REITS ASSOCIATION OF KENYA (RAK)

# NEWSLETTER

9TH EDITION OCTOBER 2022

## REITS AND ESG

## Welcome Note from the **RAK Chairman**

*A warm welcome to the 9th Edition of the RAK Newsletter.*

According to NAREIT's REIT Industry ESG Report, 2022, REITs and publicly traded real estate companies are institutionalizing ESG within their corporate strategy, business management and operations. Sustainability practices are increasingly integrated into REITs' corporate and investment strategies and elevated in governance frameworks. 82% of REITs surveyed integrated ESG risks and opportunities into their strategy and financial planning in 2021, up from 77% in 2020.

In the 8th Edition of the Newsletter, we looked into ESG in the real estate sector and spoke to some of the leading local real estate companies and industry leaders to see how they are incorporating ESG practice into their operations. In this edition, we focus on REITs to explore and highlight trends in industry, REITs industry primary ESG practice, investor perspectives, useful guidance and include an in-depth case study of the Acorn REITs journey towards achieving Global ESG Benchmark for Real Assets (GRESB) certification.

We also share a highlight of the REIT Ratings Breakfast workshop which took place on 27th July 2022 from 7am – 10 am at the Villa Rosa Kempinski Hotel. We partnered with GCR Ratings and Nairobi Securities Exchange (NSE) to take *'A deep dive into REIT ratings'* where we had a key note presentation from Head of Corporate Ratings at GCR Ratings. Additionally, in August 2022 we met with the Ethiopian Stock Exchange (ESX) project implementation team led by Financial Sector Deepening Africa (FSDA) team. During the meeting the team highlighted the progress on the establishment of the ESX and got a chance to learn about REITs in the Kenyan context including the regulatory framework, structures, challenges and benefits of REITs.

Lastly, towards our aim of providing insightful market data that can be practically utilized by stakeholders, we have included an analysis of the REITs 2022 Half Year Financials from page 6. We purpose at improving transparency and providing quality research and information to local, regional and international investors.

Enjoy the Read!

*Kenneth Masika*
RAK CHAIRMAN

## CONTENT

# RAK-GCR BREAKFAST WORKSHOP: *'A DEEP DIVE INTO REIT RATINGS'*

## JULY 2021

RAK partnered with GCR Ratings to conduct a workshop on REIT Ratings. GCR Ratings is a leading ratings agency with a 25 year track record encompassing over 600 credit ratings across 25 countries in Africa. In May this year, Moody's Corporation acquired a majority (51%) stake in GCR Ratings, which was expected to further solidify GCRs position as a leading provider of quality, objective and independent credit opinions on African markets.

The forum themed *'A deep dive into REIT Ratings'* was held on 27th July 2022 from 7am – 10am at the Villa Rosa Kempinski Hotel. The keynote presentation was made by Eyal Shevel, Head of Corporate Rating at GCR Ratings and remarks to set the scene for the discussion were presented by Sylvia Chahonyo, East Africa Managing Director, GCR Ratings; Geoffrey Odundo, Chief Executive Officer, NSE; Hilda Njoroge, MRICS, Property Investment Manager, Co-op Trust Investment Services Limited; Justus Agoti, Manager Product Development and Uptake, CMA and Mbithe Muema, Chief Business Officer, NSE.

The keynote presentation highlighted that the largest use of financial instruments ratings within the Capital Markets globally is by REITs and ratings play an important role in managing REIT capital structure and underpinning sustainability of REITs in the long term. Additionally, REIT Ratings unlock quality and sustainable capital raising capabilities within the REIT structure to meet continuous fund-raising requirements. Some of the key risk score building factors include Sector, Portfolio Quality, Management and Governance, Capital and Leverage and Liquidity.

