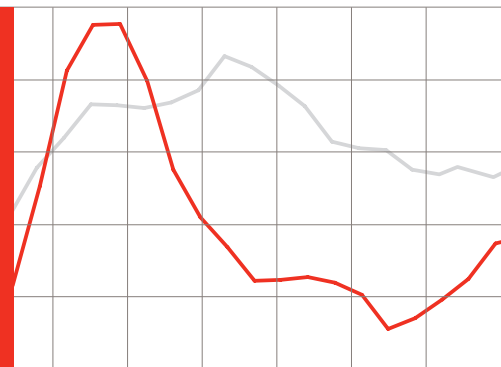


# PAYPROP RENTAL INDEX

A comprehensive view of the state of the residential rental market in South Africa



## SLOW GROWTH IN A SLOW ECONOMY

While the slow growth trend in the rental industry continues, property still remains a good long term investment

As South Africa's economic recovery continues its struggles to get under way properly, growth in residential rentals remains modest – hampered on the whole by affordability in key provinces.

For many years an evergreen investment, property ownership has lost some of its sheen – in some cases even returning negative growth in past months. In this climate, landlords are passing on higher costs to tenants and taking a broader, long-term view of return on their investment.

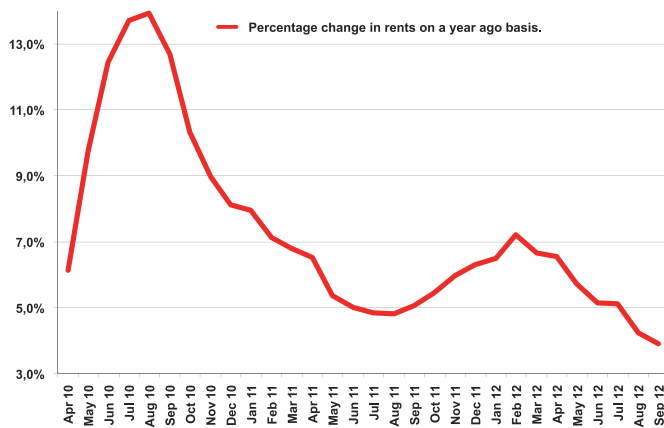


Figure 1: Increases in South African rents  
Source: PayProp and Economists.co.za

### Lowest Rental Growth Since Start of PRI

The September 2012 PayProp Rental Index (an industry research tool provided by PayProp – South Africa's largest

processor of rental transactions) shows that South African rentals increased at their lowest rate since the index came into being two years ago.

Average rentals grew to R5 221 over the three months to September – only 3.9% more than the average measured for the same period in 2011.

### Climate of Slim Pickings

Rentals peaked in June 2012 at R5 232 per month, showing that average rentals actually declined by R11 over the last four months.

This is nothing new, unfortunately – rental growth has been in the single digits for 23 months now, year-on-year, with the Soccer World Cup the last big boom for the residential letting market.

In addition, the 3.9% increase from a year ago is much lower than the 5.5% consumer price index increase in September, evidence that rental increases are not shielding investors fully from inflation risks.

With the pace of economic recovery still very slow, landlords are finding it difficult to match pre-recession increases. Tenants whose financial position has deteriorated due to increases in the cost of living simply cannot afford more.



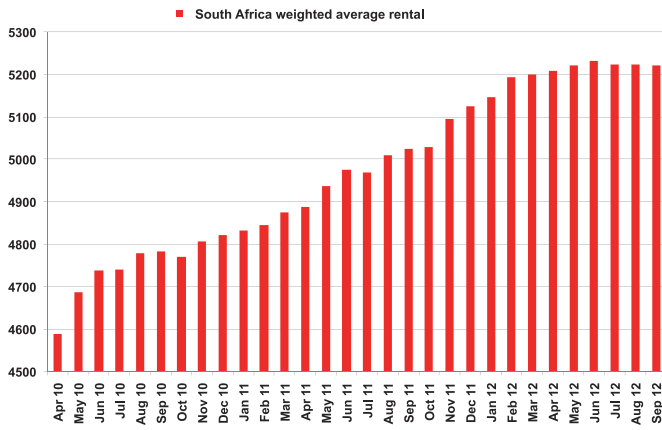


Figure 2 South African regionally-weighted average rental  
Source: PayProp and Economists.co.za

