Chapter 1: State of the property market

State of the property market in quarter 1 of 2024

The front page of this issue features the industrial property market, which continues to defy the odds with its low vacancies and strong rental growth.

In Cape Town, nominal rentals of industrial space are booming, with the first-quarter 2024 figure up about 20% compared to 2019 (that is before the pandemic). One of Rode's survey respondents said there is a severe shortage of industrial buildings and there have been rental wars because of multiple tenants looking to lease the same space. Another broker said a tenant was secured after only one day of advertising, without the tenant even viewing the property. However, is not only Cape Town that is shining. The other major industrial areas in South Africa, like Durban, are also showing robust growth. We report on this in **Chapters 7** and **8**.

In this issue, you will also read that the office market continues to recover. As far as the housing market is concerned, house prices remain under pressure, while flat rentals are looking relatively better.

Unfortunately, the spectacular rally in the share prices of listed properties pulled back in March and April as expectations of interest rate cuts have been dialled back. Another factor that has held back some buyers is uncertainty over the outcome of the SA elections and the numerous problems faced by SA Inc (see **Chapter 4**). That said, the world is also not as safe as before, given lower-than-usual economic growth and heightened geopolitical risks.

In such an uncertain environment, property companies are selling assets and holding back distributable income. The coming quarters will no doubt be a rough ride, considering the uncertainties about the local elections and the direction of interest rates.

A summary of the main findings by property type follows.

Quantitative overview of the property market

Tables 1.1 and **1.2** provide a snapshot of how the property market has performed over the past four quarters by comparing the latest information (quarter 2024:1) with data collected a year earlier.

Office market

As mentioned above, the recovery of the office market in South Africa continued in the first quarter of 2024, as evidenced by slowly growing nominal rentals and lower vacancy rates.

Rode found that the average national vacancy rate of grades A^{+}, A and B space combined in *decentralized*[1] nodes was 13,9% in the first quarter of 2024, one percentage point better than the 14,9% average in the first quarter of 2023. This is based on the opinion of brokers active in nodes across the country. Looking at the bigger picture, the current national vacancy rate is still well above the pre-Covid level of 10,5% in 2019 and the historical long-term average of 9,3%, as per SAPOA data.

[1] Decentralized means all nodes in a metro lumped together, excluding the (old) central business district (CBD).

The Gauteng cities of Johannesburg and Pretoria are where vacancy rates are higher than the South African average. The coastal cities of Cape Town and Durban have performed comparatively better.

In the first quarter of 2024, weighted gross market rentals for *decentralized* grade-A space increased nationally by a measly 1% in *nominal* terms compared to the first quarter of 2023. All in all, rentals have improved from the big Covid declines, but are still about 2% below 2019 levels (that is before the pandemic). The market has been boosted by the return of some workers to offices since 2022, albeit in many instances in a hybrid way.

Cape Town has been the clear standout of the four major cities since 2022. Here nominal decentralized grade-A gross rentals in the first quarter of 2024 rose by 6,5% compared with four quarters earlier. Rentals were about 10% higher than pre-Covid levels. That said, this was not enough to outpace the appalling building-construction inflation (BER BCI) of around 13%.

Nominal rental growth in decentralized Durban grew at the second-fastest pace in the first quarter of 2024 (+3,5%), while in Johannesburg nominal growth (+0,6%) managed to at least stay in positive territory.

This implies that rentals declined sharply in *real* terms in all the major cities, which makes most new developments unviable. Indeed, office building activity in the 12 months to February 2024 declined by 43% compared to the 12 months to February 2023.

Table 1.1
Office and industrial rentals: Performance as at quarter 2024:1
% change from four quarters earlier (on smoothed data)

	Nominal	Real*
A-grade decentralized office rentals		
Sandton CBD	-1,2	-12,6
Rosebank	-4,2	-15,3
Bryanston	-2,0	-13,3
Centurion	-3,3	-14,5
Hatfield	2,5	-9,3
Menlyn	5,6	-6,6
La Lucia/Umhlanga Ridge	3,4	-8,6
Berea	-4,1	-15,2
Tyger Valley	2,4	-9,6
Century City	6,9	-5,5
South Africa	**1,0**	**-10,7**
Prime industrial rentals (500 m² units)		
Central Witwatersrand	5,8	-6,5
East Rand	5,2	-6,9
Durban	6,7	-5,7
Cape Town	5,2	-6,9
South Africa	**4,8**	**-7,3**

*Nominal values deflated by BER Building Cost Index.