*Sylvia Chahonyo, EA Managing Director, GCR Ratings*

*Geoffrey Odundo, Chief Executive Officer, NSE*

*Eyal Samuel Shevel, Head of Corporate and Public Sector Ratings, GCR Ratings*

*Mbithe Muema, Chief Business Officer, NSE*

*Hilda Njoroge, MRICS, PIM, Co-op Trust Investment Services Limited*

*Justus Agoti, Manager Product Development and Uptake, CMA*

*Irungu Waggema, Chief Officer, Strategy Risk and Compliance, NSE*

*Wendy Owade, RAK Secretariat*

*GCR, NSE, RAK Representatives Group Photo*

# GLOBAL ESG ASSESSMENT OF REITS – A CASE STUDY OF ACORN REITS AND IMPACTS TO STAKEHOLDERS

***Authored by:***
*Wangui Maranga-Okello, Director at Acorn Investment Management Limited and Ruth Okal, Property Investment Manager, ILAM Fahari I-REIT*

## Introduction

Companies have traditionally prioritized financial performance disclosures in their annual reports, but a study by NAREIT in 2022 opined that it is increasingly clear to REIT boards, management teams, shareholders, and stakeholders that a real estate enterprise's total success over time comes about by advancing environmental stewardship, practicing social responsibility, and implementing good governance, among other important corporate pursuits.

NAREIT ESG Report 2022[1] concludes that more REITs are placing ESG at the forefront of their business, with 82% of REITs surveyed reporting that they integrated ESG risks and opportunities into their strategy and financial planning in 2021, up from 77% in 2020, and offer "green financing" options, such as green bonds and climate bonds, to meet investor interest and provide enhanced accountability for sustainability spending and returns.

Locally, The Nairobi Securities Exchange (NSE)[2] recently launched its ESG Disclosure Guidance Manual with an aim to improve and standardize ESG reporting among listed companies in Kenya. Guided by the Global Reporting Initiative Standards of 2021, the NSE Guidance manual spells out the various categories and measures of performance listed companies in various sectors should use to report on their ESG compliance. The NSE is the fourth stock exchange in Africa to launch an ESG Guidance manual.

## Global Trends

Globally, there are a several standard measures of ESG such as LEED (Leadership in Energy and Environmental Design) Certification, IFC Edge Certification, GRESB (Global Real Estate Sustainability Benchmark) Certification and The United Nations Sustainable Development Goals which is part of the 2030 Agenda for Sustainable Development.

1 https://www.reit.com/investing/reits-sustainability/2022-reit-esg-report

2 https://www.businessdailyafrica.com/bd/markets/capital-markets/nse-unveils-rules-social-impact-reporting-firms-3635510

In Kenya, this position is no different; regulators are pushing for ESG compliance but the ESG aspects are spread over several regulatory and policy frameworks including The Environmental Management and Coordination Act (1999); Occupation Health and Safety Act (2007); and the Consumer Protection Act (2012). Policies that companies use to benchmark ESG include the Kenya National Climate Change Action Plan, IFC Performance Standards on Environmental and Social Sustainability, UN Sustainable Development Goals, and the Global Reporting Initiatives Standards. The multiplicity of regulatory and policy frameworks poses a challenge to collection, analysis, and public disclosure of important ESG information in a transparent and comparable format which aligns with international reporting standards.

Globally there is push towards alignment. At the recent COP26 conference, a major step to globally align ESG reporting was announced. Companies[3] and stakeholders have struggled with the myriad of sustainability standards, frameworks and metrics. The International Sustainability Standards Board (ISSB) standards will provide the foundation for consistent and global – environmental, social and governance (ESG) reporting standards that will enable companies to report on ESG factors affecting their business.

## Case Study – The Acorn Student Accommodation (ASA) I-REIT and D-REIT

The Acorn Student Accommodation (ASA) I-REIT and D-REIT this year underwent a rigorous global ESG assessment, with the I-REIT ranked 1st in Africa and 3rd globally in the Student Housing sector, while the D-REIT was also ranked 1st in Africa and 6th globally in the same sector.