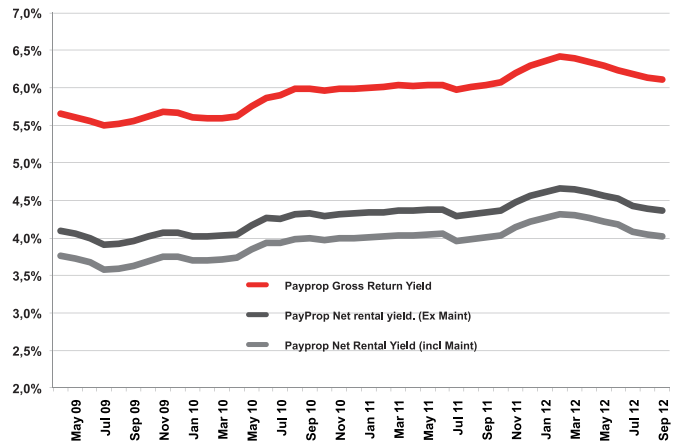


Figure 3 Rental Yields  
Source: PayProp and Economists.co.za

## More of the Same

As the PayProp data is smoothed over the last four months, the data does not yet fully reflect the depressed rent environment. With strikes hitting the North West, Gauteng and parts of the Free State, rents will likely remain under pressure in following months.

On the other hand, higher wage increases are creating hope that rental increases may recover to some degree in the new year.

## Gross rental yields – better than money in the bank

Using ABSA-determined medium-sized house prices, PayProp has developed a Gross Rental Yield Index (annualised rental income before costs, relative to average property value). This index records gross rental yields of 6.1% for the month of September – up from 6.0% a year ago, but slightly lower than the beginning of the year, when returns were closer to 6.4%.

The current gross rental yield is fairly constant, not having changed by more than 0.1% in the last four months. The figure has also remained fairly constant over a longer period – ranging between 5.5% and 6.4% over the last three and a half years. At present, it is better than bank account yields, where investors can expect to get only about 5%.

## But Net Yields a Low 4%

Gross rental returns are, however, not the best way to measure property returns. Quite often property assessment rates, sewerage and refuse collection are left for the landlord to pay. In addition, home maintenance and agent income must be subtracted.

PayProp estimates total deductions on an average property to be R1 488 per month, bringing monthly rental income down from R5 221 to R3 733. Net rental (excluding maintenance) would leave a yield of 4.4%.

However, even this is an unreliable indicator of rental returns for landlords, as not doing maintenance would lower capital returns on the property. With variable maintenance cost, the actual figure is in reality even lower.

As can be seen in the graph above (see Fig. 3), rental yields have remained relatively flat for more than three years now, despite increases in the price of a medium sized house and steep hikes in assessment rates and other municipal services. This suggests that landlords are succeeding by passing on price increases to tenants, meting it out over the long term.

## Still a Good Investment?

Despite this strategy, net rental yields have remained far below bank interest rates and risk-free government bonds. In stages over the last four years, net rental yields



have been half the risk-free government bond rate (6.5% for September 2012 on a 10-year bond).

But before landlords reconsider their investment, it should be pointed out that rents are only one part of the return that landlords get over time. Adding capital value increase to the net rental (including maintenance), total returns were 6.7% in September 2012.

## Provincial Data

### Mpumalanga – you win again

On a provincial basis, Mpumalanga continues to lead the pack with the highest rents in the country. The average rental in that province is R6 202, followed by Limpopo with R6 113 per month. Both these provinces suffer from a lack of rental stock in smaller boom towns including Lepahalale, Tzaneen and Lydenburg.

### Depressed in the Northwest

The lowest rentals can be found in the Northwest, particularly in its more depressed older gold mining towns. The Free State comes in with the second-lowest rents. The Eastern Cape is now the third-cheapest province, sinking beneath the Northern Cape by virtue of weaker demand.

Province	Sep-12
Northwest	3981
Free State	4218
Eastern Cape	4286
Northern Cape	4933
Western Cape	5204
South Africa	5221
Kwazulu-Natal	5313
Gauteng	5430
Limpopo	6113
Mpumalanga	6202



Figure 4 Average rentals per province

Source: PayProp and Economists.co.za



## MPUMALANGA CONTINUES TO LEAD THE PACK WITH THE HIGHEST RENTS IN THE COUNTRY



### Dragged down by Gauteng

The biggest drag effect came from Gauteng. Our biggest province (in an economic sense) registered rental growth of only 1% – providing ample explanation for South Africa's modest rental increase over the last year. This may be the result of over-supply starting to have an effect on the ability of landlord to increase rentals.

