TPN Rental Monitor

Risk, reward and research

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In the last quarter of 2019, residential landlords listed the lack of quality tenants; a rise in property expenses and repairs and maintenance as their top 3 challenges at the time.

It was a double edged sword in quarter 4. The reality is that rental non-payment did not deteriorate significantly, but at the price of landlords having to elect higher vacancies over placing lower quality tenants. Further pain was caused by the escalating property costs which rose faster than rental escalations which dampened profits.

Research remains the key element to a successful property portfolio

Residential tenants in good standing softened slightly to 81.88%, ending the year fairly flat. Two out of three tenants paid their rent on time and in full. A further 15.65% of tenants paid in full albeit late. This left landlords to struggle with 11.14% of tenants who only made a partial payment and 6.98% of tenants who did not pay their rent at all.

National numbers

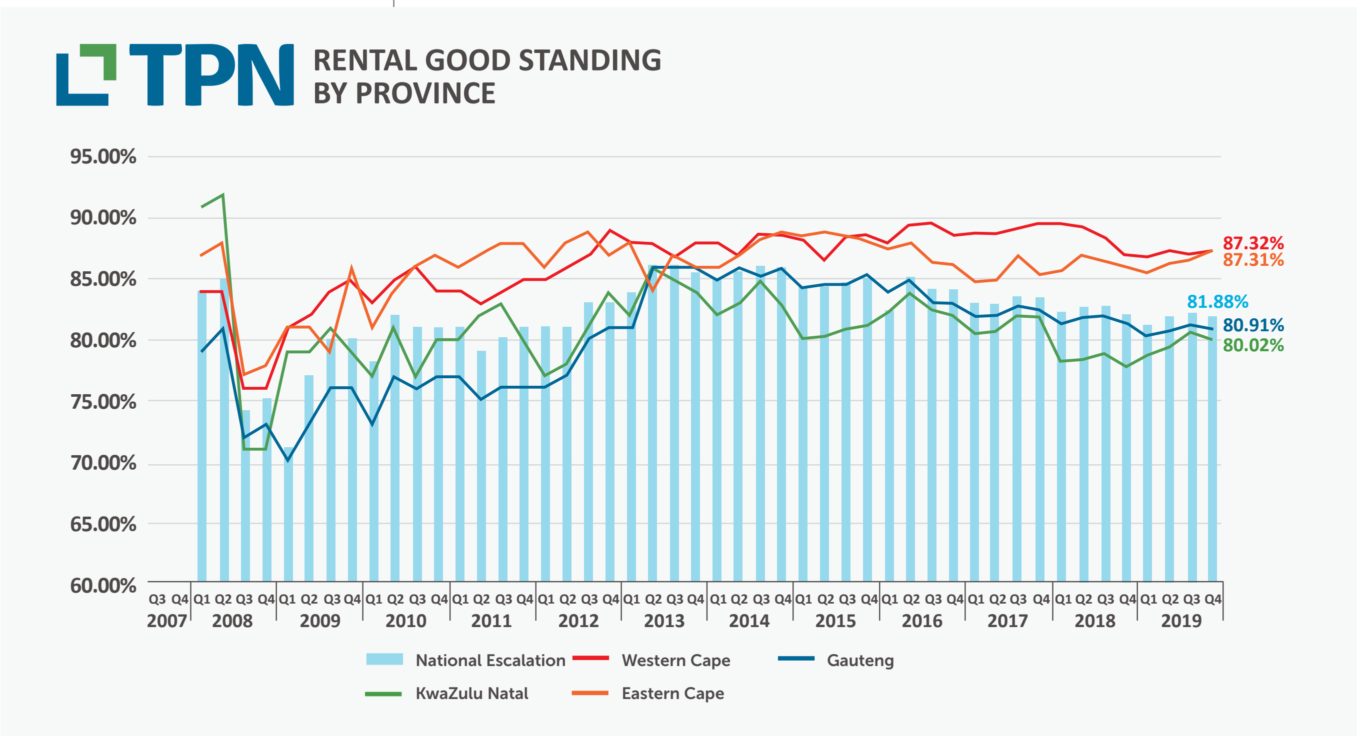
It remained a tenants' market in the last quarter of 2019. The TPN Market Strength Index points to an increasing supply of rental property stock coupled with weakening demand. This was further impacted with higher vacancy rates and lower escalations.