This assessment was undertaken by GRESB (formally the Global Real Estate Sustainability Benchmark), an internationally recognized, investor-driven benchmark assessing the Environmental, Social and Governance (ESG) performance of real estate across the globe. In 2021, more than 1,500 property companies, REITs, property funds and developers participated in the Assessment, representing $5.7 trillion in assets under management. The Assessment covers nearly 117,000 assets across 66 countries, and has gained popularity with real estate stakeholders as investors continue to demand for a global benchmark in what the industry considers to be material issues in the sustainability performance of real estate assets.

Why did Acorn choose to have an ESG assessment undertaken for its portfolio of assets under the ASA I-REIT and D-REIT?

- The REITs' investor base continues to grow, with more and more investors looking to increase their allocation to sustainable assets which can be compared to other assets globally in a standardised and fair manner. GRESB is a global gold standard in real estate ESG benchmarking, used by the world's top investors, such as Blackrock, J.P Morgan and UBS Asset Management, who are increasingly focusing on sustainable and climate resilient investments in their portfolios.
- As a real estate owner/manager, the assessment helps to identify the areas of risk, opportunity and impact in the real estate portfolio that can be improved.
- It attracts new investors seeking more comprehensive risk, opportunity, and impact analysis.
- It helps to improve investor engagement.
- It gains a clear picture of your ESG performance, how it compares against peers and what the REITs can do to improve.
- It reports validated ESG performance information to the market using a global industry standard.

Real estate managers, operators or developers willing to have their assets benchmarked are given a 3-month window starting from 1st April every year, to respond to an online survey, which includes collating entity and asset level information in line with GRESB's reporting methodology. The methodology is consistent across regions, investment vehicles and property types, and it aligns with international reporting frameworks.

The entity's performance is then analysed and assessed against a range of indicators and specific sector and/ or regional benchmarks. Once the review is completed, GRESB participants receive an individual score and ranking, alongside a detailed benchmark report that contains high-quality, validated data that investors and participants can use in their investment, engagement and decision-making processes.

The GRESB assessment generates two benchmarks that cover the key ESG real estate indicators:

1. The **GRESB Real Estate Benchmark,** which considers management and performance factors.
   The management component measures an entity's strategy and leadership; policies and processes;

3 https://www.pwc.com/gx/en/services/sustainability/publications/cop26/what-is-the-big-news-at-cop26-for-esg-reporting-pwc-cop26.html

risk management; and its stakeholder engagement approach. This information is drawn from information collected at the organisational level. In Acorn's case, this was collected at the REIT manager level.

The performance component measures an entity's asset portfolio performance, drawn from information collected at the asset and portfolio levels. It is suitable for any REIT, real estate company or fund with operational assets and includes information on performance indicators, such as energy consumption, GHG emissions, water consumption and waste. In Acorn's case, this was collected at the ASA I-REIT level.

2. The **GRESB Development Benchmark,** which considers management and development factors. The development component measures an entity's efforts to address ESG issues during a building's design, construction, and renovation phases. This component is suitable for entities with completed or ongoing projects in new construction (building design, site selection or construction) or under major renovation. Acorn's ASA D-REIT was subjected to this assessment.

## Conclusion

REITs and other entities that adopt responsible investing strategies to enhance unitholder returns are likely to weather financial storms. However, while some of the growing impact of ESG are easily measurable like access to affordable funding and reduction in cost of doing business, others are implicit. Therefore, to effectively determine the nexus between ESG initiatives and its impact on the enterprise value, the business must work through the entire value chain to record, measure and link each consideration in a transparent, comparable and easily understood manner to be disclosed in respective sustainability reports.

### References


i) https://www.pwc.com/gx/en/services/sustainability/publications/cop26/what-is-the-big-news-at-cop26-for-esg-reporting-pwc-cop26.html
ii) https://www.reit.com/investing/reits-sustainability/2022-reit-esg-report
iii) https://www.businessdailyafrica.com/bd/markets/capital-markets/nse-unveils-rules-social-impact-reporting-firms-3635510
iv) https://www.nse.co.ke › NSE-...PDF Nairobi Securities Exchange ESG Disclosures


