SA property recovery fails to take off in 2011

SA's commercial real estate market maintained modest growth over 2011, producing a 10.4% total return, according to the South African Property Owners Association/Investment Property Databank (IPD) SA Property Index.

These subdued result mark a softening in the market from the mini-recovery in 2010 - which delivered a 13.4% return - however is still an improvement over 2009.

Uncertainty in global markets, weak local demand and slowing consumer confidence resulted in muted capital growth of just 1.4%, while income returns were steady at 8.9%. Results improved marginally in the latter half of 2011, however, after completely flat growth in the first six months of the year.

Despite this minor improvement towards the end of the year concerns remain, particularly over the health o secondary markets. Even at a national level, fundamentals are placing downward pressure on rentals and bottom line returns.

Vacancies rose from 6.6% to 6.9%, rental growth reduced to 6.2% and at the same time rental yields softened by 36 basis points to 9.6%.

A sharp convergence in growth across the main market sectors highlights the increasingly important impac of macro forces and high uncertainty on the property market. Quality and location are playing a greater role differentiating property returns.

Retail property once again proved its resilient nature with the strongest capital growth of the three main sectors for the third consecutive year. Its 10.1% total return was comprised of 8.3% income return and 1.6 capital growth, boosted by relatively strong retail sales as consumers continued to spend.

Overall, however, the growth in trading density fell below inflation and the outlook is for a continued moderation in consumer spending. An increase in vacancies to 6.0% also put pressure on rental values, resulting in a corresponding weakening of rental growth.

As a whole, the office sector managed just 1.3% capital growth over the year, which combined with a 9.7% income return produced an 11.2% total return. This figure, however, masks a wide range of results within t office sector, with quality and location generally underlying the ultimate differences. Better quality offices were able to drive higher rental growth from vacancies lower than the national average of 12.1%.

Industrial property managed the highest total return of the three sectors with 11.9%, although the income return of 10.4% is much more significant than the 1.4% capital growth. Industrial vacancies continued on their downward trend, and at the end of 2011 were the lowest of any sector at just 4.3%.

The South African results reflect a growing loss of momentum in global property markets in the wake of dampened sentiment particularly across Europe, where many markets saw a reduction in returns in 2011 compared to 2010. Outside of Europe, however, returns managed to improve slightly in Canada, Australia and USA.

Stan Garrun, managing director of IPD SA, said: "The results confirm the impact of global economic instability and subdued conditions locally, on SA real estate investment performance. On top of this, high operating costs and a serious mismatch between demand and supply, are taking their toll on returns. Whil these figures do not necessarily point to further recessionary conditions, they do indicate that it is a long h back to pre-2008 levels. The good news is that prime assets are performing well in all sectors. Any economic uplift should quickly release major new income growth for both tenants and landlords, as well as pent up property development pipeline."

Despite the moderation in direct property returns in 2011, it nevertheless outperformed most other major asset classes. Equity markets and bonds returned 2.6% and 10.1% respectively.