State of the property market in quarter 2 of 2016

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

- Johannesburg decentralized office rentals are resilient
- Manufacturing recovers, but still not out of the woods
- Smaller houses showing the strongest growth in prices
- Flat rentals struggle owing to declining affordability

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 2016:2) with that collected a year earlier.

Table 1
The property market at a glance at quarter 2016:2*
% growth on four quarters earlier (on smoothed data)

	Nominal	Real**
A-grade decentralized office rentals		
Sandton CBD	9,7	6,1
Randburg Ferndale	3,8	0,3
Brooklyn/Waterkloof (Pta)	1,2	-2,1
Hatfield	9,1	5,5
Berea (Durban)	5,2	1,8
La Lucia Ridge	1,8	-1,5
Tyger Valley	7,6	4,0
Claremont	5,1	1,6
Century City	5,4	1,9
Prime industrial rentals (500-m² units)		
Central Witwatersrand	2,4	-0,9
East Rand	7,1	3,6
Durban metro	3,8	0,0
Cape Peninsula	5,1	1,6
Flat rentals (standard quality, all sizes)		
Johannesburg metro	4,0	-2,1
Pretoria metro	5,0	-1,2
Durban metro	9,2	2,8
Cape Town metro	6,2	0,0

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

Office rentals

Continued decent growth in output by the services sector of the economy has resulted in employment in the sector also showing marginal growth. However, whether this will lead to a sustained improvement in the demand for office space ─ in the midst of continued uncertain economic prospects and weak business sentiment levels ─ remains unlikely.

In the second quarter of 2016, nominal market office rentals in nodes such as Parktown (+24%), Illovo (+17%), Rosebank (+14%), Rivonia (+14%) and Sandton (+10%) all showed impressive growth, beating building-cost-inflation of 4%).

Pretoria decentralized rental performance was much less impressive than that of Johannesburg decentralized, with top nodes such as Menlyn (+3%), Centurion (+1%) and Brooklyn/ Waterkloof (+1%) all showing modest growth in nominal market rentals.

Similar to Pretoria decentralized, market rentals in Durban's decentralized office nodes also showed moderate growth. In the reporting quarter, nominal market rentals in Berea (+5%) managed to record growth in slight excess of building-costs. This was not the case in La Lucia Ridge and Westway, where rentals were up by only 2%.
The Cape Town decentralized office node of Claremont showed the strongest growth of 8%. This was followed by Tyger Valley and Century City, where rentals were up by 5%. Nonetheless, nominal rentals in all three of these nodes were at least able to show growth ─ albeit marginally ─ in excess of the expected growth in building costs.

Industrial market

A ray of hope for the industrial property market was the recovery in output produced by the manufacturing sector during the second quarter of 2016. Hopes of a sustained recovery were, however, quickly dampened by the August 2016 fall in the Barclays Purchasing Managers Index (PMI) and by continued feeble global economic conditions.

In the second quarter of 2016 the strongest performance came from industrial rentals on the East Rand, which were up by a yearly rate of 7%. This was followed by the Cape Peninsula, where rentals grew by 5%. When one compares the expected growth in building costs (as measured by the BER BCI) of 4%, the implication is that in these two regions industrials rentals were able to grow in real terms. This was, however, not the case on the Central Witwatersrand and in Durban, where nominal industrial rentals showed weaker growth of 2% and 3% respectively.

The house market

Growth in the prices of smaller houses is accelerating at the fastest pace. This according the latest FNB house price indices.

The yearly growth in prices of *small houses* (sized between 20 m² and 80 m²) has accelerated since the beginning of 2015 to such an extent that in the second quarter of 2016 nominal prices were up by an impressive 13%. This is compared to *medium* (sized: 80 m²-230 m²) and *large* (sized: 230 m²-800 m²) houses, which over the same period showed growth of 7% and 5% respectively. As for the latest year-on-year growth in nominal house prices, according to Absa and FNB, prices were on a national basis up by between 4% and 6% in August 2016.

In the medium term, we expect weak economic activity and the rising interest-rate environment to keep effective demand for houses, and hence the growth in nominal prices, at bay. (Effective demand is demand which is realisable because the latent buyer can actually afford the property.)

Flat rentals

Nationally, flat rentals are cooling and were in the second quarter of 2016 growing by a yearly rate of just under 5%.

A look at the country's major cities shows that nominal flat rentals in Johannesburg (+9%) again showed the strongest growth, albeit from a low base. This was followed by Pretoria where rentals were up by 6%. Durban and Cape Town could muster growth of only 5% and 4% respectively (although it must be said that both are from a high base). In the second quarter of 2016, consumer prices (excluding owners' equivalent rent) grew by 6%, implying that in Johannesburg alone flat rentals were able to grow in *real* terms.

As for the future, muted economic growth prospects will most likely continue to weigh down on rental growth.■