State of the property market

State of the property market in quarter 2 of 2010

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

- Reprieve for office rentals in the form of steady vacancy rates
- Industrial rentals continue to slide
- Growth in house prices losing its oomph

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 2010:2) with that collected a year earlier.

Table 1
The property market at a glance at quarter 2010:2*
% growth on four quarters earlier (on smoothed data)

	Nominal	Real**
Prime CBD office rentals		
Johannesburg	-3,0	1,3
Pretoria	3,8	8,6
Durban	5,6	10,5
Cape Town	-8,7	-4,5
Prime decentralized office rentals		
Sandton CBD	3,6	8,6
Randburg Ferndale	12,9	18,2
Brooklyn / Waterkloof (Pta)	2,2	7,2
Hatfield	12,9	18,4
Berea (Durban)	4,8	9,7
La Lucia Ridge	4,3	9,3
Claremont (CT)	-3,8	0,7
Tyger Valley	-8,2	-3,7

* 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 2010:2* % growth on four quarters earlier (on smoothed data)		
	Nominal	Real**
Prime industrial rentals (500 m² units)		
Central Witwatersrand	-5,2	-0,8
Port Elizabeth	-4,7	-0,1
Durban metro	-5,7	-1,3
Cape Peninsula	-4,0	0,5
Flat rentals (standard quality, all sizes)		
Johannesburg metro	0,2	-4,7
Pretoria metro	-0,3	-5,2
Durban metro	2,8	-2,3
Cape Town metro	2,3	-2,7
Port Elizabeth	-3,2	-7,9

* 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 second quarter of 2010, capitalization rates on industrial and office property showed some marginal weakness when compared to their previous-quarter levels.

There are two opposing forces at work here. Real market rentals have been performing poorly over the past few quarters, thus potentially exerting upward pressure on capitalization rates. On the other hand, inflation prospects remain benign, thus putting downward pressure on long-bond yields, which are regarded as a substitute asset class to property. Whatever the eventual outcome of this contest, we do not expect capitalization rates to move decisively either way.

Office rentals

The upward march of vacancy rates of office buildings is seemingly losing momentum, thus holding out hope for office-block landlords that market rentals will stabilise quite soon. In fact, in the second quarter, market rentals in Johannesburg decentralized, as a whole, were up by 3% when compared to the same period a year earlier. In Pretoria decentralized rental growth of 2% was achieved, while growth was the strongest in Durban decentralized, where rentals were up by almost 10%. In contrast, oversupplied Cape Town decentralized still registered a rental decline (of 5%).

Industrial market

In the second quarter of 2010, market rental rates for prime industrial property continued to contract. On the Central Witwatersrand (-5%), in Durban (-6%), in the Cape Peninsula (-4%) and in Port Elizabeth (-7%) market rentals were all lower than a year ago.

Despite the fact that building-cost inflation (-5%) is also expected to have contracted, the poor nominal rental performance still meant contracting *real* rentals in all of these industrial conurbations, barring the Cape Peninsula. Here, *real* rentals managed to stay at roughly the same level they were a year ago.

Flat rentals

Residential rentals are continuing to show unimpressive growth, and had it not been for the relief brought to debt-service payments by falling interest rates, many more buy-to-let investors would have struggled.

In fact, in the second quarter of 2010, flat rentals in Durban and Cape Town could only muster meagre yearly growth of 3% and 2% respectively. In Pretoria and Johannesburg, flat rentals flat-lined.

The house market

Some of the wind has been taken out of the sails of house prices.

After having accelerated to 13% off a low base in April 2010, the growth in nominal prices has since then cooled to 3% in September 2010. This high growth rate was never going to be sustainable in light of the affordability constraint.

This constraint includes the exceedingly high level of house prices, the shedding of jobs, the high indebtedness of consumers and fast rising electricity tariffs. In addition, taxpayers seem to be facing income-tax hikes next year, not to mention the ongoing escalation of assessment rates in many municipalities.■