

PayProp Rental Index  
**Annual Market Report 2013**

The only comprehensive view of the state of  
the residential rental market

2013 EDITION

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## The year that was...

For the first time ever PayProp is combining our eagerly anticipated quarterly market reports into a combined review of the residential letting market for the preceding calendar year.

 **60 000**  
ACTIVE RENTALS IN PAYPROP

 **700**  
ESTATE AGENCIES USE PAYPROP

 **2.5 million**  
TRANSACTIONS AUTOMATED  
PER YEAR

 **3 000**  
USERS ON THE SYSTEM

 **17%**  
AVG CLIENT PORTFOLIO  
GROWTH PER YEAR

 **10**  
YEARS IN BUSINESS

## Origins of the PayProp Rental Index

The PayProp Rental Index was created in response to client requests for our insights into the letting part of the property market. Historically the industry could draw on a lot of detailed sales data, but had very little reliable information on average rentals, growth rates, damage deposit ratios and agent commissions.

At the time, as the largest processor of residential letting transactions in South Africa, PayProp helped our clients manage more than 35 000 properties with our state-of-the-art trust account environment. Our view was that this provided a statistically significant enough sample to draw conclusions from, and thus the idea of the PayProp Rental Index was conceived.

We were further extremely fortunate in securing one of South Africa's leading economists, Mike Schüssler, to assist us with conceptualising, designing and building the Index, which was launched in December 2011 at South Africa's first ever State of the Rental Industry conference.

Since then the PayProp Rental Index has grown from strength to strength. Currently, we draw our information in the form of actual transaction data from a sample base of 60 000 active rental properties, bringing South African real estate professionals the most complete, up-to-date and accurate analysis of the rental market. And we will continue to do this free of charge, because we feel that an industry with sound information is one that can make better decisions.

South Africa has 1.7 million rental properties. Around a quarter of those are managed by letting agents, whom we estimate to number more than 6 000 out of a total of about 10 000 estate agencies.

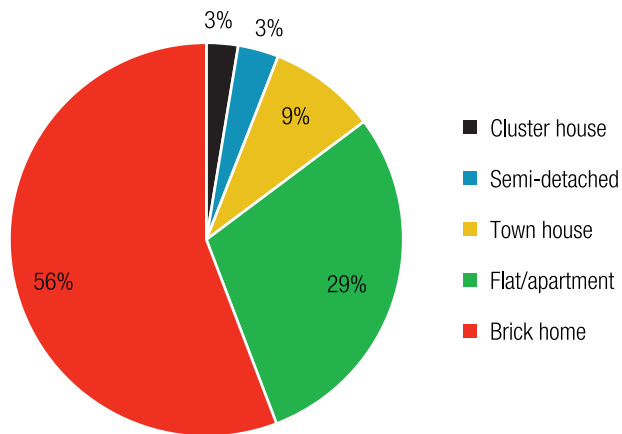
# Just how big is the rental market?

Big as it got, we couldn't help wondering how much ground we were actually covering.

## 1.7 million rentals

There are varying views on the critical question of the size of the rental market, depending on which method of calculation is used. According to Statistics South Africa's General Household Survey (revised in October 2013), there are just over 1.7 million homes in the 'formal' residential letting market. This is substantially bigger than we had previously thought.

Broken down by property type the distribution looks as follows:



Rentals by dwelling type  
Source: Statistics South Africa

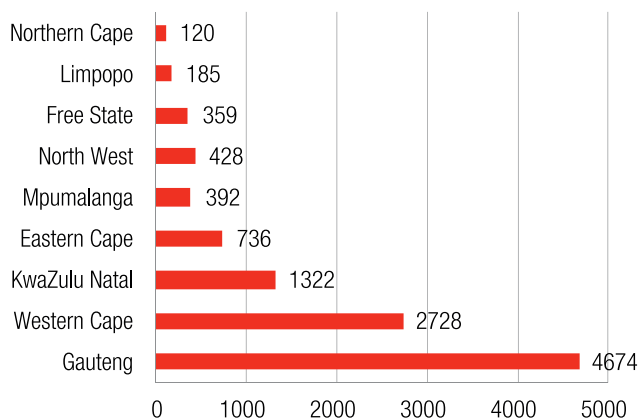
## 11 000 agencies

The next important question is, how many of these are managed by agents versus independent landlords?

To answer this question, PayProp embarked on a massive research project in the last two months of 2013. We phoned every estate agency whose details we could find and asked the simple question – “Do you manage a rental portfolio?” In total, we reached just under 5 000 estate agents, of which 63% answered in the affirmative.

## ...two thirds of whom do rentals

We further know that the Estate Agency Affairs Board (EAAB) issued 10 944 firms with fidelity fund certificates in 2013, which means that there may be around 6 000 managing agents in South Africa.



Firm FFC's issued by province in 2013  
Source: EAAB

## ...managing 25% of rentals

Just how many properties do South Africa's 6 000-plus rental agents manage? To get to a sensible answer, a little more statistical wizardry is required. Using the PayProp average portfolio size as a basis and adjusting for varying portfolio sizes in the rest of the market, we estimate that the 6 000 or so letting agents manage a total of 380 000 residential rentals. That represents just less than 25% of the total rental market – leaving over a million rental units in the hands of private landlords.

