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Real Estate

Kenya
Trends & Developments

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Trends and Developments

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When COVID-19 was declared a public health emergency in 2020, economic activity was brought to a near global standstill, as governments imposed restrictions on movement to contain the spread of the virus. This unexpected turn of events affected many sectors in Kenya, including the real estate industry, and it continues to be a factor in key industry decisions amid COVID-19's ongoing grip on the world. Studies have shown that the Kenyan economy contracted in 2020 due to the global ripple effect.

For this reason, it is important to take account of the developments that occurred in 2020 before highlighting the trends and developments we expect to see in 2021.

The first quarter of 2020 saw the government of Kenya issue ministerial directives concerning social, health and safety requirements and impose curfews, travel restrictions and county lockdowns. This negatively impacted various property segments, in particular retail, commercial, travel, hospitality and leisure. As an example, the effect of these measures and the strenuous economic conditions led to a decline in the demand for office space, as tenants reassessed their office requirements in response to many employees working remotely over the pandemic period. Where existing tenants retained their office space, they sought to suspend rental payments to cushion themselves from the economic shock caused by the pandemic, leading landlords to consider flexible rental payment plans. Similarly, hotels across the country had to shut down as travel was affected for almost six months, costing the industry billions of Kenyan shillings. Hosts of short-term rentals such as Airbnb also had to turn to longer-term rental income due to a significant decline in users.

COVID-19 morphed into a financial crisis, leading to a decline in uptake of banking facilities caused by anxiety as well as uncertainty concerning the ability to service loans. Many companies took steps to minimise borrowing and overheads in the second quarter of 2020 by downsizing or foregoing their office space.

Prior to the COVID-19 period, services at the land registries were already affected by the disruptions caused by the ongoing transition to a digital platform. The onset of COVID-19 compounded this issue due to the physical closure of land registries within the country which crippled operations.

In terms of what lies ahead for an economy that relies on the hardest hit sectors for economic growth, we are inclined to the proposition that levels of disposable income are expected to decline therefore constraining investment in real estate. Looking at the changes happening due to the pandemic, occasioned by the first wave, the second wave and the current third wave of COVID-19 which has hit the country leading to revised containment measures announced by the president on 26 March 2021, and also considering the market's reaction previously and presently, we now take you through what we anticipate will be the trends and developments in the year 2021, as well as ongoing developments.

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The Impact of COVID-19 on Kenya's Real Estate Sector and Emerging Trends for 2021

Commercial sector

As stated earlier, the commercial property space in Kenya witnessed a significant decline in office space absorption due to the disruption caused by COVID-19. The work-from-home approach employed to curb the spread of the virus has led experts to project a further decline in demand beyond the first quarter of 2021, as remote working is increasingly becoming a mainstream way of life. Executives are expected to rethink their real estate strategies over time as the workplace is evolving to accommodate remote and hybrid workplace options.

Separately, the stringent health and safety requirements introduced as a result of COVID-19 have necessitated the provision of a safe and healthy environment for workers. Developers are now employing design strategies aimed at confronting the impact of infectious diseases to protect occupiers of buildings.

Residential sector

In June 2020, the Kenya National Bureau of Statistics (KNBS) released the results of a survey which indicated that in six out of every ten households, the breadwinner was unable to provide due to the COVID-19 pandemic.

Given the resultant impact on livelihoods due to pandemic-related lay-offs and redundancies, thousands of Kenyans struggled to pay rent, with some requesting landlords to reduce or waive the rent, and others moving to cheaper housing options or opting to relocate from urban spaces to rural towns to save on costs.

As a result of these relocations against the backdrop of falling incomes, satellite towns such as Ngong, Thika and Kitengela have experienced increased rentals and demand for property, with consumers looking to rent cheaper decent housing and seeking to purchase affordable land within a reasonable distance from Nairobi. We see the purchase of land and property in satellite towns as a trend in 2021. As such, offering serviced plots or quality houses in satellite towns is something investors can consider.

On the flip side, the rise in demand for cheaper or more affordable rental options has led to a high tenant turnover in high-end developments. We expect to see this trend continue, thus catalysing the potential for private developers in the affordable housing market.

Hospitality sector

Due to the COVID-19 pandemic, the world's economy was shut down almost overnight, with the hospitality industry facing an unprecedented challenge as a result. Strategies to flatten the COVID-19 curve, such as community lockdowns, social distancing, stay-at-home orders, and travel and mobility restrictions, resulted in temporary closure of many hospitality businesses and significantly decreased demand in those that were allowed to resume operations.

