State of the property market in quarter 1 of 2015

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

- Office rentals feeling the pinch
- Industrial property's support pillars remain fragile
- Growth in house prices slowly losing its momentum

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 2015:1) with that collected a year earlier.

Table 1
The property market at a glance at quarter 2015:1*
% growth on four quarters earlier (on smoothed data)

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

Table 1 (continued) The property market at a glance at quarter 2015:1* % growth on four quarters earlier (on smoothed data)		
	Nominal	**Real****
Prime industrial rentals (500-m² units)		
National	4,1	-2,9
Central Witwatersrand	2,8	-4,1
East Rand	3,7	-3,2
Durban metro	5,2	-1,8
Cape Peninsula	6,0	-1,1
Flat rentals (standard quality, all sizes)		
National	5,2	1,1
Johannesburg metro	2,2	-1,9
Durban metro	7,2	2,9
Cape Town metro	6,6	2,4
Bloemfontein metro	5,4	1,2

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

Office rentals

For now, the growth prospects for market rentals of office buildings remain modest. This as an underperforming services sector is likely to continue to place a lid on the demand for office space.

In the first quarter of 2015, market rentals for grade-A office space — on a national basis — mustered growth of roughly 4%. The general trajectory of the national office vacancy rate has been north since 2012, which explains the moderate growth in market rentals. Of course, the main reason for the uptick in national office vacancy rates was waning demand for office space on the back of lacklustre economic growth, and — on the supply side — bold development activity in nodes like Sandton, Cape Town CBD, Century City and Umhlanga Ridge

Nonetheless, at the regional level, the strongest yearly growth in market rentals was recorded in Cape Town decentralized (+7%). It was followed by Pretoria and Johannesburg decentralized, where rentals were on average up by 5% and 4% respectively. In the reporting quarter, rentals in Durban decentralized (+1%) showed the weakest growth.

Industrial market

Until there is a significant turnaround in the performances of the manufacturing and retail sectors, strong growth in industrial market rentals cannot be expected.

In the first quarter of 2015, market rentals for prime industrial property in the Cape Peninsula showed the best yearly growth of 6%. This was followed by Durban and the East Rand, where rentals were up by 5% and 4% respectively. On the Central Witwatersrand, rentals could only muster growth of roughly 3%. Over the same period, building costs are expected to have shown growth of about 7%. This implies that in all of these major industrial conurbations, market rentals are still unable to show *real* growth.

The yearly growth in manufacturing output and retail sales volumes has, in general, waned since 2010. Households that are overwhelmed by debt, high unemployment, modest household credit growth and sharply slumping consumer confidence do, for now, still presage meek growth in retail sales volumes. As for the manufacturing sector, despite weak domestic conditions, the single largest hindrance to production remains the unreliable supply of electricity.

The house market

The yearly growth in national house prices is gradually losing its momentum, which should not come as a surprise as key drivers of house prices are still struggling.

After heating up to a yearly growth rate of 10% in the second quarter of 2014, the growth in national house prices has since cooled to 6% in June 2015. Interesting is how sharp the deceleration in the monthly (annualized) growth has been. This implies that the cooling in yearly growth rates will continue. For now, many factors remain that are likely to further dampen the growth in house prices. Consider here:

- Weak economic activity and its likely damper on growth in employment and disposable income. Also, the public sector's employee-appointment and salary-boosting sprees will come to end as the fiscus is under severe pressure. If not, we could find ourselves in a Greece-like situation overnight.

- Still-high household debt-to-disposable income levels. The ratio of debt-to-disposable income of households has decreased since 2009 but the ratio remains uncomfortably high at 78%.

- The disproportionate increases in administered prices, which negatively affect affordability.

- Consumer confidence levels that are fast sliding, which will affect the willingness of households to make substantial financial commitments, such as buying a house.

The only positive factor for house prices is the continuing low level of new supply being added to the stock of houses. This means that when the negative factors disappear one day, the upward house price correction will be enormous. But this, we reckon, is many years away.

Flat rentals

The growth in flat rentals is slowly accelerating and is now at more or less the consumer-inflation rate. However, given households that remain financially stretched, a strong and sustained recovery in flat rentals cannot, for now, be expected.

In the first quarter of 2015, national market flat rentals again gained a bit of momentum as they grew at a yearly rate of roughly 5%. Of course, considering consumer inflation was roughly 4% over the same period, this implies that flat rentals have shown some *real* growth. Zooming in on the performances at the regional level, we can see respectable — inflation beating — growth of 7% in Cape Town, Durban and Port Elizabeth. Elsewhere, in Johannesburg, Pretoria and Bloemfontein, growth in flat rentals ranged between 2% and 5%.■