Let us sum that up. South Africa has 1.7 million rental properties – that is, 'formal homes' occupied by tenants as opposed to their owners. Around a quarter of those are managed by letting agents, whom we estimate to number around 6 000 or more out of a total of about 10 000 estate agencies. That leaves close to 1.3 million rentals in the hands of private landlords.

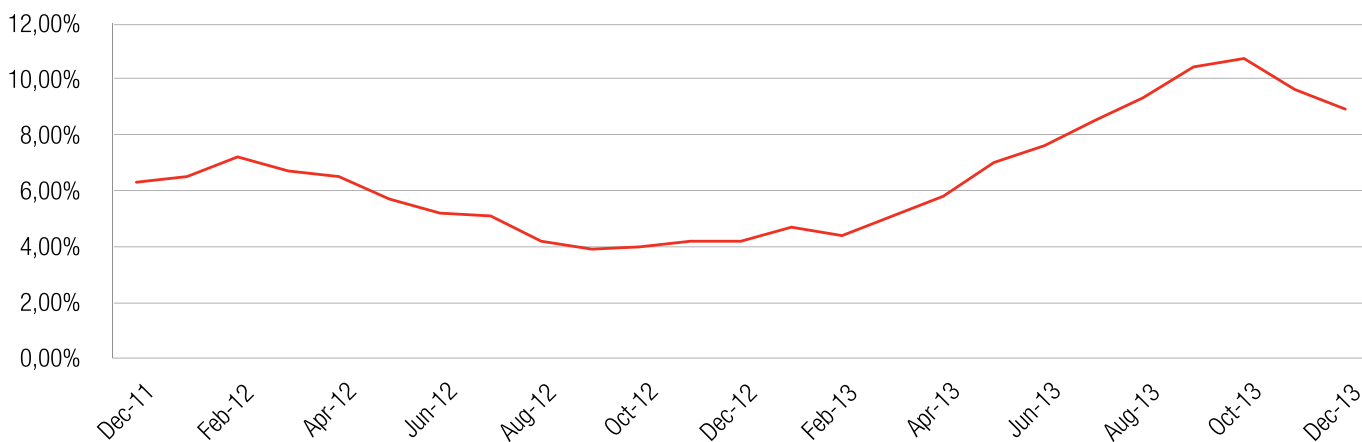
With this bit of eye-opening context to frame our thinking, let us turn our attention to the current state of the rental market, as at the end of 2013.

## A pretty good year

If we have to pin a single word on the market throughout 2013 it would have to be 'recovering'. After a flat-to-negative 2012, our first-quarter report noted the first 'green shoots' of recovery – year-on-year rental increases of 5% and higher.

The tone of our second quarter report was even more upbeat – the recovery had not only maintained its momentum, but for the first time in more than 18 months, year-on-year increases beat inflation at 7%!

The third quarter report did not disappoint either, as the growth continued, breaking through the psychological 10% barrier. To keep our feet on the ground, fourth-quarter results show a slightly lower annual increase of around 9% – but note that this number held constant for each month of the quarter. This points to a probable stabilisation. Our expectation is that rental increases for 2014 will remain above 8%.



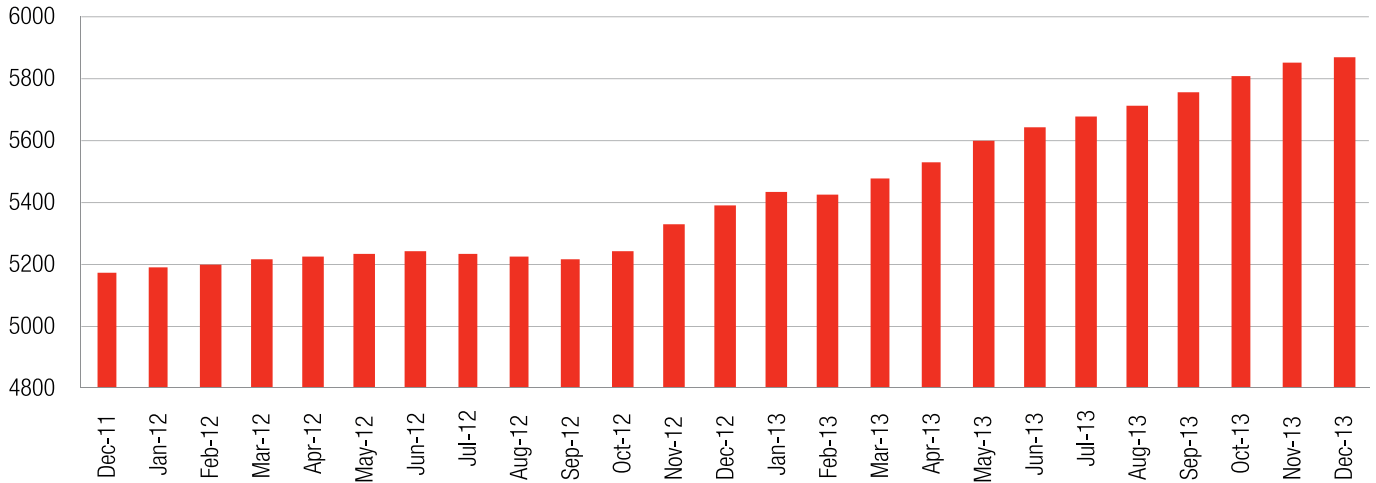
Year-on-year percentage change in rentals  
Source: PayProp