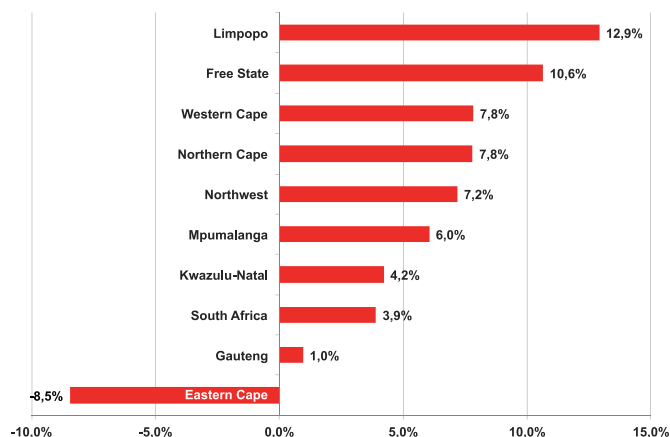


Figure 5 Provincial changes in rents over the past year

Source: PayProp and Economists.co.za

National increases vary greatly, with figures of over 10% for both the Free State and Limpopo. After many depressed months, it seems property rental in the Free State is finally seeing an increase on our new four-month moving average scale.



## Agent Commission Data

For the first time in its history, the 2012 PayProp Rental Index includes figures of agent commissions received versus rentals invoiced. The aim of this index – to better understand average rental portfolio incomes from an agent point of view, as well as how these may vary regionally – is shown in the table below (see Fig. 6):

Province	12 Month Average
Eastern Cape	8,3%
Free State	7,4%
Gauteng	10,1%
KZN	12,0%
Limpopo	8,9%
Mpumalanga	8,6%
Namibia	7,5%
North West	8,8%
Northern Cape	9,2%
Western Cape	10,7%
Grand Total	10,2%

Note the national average commission charged of 10.2%. The top-performing regions are KZN, the Western Cape and Gauteng. For the remainder, provinces with lower rentals generally seem to also have the lowest commissions, with the Free State and Eastern Cape being prime examples.

A further interesting view on commission data emerges when analysing the national average over time (see Fig. 7). When plotted over a 12-month period, the following trend is evident:

Interestingly, commission percentage numbers broadly correlate with the percentage of national rental increases over time. Of concern is the slight, yet steady downward trend in the percentage commission line, indicating that agent margins may be coming under pressure.



