State of the property market

State of the property market in quarter 1 of 2010

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

- The business-cycle downswing is still weighing down on rents
- The FIRE sector continues to shed jobs, putting pressure on office vacancies
- The trends in residential rentals reflect the distress being experienced by households.

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 2010:1) with that collected a year earlier.

Table 1
The property market at a glance at quarter 2010:1*
% growth on four quarters earlier (on smoothed data)

	Nominal	Real**
Prime CBD office rentals		
Johannesburg	-3,9	-3,8
Pretoria	6,0	6,3
Durban	5,2	5,6
Cape Town	-2,1	-1,9
Prime decentralized office rentals		
Sandton CBD	-10,6	-10,2
Randburg Ferndale	-3,8	-3,5
Brooklyn/Waterkloof (Pta)	10,0	10,1
Hatfield	12,5	12,6
Berea (Durban)	7,8	8,0
La Lucia Ridge	3,7	4,1
Claremont (CT)	-10,1	-9,4
Tyger Valley	-10,7	-10,5

* 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 2010:1* % growth on four quarters earlier (on smoothed data)		
	Nominal	Real**
Prime industrial rentals (500 m² units)		
Central Witwatersrand	-6,6	-6,3
Pretoria metro	-5,0	-4,4
Durban metro	-1,6	-1,2
Cape Peninsula	-3,4	-3,0
Flat rentals (standard quality, all sizes)		
Johannesburg metro	0,1	-5,5
Pretoria metro	-0,3	-5,9
Durban metro	1,1	-4,5
Cape Town metro	1,1	-4,6
Port Elizabeth	-3,0	-8,4

* 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.

Capitalization rates

In the first quarter of 2010, capitalization rates remained at roughly the same level they were in the previous quarter. Thus the adjective that best describes the situation is 'stable'.

The fact that *real* office, industrial and mall rentals are shrinking, could eventually lead to property investors requiring higher minimum income returns to invest in property. Having said that, owners are seemingly — despite the impact that the business-cycle downswing is still having on their income streams — not under any duress to sell. This could, naturally, lead to a continuation in the capitalization rate stalemate.

Office rentals

A look at the yearly growth in market rentals highlights the lagged impact that the business cycle downswing is having on the office property market.

In the first quarter of 2010, only market rentals in Durban decentralized (+5%) could muster growth in excess of the expected growth rate in building-cost inflation (+2,6%). In Pretoria (+2%), Johannesburg (-5%) and Cape Town decentralized (-7%) the growth in market rental was, on average, below that of building-cost inflation. This, of course, means that in all of these three regions, *real* rentals are currently lower than they were a year ago.

Industrial market

Although the stilts of the industrial property market — namely manufacturing activity and retail sales — can be said to be in recovery mode, the strength and sustainability of the recovery remains an uncertainty. This uncertainty comes mainly against the backdrop of a South African economy that is still shedding jobs, and a wobbly world economy.

It follows that uncertainty regarding the industrial property market's supporting stilts also means uncertainty regarding market-rental prospects. In fact, in the first quarter of 2010, market rentals continued to contract. On the Central Witwatersrand (-7%), in Durban (-5%), Port Elizabeth (-3%) and the Cape Peninsula (-2%) market rentals were lower than a year ago.

Flat rentals

Flat rentals are at the moment continuing to move sideways.

In the first quarter of 2010, flat rentals in Durban and Cape Town could only scrape together growth of 1%, while in Johannesburg and Pretoria rentals were at the same level they were a year ago. Naturally, one can presume that the poor growth in flat rentals is indicative of the financial distress under which households still find themselves.

The house market

An interesting phenomenon over the past few months has been the recovery in the growth of nominal house prices.

After reaching its lowest point in the first half of 2009, yearly growth accelerated to almost 14% in April, up from 12% in March 2010. Given that house prices were contracting on a year-on-year basis 12 months ago, the strong growth can at first glance be attributed to base effects. But, easing credit standards have seemingly also buoyed the recovery. Understandably, given the general need for potential home-buyers to gear their purchases, easing credit standards by banks will help the recovery in house-price growth. However, once the base effects have played themselves out, one can again expect house prices to show moderate growth rates, especially considering that household coffers remain under pressure and that in *real* terms, house prices are still very high relative to previous periods.■