Industrial market

Nominal gross market rentals in South Africa for industrial space of 500 m^2 grew by 4,8% in the first quarter of 2024 compared to the first quarter of 2023. This is up from the pace of roughly 4% recorded over 2023. Rentals in the first quarter were up about 15% compared to the pre-pandemic levels of 2019. However, in *real* terms, rentals are still declining due to elevated building-cost inflation.

Regionally, all the major conurbations shone with strong nominal rental growth (5% to 7%) and low vacancies. Logistics properties continue to have ultra-low vacancy rates.

In the Central Witwatersrand, nominal rental growth averaged 6% amid very low vacancies. One of Rode's panellists noted that since the last quarter of 2023 there has been a distinct sense that the industrial market is strengthening generally. It is no longer only logistics warehouses where landlords have leverage. Durban's rental growth was also strong at 7%.

However, stand values did not perform as well as rentals.

Retail market

National retail sales, which include malls and street-front shops, increased by 3,4% year on year. This was slower than the 5,6% growth achieved in 2023. In *real* terms, national sales fell by 1,4%. This indicates that the market has generally been under pressure, which makes sense given the financial situation of consumers.

However, readers will note that in **Chapter 4** we report on the retail operating results of the listed property sector for 2023. These showed the malls performed relatively well. Indeed, rental reversion rates turned positive in some cases, while mall vacancy rates fell to 4,5% in the fourth quarter of 2023, based on MSCI/SAPOA data. Nevertheless, mall vacancy rates remain above pre-pandemic levels. Nominal trading densities also grew strongly, but did moderate from 2022 levels. *Unfortunately, no mall statistics are available for 2024 yet*.

We discuss the retail sector in detail in our sister publication *Rode's Retail Report*.

Table 1.2
House prices and flat rentals: Performance as at quarter 2024:1
% change from four quarters earlier

	Nominal	Real*
House prices		
South Africa#	0,8	-4,6
Flat rentals		
South Africa	3,6	-1,8

* Nominal values deflated by the Consumer Price Index (CPI).
\# Please note that this data is for January and February as March was not available at the time of writing.

Residential market

Nominal **house** price growth in South Africa is still slow amid a weak economy and elevated interest rates. Indeed, expectations of interest rate cuts have been dialled back. Another factor that has held back some buyers is uncertainty over the outcome of the SA elections.

Nominal house prices grew by 0,8% over January and February 2024 compared to the same period in 2023, based on FNB data. This implies that prices in *real* terms have continued to fall significantly as the average consumer inflation (CPI) rate was 5,4%. Regionally, houses sold the quickest in the Western Cape in the first quarter of 2024.

Turning to our forecast, we still expect SA nominal house prices in 2024 to grow at a slower rate than 2023's average of 1,5% amid a weak economy and elevated interest rates. Rode has warned numerous times before that interest rate forecasts can change quickly, which has indeed happened. At the time of our last *Rode Report* in December, the market was optimistic that interest rates in the US and in South Africa would decline several times in 2024. So far, no cuts in the US and locally have occurred due to sticky inflation, with many forecasts being pushed back to late in the year. When interest rates eventually do decline, the market would get some support, but do not expect fireworks. It is all about affordability.

Turning to **flats**, vacancy rates on a national level edged down to 7,9% in the first quarter of 2024 from 8,1% in the fourth quarter of 2023, according to Rode's residential survey data. Vacancy rates are still up from the average 2023 level of 7,2%.

Regionally, the Western Cape continues to stand out with its low flat vacancy rate of 2,3% in the first quarter of 2024, well below the national average. In contrast, vacancy rates in Gauteng and KwaZulu-Natal were much higher. On a positive note, flats were less empty in Johannesburg than at the end of 2023, while the trend was the opposite in Pretoria.

Official data from Stats SA shows that in the first quarter of 2024 nominal flat rentals in South Africa increased on average by 3,6% compared to a year earlier. But overall, house prices and rentals are still declining in *real* terms in most parts of the country. ■