Office buildings:

Some thoughts on the decentralization trend in SA

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Worldwide, the tertiary or services sector of the economy -- manned to a large extent by knowledge workers -- is growing much faster than the manufacturing of goods (secondary sector) and the production of raw materials in the primary sector (agriculture and mining). South Africa is no exception, which goes a long way explaining the widening income gap between the poor and well-off. It's all about knowledge and education.

Workers in the tertiary sector are housed in office buildings, so over the past half century the demand for office space has been outpacing the demand for manufacturing space. Historically, office space was predominantly located in the metropolitan CBDs to take advantage of agglomeration economics. However, with the suburbanisation of cities, the need for decentralized office space, viz. offices closer to home, has been growing in many countries, and South Africa was no exception.

Simultaneously, in the 1980s, the CBDs in South Africa began a process of degradation, and with it started the exponential growth of decentralized office nodes. This trend has gathered pace ever since and today our cities reflect the two-nations economy: the middle class and the poor. The poor do business in the regressing old metropolitan CBDs, whereas the middle class patronize the posh decentralized nodes like Umhlanga Ridge (Durban) and Sandton (Johannesburg). These upmarket nodes are typically anchored by super-regional shopping centres.

The only exception in South Africa is the Cape Town CBD. There are two reasons for Cape Town's exception. First, it is on the mountain side bordered by high-income residential areas, where decision-takers live, and who evidently want to work close to home. Second, the regression in Cape Town central was close to tipping point when in November 2000 -- in the nick of time − the Central City Improvement District (CCID) was established by local property owners. The turning point is vividly documented by the peaking of capitalization rates – as reported at the time by the *Rode Report* − a few quarters after the establishment of the CCID.

In contrast, the CIDs in the other metropolitan areas were established after passing the tipping point, but these CBDs are in any case not bordered by upmarket residential areas.

The continued success of the Cape Town CBD was strengthened by the rise of the exclusive neighbouring V&A Waterfront, including its recently developed Silo District. As a result, the traffic to and from the greater CBD has become a nightmare. Yet, going by the market rental rates commanded by the greater CBD, office users are prepared to pay this price for the 'address' offered by the CBD and environs.

This brings us to the 'best' office nodes in the country. No doubt, using the latest *Rode Report*, some of the highest market-related grade-A rentals are achieved in Rosebank (R190 per m² per month gross), and Sandton CBD (R179) (both thanks to the Gautrain stations), and the Silo District in the V&A Waterfront (R185). In fact, considering the market rentals of all the nodes in the Cape Peninsula, it is evident that the greater CBD nodes command the highest rentals. This is the only CBD in South Africa where the central nodes outperform the decentralized nodes.

In contrast, Umhlanga Ridge and La Lucia, the best nodes in Durban, can only muster R140 for grade-A space.

The market-rental rate that a node commands is a good gauge of its attractiveness because all the good and bad news of a node is encapsulated in the market rental rate. The exception to this is where a node has a temporary high vacancy because of over-enthusiastic development in the wake of the node's popularity with developers and investors. Sandton CBD is a good example of this.