Vacancy rates declined marginally to 8.97%. Although this remained persistently high, at these levels landlords lost on average a month's rent every year.

Escalations continued to drop, to a weak 3%. It is not surprising that landlords have reported the second biggest challenge they faced last year was the rising cost of property expenses. Gross yield was 9.59%.

Provincial perspective

The Eastern Cape made a comeback, nearly three out of four tenants paid their rent on time and in full which indicates a landlord's market. Demand for rental property was high although the long term trend indicated a declining demand, estate agents and landlords reported a limited supply. Escalations of 5.6% were the highest in the country, with vacancy rates of 5.4%, the lowest in the country. Gross yield continued to improve to 9.57%.



Western Cape retains the best performing province spot in terms of rental payment performance but only by a whisker. 87.32% of tenants were in good standing in 2019 Q4. The demand for rentals improved, driving a slight improvement in the market strength. It is difficult to determine if the demand was due to the short term holiday letting season or if the previous low demand/high supply scenario has bottomed out. Vacancies also benefited recording slightly lower numbers at 7.6%, although escalations continued to drop to 3.2%. This is possibly due to landlords preferring lower vacancies rather than lower escalations.

Gauteng rentals are risky business but deliver on returns. With good standing at 80.91%, high vacancies at 9.5% and dismal escalations of 2.5%, all of which performed worse than the national averages. Gauteng landlords can at least be comforted to know that gross yields in the province remained in the top 3 at 10.18% - but remember gross yield is not net yield. The key focus will be how to limit vacancies and non-payment.

Provincial perspective

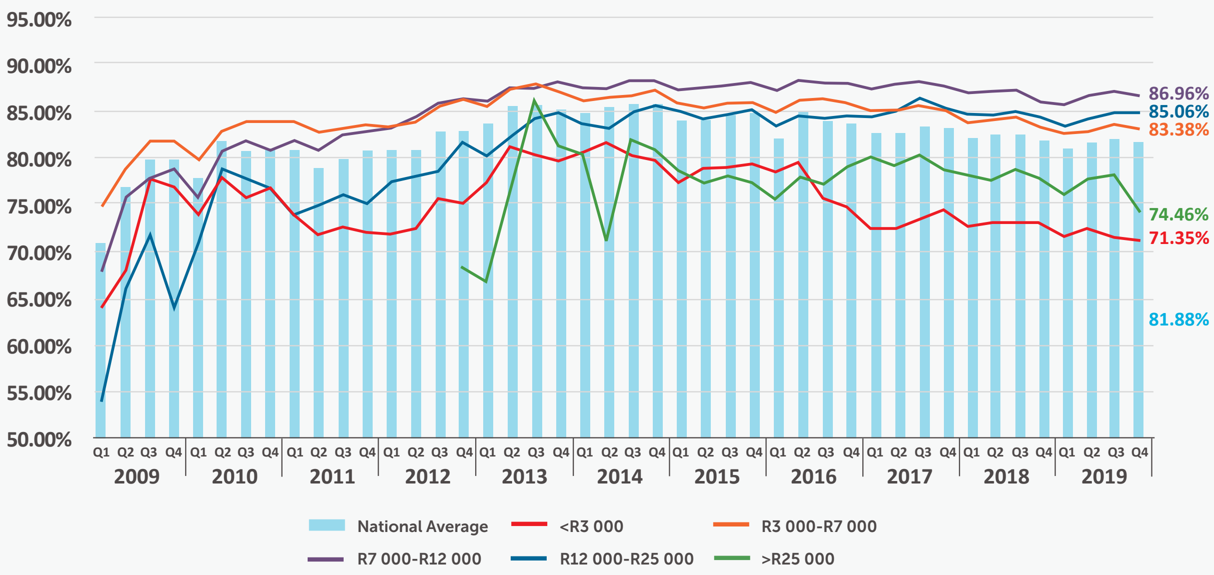
KwaZulu-Natal tenant rental behaviour stabilised in 2019, coming off of a difficult 2018 where rent paid on time reached a low point at 59.86% which was last experienced in the 2008/9 global economic recession. Currently, KZN tenants in good standing just managed to cling to above eighty percent at 80.02%. An acceptable vacancy rate of 5.9% was helped by a Market Strength of 51.3 (the demand rating of 58.7 is slightly higher than the supply rating of 56.1). No doubt, the below average gross yield of 9.3% within the context of difficult rental collections is not enticing to most investors.

