSE, allowing REIT investors to participate in the indirect ownership of petrol service station properties.

Notwithstanding the many challenges in the REITs sector, the first quarter of 2024 has seen improvements in the South African REITs sector. Some of the reasons for this have been: the recovery of sales and rent in shopping centres; improvement of load-shedding levels, heavy investment in back-up generators and renewable energy.

On its part, Kenya has also made significant headway in the growth of the REIT sector. This has been made possible by several factors such as: diverse opportunities in purpose-built housing projects, rapid population and urbanization rates, aggressive expansion strategies by local and international institutions and enhanced investor confidence in the Kenyan real estate market. Kenyan REITs have applied several growth strategies to ensure scaling and enhanced returns to investors. Some of these strategies are specialization in specialised student housing accommodation, restructuring of a listed REIT to attract institutional investors and maintaining a well-planned equity and debt financing.



Kenya now has three REITs trading on the NSE's over-the-counter Unquoted Security Platform (USP), and one REIT in the main market segment, affording the benefits of professional investment, liquidity and an enabling growth environment. The de-listing of ILAM FAHARI I-REIT and subsequent admission to trading on the NSE's USP platform is expected to afford lower price volatility unlike the previously fragmented trading of units on the main bourse.

In contrast to Kenya and South Africa, Zimbabwe is relatively new to the REIT market but shows potential for significant growth. The introduction of REITs in Zimbabwe aims to attract investment by offering a structured approach to real estate investment that promises liquidity and transparency. The REIT framework is designed to encourage investments in various real estate sectors, including residential, commercial, and industrial projects. REITs in Zimbabwe were introduced as regulated collective investment entities in 2019 six years after Kenya introduced its regulations.

Since the introduction of REITs as a tool for collective investment in Real Estate in 2019, the REITs sector in Zimbabwe has seen a fair growth pattern relative to the date of the introduction of REITs and considering the occurrence of the COVID-19 pandemic that weakened economic growth. Subsequent to the enactment of the regulations, two REITs currently listed in the Zimbabwe Stock Exchange (ZSE), have been established. Tigere Property Fund became the first REIT to be listed on the ZSE in November 2022. The second REIT, Revitus Property Opportunities REIT was listed on the ZSE on 18th December 2023. The REIT's investment strategy involves strategic purchasing of commercial properties in urban areas, revitalising the properties into modern green property assets (through renovation, repositioning and re-generation) and earning improved rental incomes while benefiting from potentially substantial growth.

Zimbabwe's REIT market faces unique challenges, including economic volatility and complex regulatory frameworks.

However, the establishment of the two REITs within a short span has marked a significant step towards cultivating a viable REIT market. This initiative reflects a growing recognition of the benefits of REITs in mobilizing capital for real estate development and offering investors stable income streams. Overall, the REITs sector in Zimbabwe is on a positive trajectory with the ZSE prioritising the sector as its main growth area in the short to medium term, as part of its wider goal of fostering growth and diversification of the Zimbabwean capital market.

In a similar vein, Zambia's REIT market is in its developmental stages but poised for significant growth. The Zambian Securities (Real Estate Investment Trust) Guidelines were enacted in 2020 and are the primary regulation relating to REITs. Zambia currently has only one REIT, the Real Estate Investments Zambia REIT. The REIT was listed in June 2024. Recent developments, such as the transition of Real Estate Investments Zambia Plc towards REIT status, signify a maturing understanding and acceptance of REITs within the Zambian investment community. This shift towards structured real estate investment is expected to enhance market liquidity and attract a broader investor base. The Zambian government has supported this development by creating favourable regulatory conditions that encourage the listing and growth of REITs, aiming to enhance market liquidity and attract both local and international investors.

The upcoming RAK annual REIT conference will serve as an essential platform for stakeholders to explore these insights more deeply, discussing strategies to overcome challenges and leverage opportunities within the African REIT sector. The conference will serve as a dynamic platform for stakeholders to explore innovative solutions, discuss regulatory enhancements, and engage in strategic dialogues aimed at advancing the REIT sector continent-wide. This article sets the stage for a comprehensive discussion at the conference, aiming to delve into these insights with a focus on practical solutions and strategic advancements to nurture the growth of REITs in Africa.

