

# Impact of COVID-19 on Real Estate Funds, & Cytonn Weekly #25/2020

## Real Estate

### I. Residential Sector

During the week, Unity Homes, a local residential developer, rolled out its first batch of low-cost residential housing apartments in Tatu City, comprising of 48 two-bedroom apartments each with a plinth area of 58 SQM and selling at Kshs 4.25mn, which translates to Kshs 73,310 per SQM, 18.0% lower than Ruiru apartments' average price of Kshs 89,421 in 2019 according to our **Nairobi Metropolitan Area Residential Report 2019**. This is the first phase of the 1,200-unit residential development that is located within a 23-acre community, inside Tatu City. This is the second affordable housing project by the developer locally, after the completion of Unity Gardens in 2018, a 250-unit development in Kapseret, Eldoret, which comprised of 3-bedroom villas each with a plinth area of 95 SQM. The project indicates investor focus on the affordable housing sector as part of the ongoing efforts by the private sector to support the National Government's goal of increasing homeownership in the country. Kenya's Affordable Housing agenda is facing various headwinds such as reduced budgetary allocation towards the programme to Kshs 6.9 bn for FY'2020/21, a 34.3% reduction from the Kshs 10.5 bn allocated in 2019/2020, and the proposed Financial Bill 2020 amendment of the Income Tax Act to do away with Home Ownership Savings Plan (HOSP) tax incentives. Nonetheless, we expect more private developers to continue tapping into the sector to address the ongoing demand for affordable housing which, according to the Government's Boma Yangu website, is currently at 298,193 against the measly 228 units completed in Ngara. Incentives by the government that are expected to draw in the private sector include; (i) a reduction in corporate tax by 50.0% from 30.0% to 15.0% for developers of over 100 affordable housing units annually, (ii) exemption from Value Added Tax for supplies imported or purchased for direct and exclusive use in the construction of affordable houses by licensed Special Economic Zones (SEZ), (iii) reduced customs tariffs such as Import Declaration Fee (IDF) which was reduced from 2.0% to 1.5%, in addition to the scrapping of NEMA and NCA levies of 0.1% and 0.05%, respectively, of the cost of construction, and, (iv) the waiving of building approval fees for all affordable housing projects in Nairobi, under the Nairobi City County Sessional Paper Number 1 of 2018. In light of this, we expect to see more private sector developers undertaking affordable housing projects targeting the low and middle-income earners as the segment presents an investment opportunity supported by the growing demand, which is estimated to be growing at 200,000 units per annum as per National Housing Corporation (NHC). Moreover, for private developers, satellite towns such as Ruiru continue to be attractive for low-cost housing due to the availability of relatively cheaper development land as well as the growth of infrastructure.

### II. Hospitality Sector

During the week, Swiss-owned Planhotel Hospitality Group announced that it was offering holiday bonds, where prospective guests would be required to pay half the cost to reserve a room, for two years for its three properties in Malindi; Diamonds Dream of Africa, Sandies Malindi Dream Garden,

and, Sandies Tropical Village. Under this concept, a one-holiday bond represents one all-inclusive night at any of the 3 resorts where regular room rates range between Kshs 19,000 to Kshs 30,000 per night. However, with the bond, the rooms will be priced at half the regular rates. For example, regular rates at the Sandies Tropical Village Resort are Kshs 19,000 per night, but if a guest buys one-holiday bond, that would be equivalent to 1 night and will go for Kshs 9,500, a 50% discount. Bonds purchased will be valid up to June 2022 and guests can buy as many hospitality bonds as they want which can also be liquidated after buying anytime between now and June 2022. The move signals a shift by the hospitality group towards innovative strategies designed to boost reservations and cash flow at a time when the hospitality sector continues to grapple with the effects of the Coronavirus pandemic, mainly due to its reliance on tourism, as travel restrictions and social distancing rules continue to result in reduced demand for hospitality services. We expect revenues raised through the initiative to help foot operational costs as well as keep the facilities open during downtime caused by the COVID-19 pandemic.

Also during the week, hotel chain, Sarova Hotels, reopened its two Nairobi Hotels, Sarova Stanley and Sarova Panafric. The partial reopening will see operations resume at Sarova Stanley's Thorn Tree restaurant and Sarova Panafric's eatery wing after the hotel chain suspended operations in all its 7 hotels and resorts in March this year, namely; Sarova Stanley, Sarova Woodlands, Sarova Whitesands, Sarova Mara, Sarova Shaba, Sarova Lion Hill, and, Sarova Panafric, in addition to an announcement that it would stop managing the Sarova Taita Hills Game Lodge and Sarova Salt Lick Game Lodge effective July this year. The closures were as a result of strained revenues attributed to the ongoing COVID-19 pandemic. The reopening signals the hospitality sector's gradual recovery backed by various conducive measures by the National Government such as the extension of working hours for hotels and restaurants from the previous closing time of 5.00 p.m. to 7.30 p.m. daily, a move that is expected to see hotels and restaurants raking in more revenues attributed to the increase in operating hours. We expect the hospitality sector's recovery to commence in the near term on the back of government policies aimed at cushioning the sector such as the gradual easing of movement restrictions coupled with monetary allocations through bodies such as TFC aimed at enhancing liquidity.

### **III. Infrastructure Sector**

During the week, Transport Secretary, James Macharia, announced that Kenya was set to open its first annuity road this year under the Annuity programme where contractors design, finance, construct and maintain roads based on agreed periodical payments by the government. The 91km road project in Kajiado County comprises of a 48km section through Ngong, Kiserian and Isinya townships, and will join the 43km Kajiado-Imaroro road. The roads annuity programme dubbed, Roads 10,000 Programme, was approved by the Cabinet in March 2015 as an alternative financing method in response to the government's huge funding gap for its infrastructure investment plans and was to be implemented under the Ministry of Transport and Infrastructure through the roads authorities; Kenya National Highways Authority (KeNHA), Kenya Rural Roads Authority (KeRRA), and, Kenya Urban Roads Authority (KURA). The financing model consists of a variation of PPPs involving private contractors and the government each meeting agreed portions of the total construction cost then thereafter, the government repays the contractor its portion in equal instalments over a set period from the time after a road is completed. Other key road projects to be constructed and maintained through the PPP model include; the ongoing dualling and upgrade of the Nairobi-Mombasa highway, the ongoing construction of the Nairobi-Nakuru-Mau Summit highway, and, the construction of the 2<sup>nd</sup> Nyali Bridge in Mombasa which is expected to kick off in June this year. We expect the government to continue rolling out such innovative financing models in a bid to bridge Kenya's significant infrastructure funding deficit especially at a time when the government is experiencing revenue shortfalls in the wake of an economic slowdown caused by the COVID-19 pandemic, which saw the infrastructure sector get an allocation of Kshs 172.4 bn in the 2020/2021 budget, 60.4% lower than the 435.1 bn allocated in the 2019/2020 budget, the lowest allocation in

the last 10 financial years. Improved road connectivity opens up previously inaccessible areas thus making areas more attractive for investment and results in increased demand for property, which then causes an increase in property prices.

***We retain a neutral outlook on the performance of the real estate sector. We expect the sector to continue being supported by increased demand for low-cost housing, increased infrastructural improvements, and, the hospitality sector's expected recovery in the near term on the back of favourable government policies.***

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