With government support and campaigns for domestic tourism, we have seen renewed hope for the hospitality industry in Kenya. The Christmas season in 2020 offered hospitality stakeholders a means to offset the impact of the pandemic and resulted in a booking rate of more than 65% in almost all hotels, a first for many after a long and bleak year due to the pandemic. However, the current third wave of COVID-19 that has hit the country may derail progress as it may demotivate tourists from going ahead with their travel plans, even though the government has urged international tourists who have booked to travel to Kenya not to cancel as they are free to tour the country, provided they have a valid COVID-19 negative certificate and can hire private planes to their destinations within the country.

Having said that, investment in the tourism sector is not projected to trend in 2021 unless an investor seeks to invest in eco-tourism with facilities that will ensure minimal or no crowding. Beachfront properties and bush adventures continue to be the most popular tourist attractions for investment purposes.

Holiday homes are increasingly growing in popularity in Kenya, with Naivasha being much sought after as a holiday/second home destination for the upper and upper-middle classes. With the pandemic throwing mainstream tourism into disarray, holiday homes will become increasingly lucrative as a means for holiday-goers to escape the city while ensuring minimal contact with other tourists.

Retail malls

The retail sector in Kenya appears to be resilient to the effects of the COVID-19 pandemic. Although the sector has experienced a period of stunted occupancy due to over-supply, reports indicate that occupancy levels for retail centres averaged 70% to 80% with the more established malls recording higher occupancy levels of 90%. Knight Frank's Kenya Market Update for the second half of 2020 further indicates that some supermarket chains expanded their local presence, establishing a stronger footprint in the retail market. A few supermarkets scaled down operations mainly due to liquidity problems but the spaces they occupied as anchor tenants have already been taken up by competitors.

We project that the aggressive expansion of retail chains will continue in 2021.

Land

The 2020 third quarter report by Cytonn Investments, an investment and real estate company in Kenya, indicated that the land sub-segment recorded an overall annualised capital appreciation of 2.4% at the end of that quarter. This suggests that investors still consider land as a good investment in the long term.

Our view is that this sub-segment will improve, as the market seems more stable in 2021.

Agricultural sector

This sector has exhibited growth that defies COVID-19 and continues to be lucrative, especially in vegetables and tea. Agriculture plays a vital role in the economy and due to this, there is a sustained demand for farming land. While inflation has risen in the country, the agricultural sector has remained profitable. We see this continuing in 2021.

Health sector

With hospitals being occupied beyond capacity with COVID-19 patients in 2020, as well as the first quarter of 2021, and their insurance cover plans being rejected, we see health as an important sector that can yield returns for investors. We have highlighted it here, as any investment in the health sector is likely to have a real estate angle, with real estate necessary for the construction of hospitals and facilities.

Education sector

The economy in 2021 has a positive outlook as a result of pupils returning to school, even though there may be phased temporary closures every now and then. Indeed, with the closure of many private schools, this is definitely a sector that should attract investors, especially those that offer online or hybrid solutions, adequate spacing within classrooms and good green facilities in schools, all of which will require investment in real estate through the acquisition of properties in the relevant location.

Contract drafting and negotiation

The effects of the COVID-19 pandemic have led to a shift towards contract-drafting strategies that protect parties to leases (particularly tenants) from economic hardships brought about by the pandemic. There has been an unprecedented increase in lease modifications incorporating alternative clauses providing relief to parties, as guided by the disruptions caused by COVID-19.

Affordable Housing

The Kenya Mortgage Refinance Company (KMRC), the public-private partnership (PPP) firm formed by the government of Kenya, was established as a key institution to support the affordable housing pillar of the government's Big 4 Agenda. It was incorporated on 19 April 2018 as a non-deposit taking financial institution with the single purpose of providing long-term funds to primary mortgage lenders (ie, banks, micro finance banks and saccos, which are savings and credit co-operatives) in order to increase the availability and affordability of mortgage loans to Kenyans.

KMRC was licensed by the Central Bank of Kenya in September 2020 to commence lending. Its licensing as the first mortgage refinance company in Kenya is expected to facilitate the growth of the affordable housing market. By making mortgages affordable for larger sectors of the population, and capping affordable housing loans at KES4 million in Nairobi and KES3 million with respect to the rest of the country, the affordable housing pillar of the Big 4 Agenda will be supported.

The government expects that KMRC will contribute to more home ownership through cheaper mortgages since it will source loans from big investors and multilateral lenders and act as a pool from which mortgage lenders in the country can draw at affordable rates.