Secretariat Report

Insights and Learnings from the 2024 NAREIT REIT Week



The recent NAREIT REIT Week provided valuable insights for Kenyan delegates, highlighting several key areas of focus that could significantly enhance the growth and success of the REIT sector in our region.

Tax Implications and Policy Considerations for REIT Growth

The securitization of real estate in the US is extensive, and achieving similar levels of GDP-to-REIT market capitalization and trading volumes in Kenya could substantially increase tax revenue, particularly through stamp duty on REIT unit trading. Exploring the potential tax benefits of a robust REIT market could be an insightful exercise, especially when paired with effective policy-level incentives. Providing such incentives, including stamp duty exemptions, is crucial for the sector's growth. Additionally, encouraging the adoption of up-REIT structures could drive greater success in the industry. Utilizing private placements and insurance funds can offer stable financing for REITs, while engaging in national policy discussions on stamp duty and other tax considerations—drawing on successful models from the US and EU—can further support the development and expansion of REITs in our region.

Debt Management:

Presentations underscored the importance of managing debt, especially in light of rising interest rates. While our market is still developing, leveraging some debt could be beneficial if it can be serviced from income and contributes to growth and value enhancement. Understanding the regulatory frameworks governing REIT debt in the US could offer valuable lessons for our local context.

Valuation Challenges, Specialization, and Asset Management:

The US market demonstrates a high degree of specialization in real estate categories, which allows managers to develop deep expertise and enhance value. In Kenya, fostering diversified REITs that specialize in specific asset types, such as industrial or commercial real estate, could similarly boost value. Streamlining asset acquisitions and disposals between REITs, or with non-REIT parties, is crucial for optimal positioning. Beyond traditional real estate, REITs also have the potential to fund various infrastructure

projects, including highways and farmland, as seen in China and the US. Expanding the scope of REITs to encompass other forms of infrastructure presents a promising avenue for growth and diversification.

Governance, Strategic Management, and Market Trends

The success of REITs hinges on effective strategic management that aligns with shareholder objectives, particularly through robust cash flow management, debt service coverage, and strategic capital allocation. Engaging third-party professionals for capital and operational management can further align these strategies with investor goals. Governance and asset management play a critical role in this success, requiring a focus on strategic acquisitions, lease renewals, and maintaining high portfolio quality. Effective timing and targeted concessions are essential for managing lease expiries and securing strong renewal rates.

The scale of the REIT sector in the US, with assets valued at USD 3.5 trillion, underscores the immense growth potential for our region. Looking ahead, the future of REITs lies in achieving economies of scale, optimal balance sheet management, and developing core competencies. Emerging trends include increased specialization, market consolidation, exploration of new markets and property types, and the pursuit of sustainability initiatives aiming for net-zero carbon emissions by 2030. Mature REITs are increasingly focusing on specialization, while smaller REITs are consolidating to improve access to equity and debt. However, the challenge of aligning private and public valuations persists, necessitating the development of standardized REIT valuation methodologies to enhance accuracy, comparability, and investor confidence.

Regional Integration:

The concept of cross-listing REITs within the region was validated, promoting broader investment opportunities. Collaborating with NAREIT to support national policy agendas is also recommended.

Valuation Challenges and Standardization:

Divergences between private and public valuations present significant challenges in the REIT sector. Developing standardized valuation methodologies could improve accuracy and comparability, thereby boosting investor confidence. Additionally, standardizing investor materials, with technical input from NAREIT, could further enhance transparency and trust. The success of REITs is also closely tied to interest rate environments, with better performance anticipated at the end of tightening cycles. Therefore, advocating for policymakers to consider the impact of interest rates on REITs is crucial for the sector's stability and growth.

By incorporating these insights and strategic recommendations, we can significantly enhance the development and success of the REIT sector in Kenya and beyond.

Photos/Gallery





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