

**Valuation Summary:**

- We are of the view that the ILAM Fahari I-REIT is a “BUY” with a target price of Kshs 13.8, representing an upside of 108.9%, from the current price of Kshs 7.0 as at 19<sup>th</sup> March 2021, inclusive of a dividend yield of 10.7%,
- The I-REIT’s performance in terms of dividend yield at 10.7% is significantly higher compared to the average rental yields recorded in commercial office and retail sectors in FY’2020 with 7.0% and 7.5%, respectively. However, the high dividend yield is largely attributable to the low trading price of the I-REIT, at Kshs 7.0 as at 19<sup>th</sup> March 2021 compared to Kshs 7.9 as at 19<sup>th</sup> March 2020. Additionally, dividends are likely to remain weak due to the current unfavorable economic environment,
- The Fahari I-REIT is currently trading at a P/B of 0.3x and P/E of 8.5x.

**Key Highlights in FY’2020:**

- In May 2020, ICEA Lion Asset Management (ILAM), a local fund manager, announced that it had completed a transaction with Stanlib Kenya Limited (SKL) that would see it acquire the latter’s role of managing the property fund, Stanlib Fahari I-REIT, from South Africa-based Liberty Holdings Ltd. ILAM acquired all rights, obligations, and benefits of SKL in connection with SKL’s role as promoter and REIT manager,
- In June 2020, the Cabinet Secretary for the National Treasury and Planning, Ukur Yatani, drafted rules under the Income Tax (Real Estate Investment Trusts) Rules, 2020 that will require Real Estate Investment Trusts (REITs) to apply for tax exemptions from Kenya Revenue Authority (KRA) during registration. The proposed rules seek to assure investors of the tax exemptions and seal any possible loopholes in tax collection.

**Income Statement:**

- Earnings per unit declined by 15.5% to Kshs 0.82 in FY’2020, from Kshs 0.97 in FY’2019 driven by a 8.4% decline in total operating income to Kshs 347.5 mn, from Kshs 379.2 mn in FY’2019,
- Rental income declined by 0.9% to Kshs 341.2 mn, from Kshs 344.3 mn in FY’2019. Notably, the decline was mainly attributable to the COVID-19 impact on the retail and commercial office sectors which has led to rent rebates for struggling tenants thus, suppressing rental income growth,
- Interest income decreased by 10.3% to Kshs 22.4 mn, from Kshs 25.0 mn in FY’2019 due to the downward readjustment on interest rates being experienced in the market due to the cumulative 1.5% downward revision in the Central Bank Rate (CBR) to the current 7.0% coupled with the bias by banks towards government securities as opposed to lending due to increased credit risks,
- Total operating expenses grew by 1.8% to Kshs 229.6 mn in FY’2020, from Kshs 225.6 mn in FY’2019 attributable to the 14.0% growth in Property Expenses to Kshs 130.4 mn, from Kshs 114.3 mn in FY’2019. The growth was however weighed down by a 10.8% decline in Fund Operating Expenses to Kshs 99.2 mn, from Kshs 111.3 mn in FY’2019,
- Distributable earnings declined by 6.7% to Kshs 134.4 mn, from Kshs 144.0 mn in FY’2019. The fund manager attributed the decline to the higher property expenses arising from a significant provision for bad debts as a result of non-performance of the anchor tenant at Greenspan Mall. This was partially offset by a reduction in fund operating expenses after the REIT Manager temporarily reduced their fees by 10.0% to cushion the investors during a particularly difficult year,
- Net profit declined by 15.5% to Kshs 148.0 mn in the period under review from Kshs 175.2 mn in FY’2019, driven by an 8.4% decline in total operating income to Kshs 347.5 mn, from Kshs 379.2 mn in FY’2019, coupled with a 1.8% growth in operating expenses to Kshs 229.6 mn, from Kshs 225.6 mn in FY’2019. Notably, fair value of investment property declined by 56.4% to Kshs 13.6 mn, from Kshs 31.2 mn in FY’2019, and,

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- The REIT recommended a Kshs 108.6 mn dividend distribution to its unitholders at Kshs 0.60 per unit. At the current price of Kshs 7.0, this translated to a dividend yield of 10.7%.