Changes in the Dispute Resolution Landscape

On 1 July 2020 the Kenyan Chief Justice launched the E-Judicial system which features virtual court sessions and a paperless court case management system. Although litigants, practitioners and judicial officers are still interacting with the new system (and there have been some challenges), dispute resolution through virtual hearings is seen as a big step towards helping improve access to justice and speedy resolution of land disputes.

Nairobi Railway City

The government of Kenya through the State Department for Housing and Urban Development (SDHUD) under the Ministry of Transport, Infrastructure, Housing and Urban Development and Public Works affirmed its commitment to the construction of Nairobi Railway City when it invited interested and eligible candidates to tender for the development of the railway city and related amenities in July 2020.

The total area for the project is 172 hectares (425 acres) and is said to be the largest and most ambitious development to be undertaken in the Nairobi metropolitan region since independence. The features include a diverse urban programme comprising mixed-use commercial, offices, residential and public buildings with wide open space and plazas, and elaborate non-motorised/pedestrian walkways. The diverse urban programmes are expected to generate a 24-hour dynamic city.

The main aim of the project is expansion of the central business district and development of a railway station to link all city suburbs. The government hopes that Nairobi Railway City will transform Nairobi into a sustainable, integrated and iconic city reflecting a transformative vision for urban planning.

With regard to real estate, the project is intended to capture land value for sustainable urban regeneration of the project area and development. Furthermore, an integrated railway transportation network can aid in transit-oriented development, maximising residential, business and leisure space. Such infrastructure development could also open up remote areas for real estate development and strengthen housing values in those areas.

Changes in the Tax Regime

Effective 1 January 2021, the government enacted fundamental changes to the tax regime, some of which directly affect the real estate industry.

Residential Rental Income Tax (RRIT)

The upper threshold of RRIT has been increased from KES 10 million to KES15 million per annum. The lower threshold has also been increased from KES144,000 to KES288,000.

These wider tax bands will increase the number of landlords who fall within the ambit of the tax.

Home Ownership Savings Plan (HOSP) amendments

Depositors no longer enjoy a tax deduction on deposits placed with an approved HOSP institution. Previously, contributions of up to KES96,000 per annum to a registered HOSP were treated as an allowable deduction.

Furthermore, the income of a registered HOSP, which was previously exempt from income tax, is now taxable.

System Overhaul at the Lands Registry

The Lands Registry will be undergoing a system overhaul that is expected to improve efficiency in the long term but may occasion delays in land transactions in the short term.

The ongoing land title conversion

On 31 December 2020, the cabinet secretary for Lands and Physical Planning notified the public, by way of a Gazette Notice, of the commencement of conversion of current title numbers to new parcel numbers, starting with Nairobi. The aim is to collapse the land registration system under the previous land laws which were repealed in 2012, to ensure a centralised and simpler land registration process, and reduce susceptibility to fraud.

What the conversion process means for landowners

Titles issued under the previous regimes will be cancelled and replaced with titles under the current regime.

There will now be a centralised land registration process under one regime, in line with the constitution.

The conversion is an ongoing process which we expect will take place over the next few months or more. There will be further publications in the Kenya Gazette and two daily newspapers of conversion lists covering other parts of the country. We are not certain how expeditious the process will be or whether conveyancing proceedings will stall in anticipation of migration from the old to the new system.

While the conversion of titles is not an economic issue per se, it will affect the time it will take to finalise land transactions. In an already volatile real estate market, the longer it takes to finalise registration, for instance, the harder the economic implications, especially since the release of funds is invariably pegged on registration being completed.

Implementation of the National Land Information Management System (NLIMS)

The government's policy is to digitalise all land transactions and do away with the current manual system. It is intended that all processes from allocation of land, issuance of titles, change of user, subdivision, transfer, charge, etc will be undertaken on the new NLIMS. The Ministry recently indicated to stakeholders that it has finalised the scanning of land records within the Nairobi metropolitan area and that it expects to launch the NLIMS in the first quarter of 2021. It is difficult to assess whether the Ministry will meet this target as the system is yet to be launched. In addition, the Ministry explained to stakeholders that it will first undertake the land title conversion process, so that all properties are able to comply with the requirements of the NLIMS.

It is projected that digitalisation of land records for the remaining parts of the country will be concluded in 2022, before the end of the current president's term. This is intended to improve efficiency in the long run.

Improved capacity at the land registries, including introduction of accredited private valuers

On 22 January 2021, the Ministry published a list comprising 247 accredited private property valuers approved to carry out valuation for stamp duty, in a move to enhance efficiency by decreasing turnaround times for conveyancing.

