State of the property market

State of the property market in quarter 1 of 2011

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

- Office rentals starting the year off with a bang
- Rental recovery bodes well for capitalization rates
- Flat rentals outperforming house and townhouse rentals

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 2011:1) with that collected a year earlier.

Table 1
The property market at a glance at quarter 2011:1*
% growth on four quarters earlier (on smoothed data)

	Nominal	Real**
A-grade CBD office rents		
Johannesburg	-16,5	-15,1
Pretoria	9,8	11,4
Durban	6,4	8,0
Cape Town	-3,2	-1,7
A-grade decentralized office rents		
Sandton CBD	26,2	28,1
Randburg Ferndale	10,9	12,5
Brooklyn/Waterkloof (Pta)	6,3	7,9
Hatfield	5,7	7,3
Berea (Durban)	-6,4	-4,9
La Lucia Ridge	-0,2	1,3
Claremont (CT)	0,1	1,7
Tyger Valley	-9,0	-7,6

* Unless otherwise specified
** Nominal values deflated by BER Building Cost Index; however, flat rentals are deflated using the Consumer Price Index.

Table 1 (continued) The property market at a glance at quarter 2011:1* % growth on four quarters earlier (on smoothed data)		
	Nominal	Real**
Prime industrial rentals (500 m² units)		
Central Witwatersrand	0,2	1,8
Port Elizabeth	6,5	8,1
Durban metro	0,8	2,3
Cape Peninsula	4,4	6,0
Flat rentals (standard quality, all sizes)		
Johannesburg metro	2,3	-0,2
Pretoria metro	5,8	0,7
Durban metro	2,7	-0,1
Cape Town metro	3,8	0,2
Port Elizabeth	2,6	-0,1
Bloemfontein	3,5	0,1

* Unless otherwise specified

** Nominal values deflated by BER Building Cost Index; however, flat rentals are deflated using the Consumer Price Index.

Capitalization rates

At the moment, the biggest factor set to benefit capitalization rates would be the current revival in market rentals. This is so because market-rental growth brings with it better prospects for capital returns. However, vacancy rates are still stubbornly refusing to drop. This might persuade property investors not to be too hasty to buy property at lower expected income returns (capitalization rates).

Nonetheless, capitalization rates for prime office, industrial and retail property managed to strengthen — albeit very slightly — in the first quarter of 2011.

Office rentals

Office rentals started the year off with a bang, with rentals on a national basis up by an impressive 9% in the first quarter of 2011.

But, given that vacancy rates are still stubbornly refusing to drop and that growth might be distorted by base effects, a moderation in growth remains a possibility. Nonetheless, strong growth in rentals was also recorded at the regional level, with rentals in Johannesburg and Pretoria decentralized up by as much as 15% and 12% respectively. In Cape Town decentralized less impressive growth of 4% was achieved while in Durban decentralized (-2%) market rentals were actually lower than they were a year ago. These variances can be ascribed to variations in vacancy levels and trends.

Industrial market

Industrial property is showing signs of a recovery, with vacancy rates seemingly levelling off and rentals once again showing growth.

In the first quarter of 2011, the growth in market rentals (on a national basis) accelerated to nearly 4%. This comes after a sharp cooling in growth and even, in recent quarters, a contraction in rentals. A closer look at the major industrial conurbations reveals that in the reporting quarter the motor city of Port Elizabeth (+6%) was able to show the strongest growth. The Cape Peninsula followed with growth of 4%, while in Durban rentals were up by 1%. On the Central Witwatersrand, market rentals managed to stay at roughly the same level they were a year ago.

Flat rentals

Despite showing mediocre growth — below consumer inflation — flat rentals are at least outperforming house and townhouse rentals.

On a national basis, in the first quarter of 2011 flat rentals were up by a yearly rate of about 2%. Rentals for houses could only muster growth of roughly 1%, while, in contrast, rentals for townhouses were down (-1%) when compared to a year ago.

Given consumer inflation (excluding housing) of 3% over the same period, these dismal figures imply contracting real rentals across all three residential property types. Considering the heavy weight (16,4%) of residential rentals in the calculation of headline CPI (the sum of actual rentals and owners' equivalent rent), residential market-rental growth is quite important. However, the very low growth at present has an almost negligible effect on the overall metric of consumer prices.

The house market

House prices remain stuck in a rut as evidenced by the continued poor performance of indices of house prices.

In May 2011, the Absa national house-price index showed no growth with prices remaining roughly at the same level they were a year ago. A turnaround in fortunes can, of course, only be expected once the magnitude of key drivers of demand changes significantly. One such driver is, of course, interest rates. But, for now, no help can be expected from falling interest rates; this as the Reserve Bank has to consider the possible second-round effects of rising food and fuel prices on overall consumer prices.■