TPN SUMMARY BY PROVINCE

Province	Good Standing	Vacancy Rate	Market Strength	Escalation
Eastern Cape	87.3%	5.4%	61.4%	5.6%
Gauteng	80.9%	9.5%	42.1%	2.5%
KwaZulu-Natal	80.0%	5.9%	51.3%	3.2%
Western Cape	87.3%	7.6%	43.1%	3.2%
Smaller 5	81.8%	11.2%	59.7%	4.0%
National Average	81.9%	9.0%	46.2%	3.0%

Rising cost of living

TPN RENTAL GOOD STANDING BY RENT VALUE



Rising cost of living

Tenants spend between 23 – 28% of their gross income on basic rent. Add utilities, sewerage, refuse removal and parking costs in and it becomes clear that one of the biggest financial commitments is a roof over their heads.

The biggest losers have been luxury properties with rentals above R25,000 per month. Tenants in good standing dropped by a significant 3.86% to 74.46%. The decline was caused mostly by a shift of late paying tenants into the partial payment bracket. It is noteworthy to report that this group of tenants record the highest rent to income ratio where 28% of their gross income is allocated to rent.

The R12,000 - R25,000 rental properties have had the benefit of 85.06% of tenants in good standing, the only category of tenants whose rental payment profile improved quarter-on-quarter. These tenants on average spend 25% of gross income on rent.

15.49% DID NOT PAY

The worst performing tenants remain the tenants in the below R3,000 rent per month category. With 71.35% of tenants in good standing, those in the did not pay profile bracket clocked in at 15.49%. Tenants in this rental range contributed the lowest gross income to rent at 23%.

Securing best performing rental payment profile were tenants in the R7,000 – R12,000 rental range. With 24% of gross income allocated to rent, these mid-income tenants have the benefit of middle income salaries and the wisdom of not over committing income to monthly rental.

TPN SUMMARY BY VALUE BAND

	Good Standing	Vacancy Rate	Market Strength	Escalation
Less than R3000	71.3%	8.0%	56.8%	2.2%
R3000 to R4500	81.4%	7.2%	53.0%	
R4500 to R7000	84.5%	6.6%	50.5%	
R3000 to R7000	83.4%	6.7%	50.8%	3.2%
R7000 to R12000	87.0%	7.0%	47.7%	3.0%
More than R12000	83.8%	15.4%	47.8%	3.6%
National Average	81.9%	9.0%	46.2%	3.0%

Conclusion

The trends in 2019 Q4 paint a clear picture in hindsight:

- **October:** Moody's keeps South Africa one notch above investment grade but changed the outlook from stable to negative.

- **November:** S&P who already rate South Africa in Junk status, adjusted their outlook to negative.

- **December:** Eskom plummets the country into Stage 6 load shedding.

- South Africa recorded a second quarter of negative growth, -1.4%.

The first quarter of each year already brings the traditional 'holiday hang-over rental collection challenge' - add to that a weakening economy and landlords are strongly urged to prepare for a difficult period ahead. The need to save wherever possible has never been more urgent!