It is anticipated that the wide reach of private property valuers will boost government revenue, improve ease of doing business, decrease the turnaround time by up to 50% and improve Kenya's international ranking in processing property deals, which is currently at 134 out of 190 countries.

Regulatory changes towards electronic signatures

On 18 March 2020, Parliament enacted the Business Laws (Amendment) Act 2020, with the aim of facilitating the ease of doing business in Kenya by providing for the use of advanced electronic signatures in place of the traditional signature. The new law came into effect at a time when the government was also fighting to contain the spread of COVID-19 through different media, including paper.

While electronic signatures are not a new concept in Kenyan law, the above law did away with the need for wet-ink signatures in virtually all legally binding documents, except for wills and negotiable instruments, such as cheques. Although this is a progressive regulatory change, electronic signatures are not yet available in Kenya as, by law, a valid advanced electronic signature can only be issued by a Certification Service Provider (CSP) duly licensed by the Communications Authority of Kenya pursuant to the Kenya Information and Communications (Electronic Certification and Domain Name Administration) Regulations 2020. At present, there are only two licensed CSPs in Kenya, which are yet to start issuing advanced electronic signatures.

The new Sectional Properties Act

The new Sectional Properties Act 2020 (the Act) came into force on 28 December 2020, effectively repealing the Sectional Properties Act 1987. The Act now conforms to the new land regime that came into force in May 2012. It also addresses the challenges associated with the repealed law which mainly relate to provisions perceived as strenuous and burdensome.

The Act now requires all long-term sub-leases issued before the commencement of the Act, intending to confer ownership of apartments, flats, maisonettes, townhouses or offices, to be reviewed within two years of the commencement date of the Act. The aim is to enable conversion to conform to the requirements of the Land Registration Act 2012 with regard to georeferencing and issuance of certificates of title and certificates of lease, as applicable. This is expected to pave the way to a clear practical approach to how to efficiently register titles for apartments and sectoral units.

Impact of Upcoming General Elections/ Political Environment

Kenya holds its general elections every five years and the next election is scheduled to take place on 9 August 2022. The upcoming elections and political environment may have a greater-than-usual impact on business and investment, especially with the effects of the pandemic still being felt in the country. Investors presently tend to be reluctant to invest in new opportunities and/or projects in the country as they have adopted a wait-and-see approach, largely attributable to the uncertainties of transitioning to a new government. This is likely to have a negative short-term effect on the real estate market.

Conclusion

From our review of the above, we see a positive to neutral outlook for the real estate industry in 2021, especially following the global roll-out of the vaccine which raises hope for the containment of COVID-19. However, investors should be mindful that most businesses may be restructuring and downsizing their operations to survive another year of uncertainty prior to the 2022 general elections in Kenya, thus affecting uptake.

Dentons Hamilton Harrison & Mathews has a robust real estate practice team, consisting of five partners and ten associates, that provides advice on various aspects of real estate transactions. The team provides advisory and transactional support in REITS, construction, real estate tax, real estate investment and development, real estate partnerships, fractional ownership and franchising within the hospitality industry. In addition, the practice offers a wide range of practice knowledge and services in business-related areas, including banking and finance, insolvency and debt restructuring, infrastructure and projects, regulatory compliance and corporate structuring. The firm has a well-established local and global presence, with two offices in Kenya (Nairobi and Mombasa) and as part of Dentons, the largest law firm in the world with access to over 185 office locations globally and more than 1,100 real estate lawyers worldwide. Some of the practice's key clients include government and state corporations, hotels, and construction companies.

The firm would like to thank Lydia Akinyi Owuor and Nasra Nanda for their contribution to the guide.

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Adil Khawaja is the managing partner of Dentons Hamilton Harrison & Mathews. He has over 27 years' experience in real estate, environmental and planning law, as well as in-depth knowledge of project development. He offers clients practical, tailor-made legal solutions, drawing on his expertise in these areas. Adil is one of the most renowned lawyers in Kenya in his field, having dealt with complicated land issues and undertaken numerous complex company restructurings and realisations.

Lorna Mainnah has over 12 years' experience in real estate, environmental and planning law. She has in-depth industry knowledge and transactional experience in all aspects of negotiating, structuring and implementing various forms of real estate financing and investment transactions as well as in the development of top-end commercial real estate deals, including in the office, retail, hotel and industrial sectors. Lorna has advised on a multitude of complex land transactions, including the development of Kenya's first grade "A" logistic and distribution warehouse park. Clients appreciate her negotiating skills and highly effective approach in handling complex transactions.

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