State of the property market

State of the property market in quarter 2 of 2012

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

- Capitalization rates going nowhere slowly
- Firming yields driving listed property prices higher
- Office rentals struggling

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 2012:2) with that collected a year earlier.

Table 1
The property market at a glance at quarter 2012:2*
% growth on four quarters earlier (on smoothed data)

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

* 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 2012:2* % growth on four quarters earlier (on smoothed data)		
	Nominal	Real**
Prime industrial rentals (500 m² units)		
Central Witwatersrand	3,1	1,0
Port Elizabeth	0,0	-1,9
Durban metro	3,4	1,4
Cape Peninsula	-1,8	-3,7
Flat rentals (standard quality, all sizes)		
Johannesburg metro	6,7	0,9
Pretoria metro	0,0	-5,4
Durban metro	4,6	-1,1
Cape Town metro	1,3	-4,2

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

Capitalization rates

Currently, industrial and office vacancy rates are refusing to drop while nominal rentals are finding it hard to outperform inflation. This does not bode well for capital return prospects, which might potentially adversely affect capitalization rates.

Yet, in the second quarter of 2012 the market's ratings of non-residential property remained steady; this as capitalization rates stayed at roughly their previous-quarter levels.

Office rentals

In recent quarters, moderate economic activity and floundering business confidence, and their debilitating effect on office demand and vacancies, have not been auguring well for office rentals.

In fact, in the second quarter of 2012, only Pretoria (+1%) and Durban (+1%) decentralized could muster some growth in nominal rentals. In both Johannesburg (-2%) and Cape Town (-1%) decentralized nominal rentals were on average slightly lower than they were a year ago. Considering that building costs are expected to have grown by a modest 2%, this implies that in none of these metros were rentals able to grow in *real* terms.

Industrial market

Industrial rentals continue to show moderate growth as South African manufacturing dwindles under international economic pressures.

In June 2012, manufacturing production was lower than expected, with growth of only 0,8% year-on-year. What's more, the Kagiso Purchasing Managers' Index (PMI) — an indicator of the overall health of the manufacturing sector — also deteriorated somewhat in August to an index level of 50. This reading implies that the manufacturing sector is essentially stalling as a reading above 50 indicates expansion and a reading below 50 indicates contraction. This poor performance is mainly driven by weak economic conditions in the Eurozone, one of SA's main trading partners.

Nonetheless, in the second quarter of 2012, nominal industrial rentals on the Central Witwatersrand and in Durban were up by a modest 3%. In Port Elizabeth they stayed at roughly the same level as a year ago, while in the Cape Peninsula (-2%) they were marginally lower. In the reporting quarter, East Rand rentals recorded the highest growth rate of just below 7%.

Flat rentals

Residential rentals in the second quarter of 2012 reflected the same trends visible in other property sectors; that is, moderate to weak growth in rentals.

Nationally, nominal market rentals on flats and houses grew by 5% and 3% respectively, whereas those on townhouses showed no growth. Given consumer inflation of about 5,7% over the same period, this implies that in *real* terms all categories of residential property rentals are contracting, thereby mirroring what is happening in the non-residential property sector.

The house market

For now, some life support for the ailing house market comes in the form of a seeming return to life of the mortgage market and a few other factors.

After contracting for more than a year, the value of new mortgage loans granted for residential dwellings and flats did show growth of about 7% in June 2012. The seeming recovery might be explained by low and steady interest rates, but also by the continued decent but unsustainable growth in disposable incomes. Despite cooling somewhat, the disposable incomes of households still managed to show fairly impressive growth of 9% in the second quarter of 2012. This comes after growing by 12% in the previous quarter.

Nevertheless, depending on which house-price index you look at, yearly growth in national nominal house prices for August 2012 ranged from no growth (according to Absa) to growth of just below 7% (according to FNB).■