State of the property market in quarter 1 of 2009

The following are the significant findings or conclusions made in this issue of *Rode's Report*:

- Are cap rates topping?
- Office market still in upswing
- Industrial rental growth curbed to single digits
- Tough times ahead for the affordable house market

Quantitative overview of the property market

Table 1 provides a snapshot of how the property market has performed over the past four quarters by comparing the latest information (quarter 2009:1) with that collected a year earlier.

Table 1
The property market at a glance at quarter 2009:1*
% growth on four quarters earlier (on smoothed data)

	Nominal	Real**
Prime CBD office rentals		
Johannesburg	23,7	20,7
Pretoria	4,4	1,5
Durban	20,4	17,0
Cape Town	3,9	1,2
Prime decentralized office rentals		
Sandton CBD	-1,0	-3,7
Randburg Ferndale	17,4	14,4
Brooklyn/Waterkloof (Pta)	19,2	16,3
Hatfield	21,9	18,9
Berea (Durban)	21,3	18,1
La Lucia Ridge	16,4	13,1
Claremont (CT)	23,1	19,2
Tyger Valley	14,7	11,8

* Unless otherwise specified
** Nominal values deflated by BER Building Cost Index; however, house prices are deflated using the Haylett Index.

Table 1 (continued)
The property market at a glance at quarter 2009:1*
% growth on four quarters earlier (on smoothed data)

	Nominal	Real**
Prime industrial rentals (500m² units)		
Central Witwatersrand	7,6	4,7
Pretoria metro	6,2	3,1
Durban metro	4,2	1,3
Cape Peninsula	1,0	-1,7
Port Elizabeth	7,6	4,7
House prices (all classes)* **		
Johannesburg metro	-2,6	-2,7
Pretoria metro	-0,5	-0,6
Durban metro	-12,7	-12,8
Cape Town metro	-4,2	-4,3
Port Elizabeth	-11,0	-11,0
Flat rentals (standard quality, all sizes)		
Johannesburg metro	5,7	-3,2
Pretoria metro	5,1	-3,8
Durban metro	8,7	-0,5
Cape Town metro	6,4	-2,6
Port Elizabeth	6,8	-2,1

* Unless otherwise specified
** Nominal values deflated by BER Building Cost Index; however, house prices and flat rentals are deflated using the Haylett Index and the Consumer Price Index respectively.
*** Based on Absa's house price indices

Capitalization rates

In the first quarter of 2009, capitalization rates in general pointed south from their previous-quarter levels. This, we believe, is in response to declining interest rates.

Office rentals

On the whole, rentals grew by impressive rates of 19% in Pretoria and Durban decentralized, followed by Cape Town and Jo-hannesburg decentralized, where rental growth of 14% and 8% respectively was achieved. Over the same period, building-cost inflation, as measured by the BER BCI, is expected to have contracted mildly by 0,7%, translating into amazingly strong *real* rental growth in all of the decentralized office areas.

As for the CBDs, Johannesburg performed the best with nominal rentals growing by a notable 24%. In the CBD of Durban, rentals were up by 20%, while in the Pretoria and Cape Town CBDs rental growth of 4% was achieved.

Industrial market

At the moment, sharp falls in retail sales and manufacturing output continue to suggest the likelihood of weaker demand for industrial space, and of course, moderating industrial rental growth.

Unsurprisingly, in the first quarter of 2009, rental growth in all of the major industrial conurbations was curbed to the single digits. The strongest growth was recorded in the Central Witwatersrand, where rentals grew by 8%; this was followed by Durban (6%), the Cape Peninsula (4%) and Port Elizabeth (1%). Nonetheless, these growth rates were still good enough to beat the expected growth in building costs (-0,7%), thereby resulting in real rental growth.

Flat rentals

There's still no magic on the flat rental front, with rental growth generally fizzling out across all of the major metropolises.

In the first quarter of 2009, rental growth in Johannesburg slowed to 6%. In the other metropolises such as Durban (9%), Port Elizabeth (7%), Cape Town (6%) and Pretoria (5%) rental growth was also curbed somewhat by rising vacancies. Given consumer inflation of 8,4% for the first quarter of 2009, means *real* rental growth declined across all of the regions.

The house market

In April 2009, house-price growth continued to march south with prices on a national basis down by roughly 3% on the same month a year earlier. More thought-provoking, however, are the trends currently emerging amongst the various value bands.

In January 2009, prices in the affordable category were still up by 4% on a year-on-year basis. In contrast, prices in all the other value bands were actually lower than a year ago. The eye-opener, however, is the trends in the month-on-month annualised growth rates. In January 2009, the annualised monthly growth rate in the affordable category was a mind-boggling minus 28%. Of course, given the ultra smoothness of the index, one can conclude that, should this month-on-month growth persist over the next twelve months, then price levels in the affordable category will be 28% lower in a year's time.

The building industry

The overall health of the building industry remains weak and is about to enter intensive care mode.

Growth in the *real* value of new non-residential buildings put in place has decelerated to a single-digit rate of 8% in the fourth quarter of 2008. But, this is not too bad if one considers the woes of the residential sector, where, unsurprisingly, the *real* value of new residential buildings put in place contracted by almost 8% over the same period. Another straw in the wind is cement sales – a fairly good indicator of building-construction activity – which have been declining since the beginning of 2007 and which continue to reflect the current weakness in the building industry.

These trends will no doubt affect building costs. Thus, in the first quarter of 2009, growth in building-input prices, as measured by the Haylett index, is expected to have ground to a halt – showing no growth over the past year. This is the result of lower demand for building materials and labour. Similarly, the BER BCI's measure of building-cost inflation – arguably a truer indication of the health of the building industry because it includes non-residential contractors' profit margins – contracted, albeit slightly, by 0,7% over the past year. This is because contractors are now being forced to trim their profit margins due to keener tendering competition on the back of fewer new projects. ■