# REIT 2022 HALF YEAR RESULTS

## ILAM Fahari I-REIT

ILAM
FAHARI I-REIT

## Key highlights from ILAM Fahari I-REIT 2022 Half Year (HY) results:

- New anchor tenant at Greenspan Mall – Naivas Supermarket opened its doors in February 2022
- ILAM Fahari I-REIT issued a cautionary statement regarding a strategic review undertaken which, if approved and implemented, may involve an operational restructuring of the REIT. The process is subject to, inter alia, regulatory and unitholders' approvals. Detailed announcement with all relevant information to be provided at an appropriate time
- REIT received an exemption from withholding tax previously applicable on rental income; subsidiaries now join their parent company in being exempt from corporate and withholding tax on rental income
- REIT manager successful in securing tax exemption letters for REIT subsidiaries; enabled tenants to cease withholding 10% of rental income

## Financial Snapshot:

- **Total net income:** KES. 86.2Mn in June 2022 up by 104% from KES. 42.2Mn recorded in June 2021. Attributable to new anchor tenant at Greenspan Mall
- **Operating expenses:** KES. 100Mn, down by 5.8% from 106.3Mn in the comparative previous year; due to a significant reduction in provision for irrecoverable withholding tax; and lower expenses resulting from the deferral of the AGM expected take place at a later date in the year
- **Total AUM:** KES. 3.68Bn; comprising investment property valued at KES. 3.3 Bn and cash reserves of

KES. 329 Mn

- **Distributable Earnings:** REIT Manager has not recommended an interim distribution for the period ended 30th June 2022. Set to declare full distribution at year end in line with REIT regulations
- **Net Asset Value (NAV) Per Unit:** KES. 19.55 down by 4.6% in the comparative period last year, attributable to decrease in AUM

**Full condensed HY report:** https://ilamfahariireit.com/assets/files/ilam_fahari_ireit_condensed_unaudited_results_30_june_2022.pdf

## Key highlights from Acorn REITs 2022 Half Year (HY) results:

acorn i-reit

acorn d-reit

### Acorn Student Accommodation (ASA) REITs

- I-REIT completed the acquisition of Qwetu Parklands into its portfolio in June 2022
- Qwetu Parklands achieved average YTD occupancy 90%
- Weighted average portfolio occupancy (Qwetu Jogoo Road, Ruaraka and Wilson View) – for 2022 H1 stood at 88%
- Average escalation of 4.7% achieved; effective April 2022; to hedge against inflationary pressures
- Seed properties - Jogoo Road, Ruaraka, Wilson View collectively registered 1.6% increase in fair value from Dec. 21 to Jun. 22
- Rights offer opened in May 2022, successfully closed on 2nd June 2022 having raised KES 433.2Mn; Offer remains open up to 31st October 2022
- 11 properties under the D-REIT either under development or operational – Qwetu Aberdare Heights I, II, Hurlingham, Catholic, Chiromo, Kenyatta University; and Qejani Catholic, Chiromo, Hurlingham, JKUAT and Kenyatta University
- Sale of Aberdare Heights I to ASA I-REIT has received approval, expected to be completed in H2 2022
- D-REIT raised KES. 269 Mn out of target of KES. 405 Mn for supplementary offering memorandum with view to raising funds for issue and subscription of units in the D-REIT
- D-REIT is in the process of closing out a KES 6.7 Bn debt facility to fund up to 10 projects

## ASA I-REIT Financial snapshot

- **Total income:** KES. 191 Mn; up by 31.6% from KES. 145 Mn majorly attributable to increased rental and related income
- **Management Expense Ratio:** 1.0x compared to 1.2x recorded over a similar period in 2021
- **Total AUM:** KES. 4.85Bn up by 25% in the previous year comparative period, due to new acquisition and fair value increase in 3 seed properties
- **Interim distribution:** KES. 64 Mn
- **NAV per Unit:** KES. 20.88 up from KES. 20.80 in December 2021
- **Interim Distribution per unit:** KES. 0.29
- **Interim Distribution yield (based on the value of the units as at 30.6.2022):** 1.8% similar to what was recorded over a comparable period in 2021