Figure 6 Percentage commission charged by province over the last year

Source: PayProp

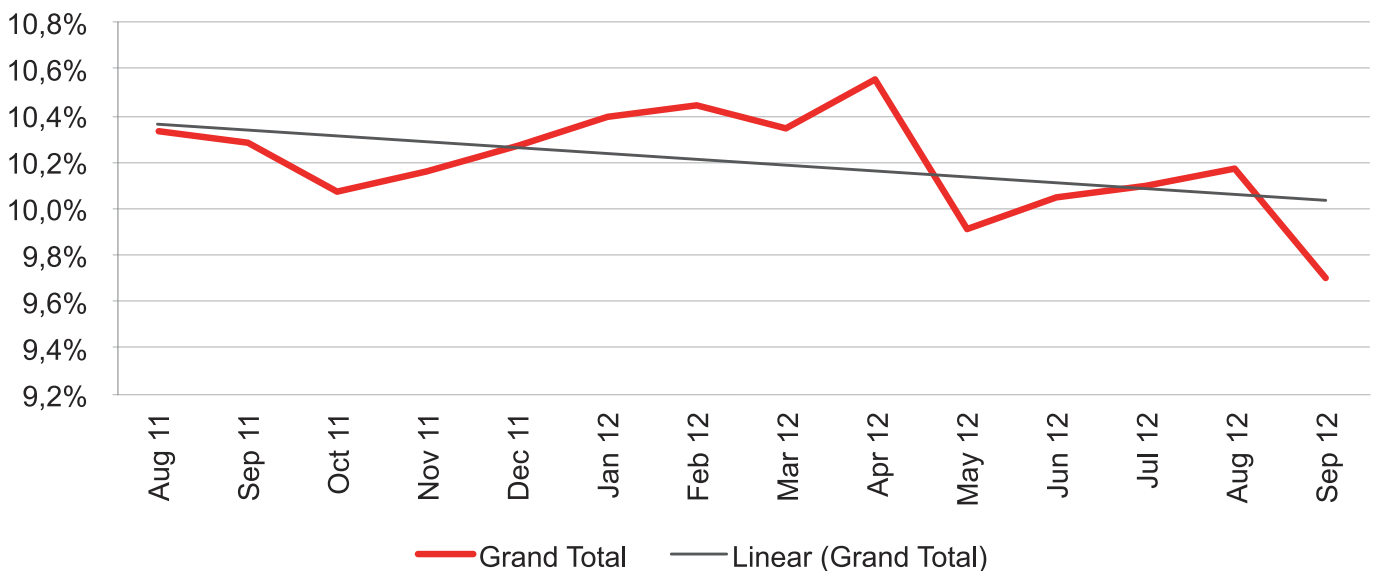


Figure 7 Percentage commission over time

Source: PayProp



Average % deposit held	Q3-2011	Q4-2011	Q1-2012	Q2-2012	Q3-2012
National	114,2%	114,7%	115,8%	118,6%	122,8%
Eastern Cape	107,8%	109,3%	105,0%	104,8%	127,4%
Free State	99,0%	101,7%	97,6%	96,2%	94,9%
Gauteng	89,2%	90,8%	92,4%	97,1%	99,8%
KZN	84,8%	91,4%	94,9%	99,7%	103,7%
Limpopo	121,6%	128,8%	121,5%	118,7%	113,5%
Mpumalanga	104,0%	103,4%	104,8%	99,8%	105,6%
Namibia	38,8%	80,3%	89,1%	98,9%	104,6%
North West	93,5%	95,0%	91,6%	92,7%	86,0%
Northern Cape	37,2%	53,9%	74,2%	97,7%	100,1%
Southern Cape	105,1%	120,5%	141,8%	158,8%	153,6%
Western Cape	140,5%	137,3%	140,2%	143,1%	147,5%

Figure 8 Damage deposits held as a percentage of rental invoiced  
Source: PayProp

## Damage Deposits

We are seeing a steady increase in the percentage of damage deposits required as a percentage of rental invoiced (see Fig. 8). Over the past four quarters, this percentage has grown from 114.2% to 122.8%, which may be interpreted as an adjustment in the amount of agent and owner security based on a perceived increase in tenant non-payment risk.

## Notes on the PayProp data

The PayProp data set has steadily grown from an initial 40 000 active leases 12 months ago to almost 52 000 active leases as of 30 September 2012. All the data is based on actual rentals collected for 51 770 leases by PayProp in September 2012 (see Fig. 9).

We used ABSA-determined house prices for medium-sized houses. ABSA data shows that medium-sized house prices increased by 2.6% in September 2012.

We further used Statistics South Africa indices for assessment rates as well as municipal rules-based data, and combined the two.

Our maintenance index was also compiled from Statistics South Africa data, and taken at two thirds the weight of assessment rates. We assumed that renters would pay for about half of maintenance, such as light bulbs, fuses and garden services.

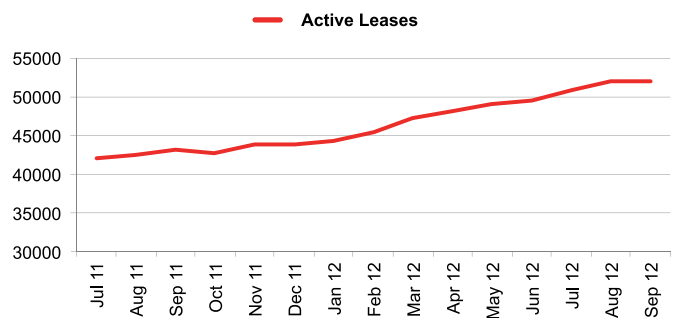


Figure 9 Number of active leases over time  
Source: PayProp

# PayProp Rental Index

The PayProp Rental Index is a quarterly guide on trends in the South African residential rental market, and is compiled in partnership with Mike Schüssler, one of South Africa's leading economists. This edition details market conditions for the third quarter of 2012 based on information collected from the PayProp database.

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The PayProp Rental Index is available from the PayProp web site at [www.payprop.com](http://www.payprop.com).

## Sign up for PayProp

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