#### **Balance Sheet:**

- Total assets increased marginally 0.1% to Kshs 3,883.7 mn, from Kshs 3,878.4 mn in FY'2019, driven by a 105.9% increase in Cash and Cash Equivalents to Kshs 197.8 mn, from Kshs 96.1 mn in FY'2019, coupled with a 0.7% increase in investment in property to Kshs 3.48 bn, from Kshs 3.46 bn in FY'2019. The growth was however weighed down by the 37.0% decline in Investment securities to Kshs 150.4 mn, from Kshs 238.9 mn in FY'2019,
- Total liabilities decreased by 6.1% to Kshs 108.0 mn, from Kshs 115.0 mn in FY'2019 attributable to the 6.1% decline in trade and other payables to Kshs 108.0 mn, from Kshs 115.0 mn in FY'2019. The REIT remained without debt as at FY'2020,
- Shareholders' funds grew marginally by 0.3% to Kshs 3.78 bn in the period under review, from Kshs 3.76 bn in FY'2019 and thus, the REIT closed with a Net Asset Value of Kshs 20.86 per share, 4.3% higher than its listing price of Kshs 20.0,
- The REIT currently has a Return on Assets of 3.8% and a Return on Equity of 3.9%.

Ratios Summary	H'1 2017	FY'2017	H'1 2018	FY'2018	H1'2019	FY'2019	H1'2020	FY'2020	Y/Y Change (% Points)
ROA	2.1%	4.5%	1.8%	5.0%	2.0%	4.5%	2.3%	3.8%	(0.7%)
ROE	2.2%	4.7%	1.8%	5.2%	2.1%	4.7%	2.3%	3.9%	(0.7%)
Debt Ratio	3.3%	2.5%	3.4%	3.3%	3.0%	3.0%	2.7%	2.8%	(0.2%)
PBT Margin	41.6%	46.0%	37.7%	49.7%	39.4%	46.2%	47.8%	42.6%	(3.6%)
Rental Yield	3.2%	7.0%	2.0%	5.7%	2.2%	5.1%	2.5%	4.3%	(0.8%)

#### **Performance:**

- On the bourse, the REIT continued to perform poorly trading at an average of Kshs 6.7 in FY'2020 and closing the period at Kshs 7.0, 65.0% lower than its initial listing price of Kshs 20.0 and 66.4% lower than the net asset value per unit of Kshs 20.86 as at FY'2020, an indication of the continued lack of investor appetite for the instrument,
- We expect the REIT's revenue to continue declining in the near term due to COVID-19's impact on commercial office and retail sectors which is expected to continue suppressing rental income growth.

**Below is a summary of the key line items in the balance sheet and income statement;**

*Figures in Kshs bn Unless Stated Otherwise*

Balance Sheet	H1'2017	FY'2017	H'1 2018	FY'2018	H1'2019	FY'2019	H1'2020	FY'2020	Y/Y Change
Total Assets	3.69	3.76	3.72	3.85	3.78	3.88	3.82	3.88	0.1%
Total Equity	3.57	3.67	3.60	3.72	3.66	3.76	3.71	3.78	0.3%
Total Liabilities	0.12	0.10	0.13	0.13	0.11	0.12	0.10	0.11	(6.1%)

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Income Statement	H1'2017	FY'2017	H'1 2018	FY'2018	H1'2019	FY'2019	H1'2020	FY'2020	Y/Y Change
Rental Income	0.14	0.28	0.14	0.31	0.17	0.34	0.17	0.34	(0.9%)
Income from Other Sources	0.05	0.10	0.04	0.06	0.01	0.03	0.01	0.02	(9.7%)
Operating Expenses	0.11	0.23	0.11	0.24	0.11	0.23	0.10	0.23	1.8%
Profit Before Tax	0.08	0.17	0.07	0.19	0.08	0.18	0.09	0.15	(15.5%)
Basic EPS	0.43	0.95	0.36	1.07	0.42	0.97	0.48	0.82	(15.5%)