**Full 2022 HY report:**
https://acornholdingsafrica.com/wp-content/uploads/2022/08/ASA-I-REIT-2022-Semi-Annual-Report.pdf

## ASA D-REIT Financial snapshot

- **Total income:** KES 105.2 Mn down by 7.8% from KES. 114Mn recorded in June 2021; attributable mainly to increased administrative and fund operating expense and decreased fair value gain on revaluation of investment properties
- **Operating expenses:** KES 92Mn; increased by 14%
- **Total AUM:** KES 9.49 Bn; grown by 56.6% from KES. 6.1 Bn in June 2021 largely due to capex that has gone into the assets of the D-REIT; also overall capital appreciation of 0.1% from December 2021
- **Net Asset Value :** KES 5.58 Bn
- **NAV per Unit:** KES. 23.87 up by 19.4% from the entry value attributable to increase in capital growth
- **Distributable Earnings:** Nil; The ASA D-REIT will not be making any distributions to unit holders as no capital gains realized in the reporting period
- **Dividend payouts;** projected to begin from 2023
- **D-REIT 10 yr. target IRR:** 34.9%
- **Blended 10 yr. return:** 18.3%; projected return based on 30% allocation to the D-REIT and 70% to I-REIT

**Full 2022 HY report:**
https://acornholdingsafrica.com/wp-content/uploads/2022/08/ASA-D-REIT-2022-Semi-Annual-Report.pdf

## Updates from the RAK Secretariat

# RAK OFFICIALS MEET WITH THE ETHIOPIA STOCK EXCHANGE TEAM

On 24th August 2022, the RAK Officials met with the Egyptian Stock Exchange (ESX) Project Implementation Team to benchmark on REITs best practice in Kenya. The team was apprised on how REITs work in Kenya, regulatory frameworks, challenges facing REITs and benefits.

***(Left-Right):** Irungu Waggema, Tilahun Kassahun, Victor Nkiri, Kenneth Masika, Joakim Lange, Michael Habte, Geoffrey Odundo; Front Row: Wendy Owade, Eskedar Sileshi, Lilian Bwire, Hilda Njoroge.*

# UPDATE ON REIT REGULATORY ENVIRONMENT

## Closed Items:

i. **Retirement Benefits Authority investment guidelines** – RBA issued a Legal notice no.72 of 2022 which amended asset category 12 in table G to the First Schedule of the Retirement Benefits (Forms and Fees) Regulation 2000. The revised asset category outlined below:

| *Item* | *Category of Assets* | *Maximum percentage of aggregate market value of total assets of scheme* |
|---|---|---|
| 12. | *All listed and unlisted* Real Estate Investment Trusts incorporated in Kenya and approved by Capital Markets Authority. | 30% |

## Ongoing/Open Items:

ii. **Proposals for Amendments to the Capital Market (REAL ESTATE INVESTMENT TRUSTS COLLECTIVE INVESTMENT SCHEMES) Regulations, 2013** – The REITs Association of Kenya and Kenya Property Developers Association (KPDA) submitted proposals for amendments to the Capital Markets regulations on 16th September 2022. These are currently under review and updates will be shared progressively.

iii. **Proposals for Amendments to Stamp Duty Act** – The lapse of the Stamp Duty Exemption set for 31st December 2022 as stipulated under Section 96A(4) of the Stamp Duty Act. Work is ongoing towards leaving the same open-ended and expand the applicable grounds for the exemption.

iv. **Proposals for Amendments to VAT Act** – There is a need to expressly provide that VAT exemption for REIT transactions also applies to the Special Purpose Vehicle (SPV) entities under it. The exemption is provided under Paragraph 33 of the First Schedule to the VAT Act.

v. **Seeking to clarify whether dividends paid to unitholders are qualifying** or non-qualifying. Usually, dividends paid out by tax-exempt companies are non-qualifying and have no tax preferences. (Should be withheld at a higher rate of 10%, unlike 5%).


**Stay engaged for upcoming REITs Event**

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