# So what's the average rental today?

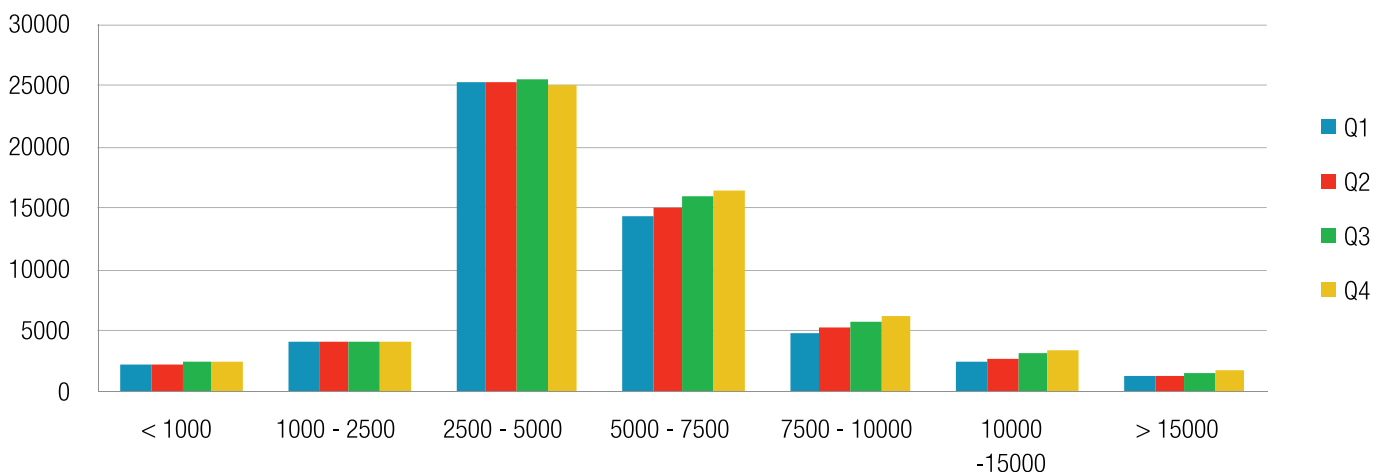
In current circumstances, anyone will take an 8% increase. But 8% of what?

The positive growth data has resulted in average rentals climbing slowly throughout the year, from R5 473 in Q1 to the current R5 867 in Q4. At the projected growth rates we expect to see the weighted national average rental exceeding the R6 000 per month level for the first time since we started tracking rental data in October 2010.

A key element of the growth in rental values is the shift in the number of rental contracts per price band. As the weighted national average moves closer to R6 000, we see a drop in rentals priced R2 500 to R5 000. Interestingly, we see increases in the R5 000 to R7 500 and R10 000 to R15 000 price bands that exceed the drop-off in the lower categories. This means tenants with lower-value leases are not just 'graduating' to more expensive leases, but new tenants coming into the market are starting at higher rental values.



Weighted national average rental  
Source: PayProp



Number of rentals by price category  
Source: PayProp

# The provincial race

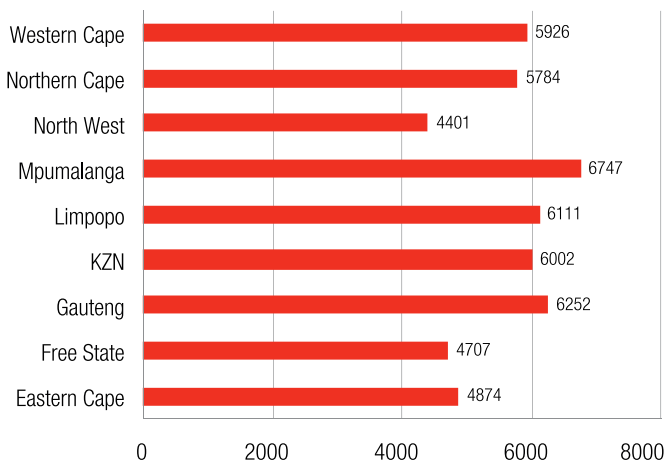
When we launched the PayProp Rental Index, the expectation was that the economic engine rooms of Gauteng and the Western Cape would lead the pack in average rentals. Against all expectations, Mpumalanga took the lead as the most expensive province to rent in. Upon delving deeper into this, we were reacquainted with an age-old first principle of economics, namely supply and demand.

We didn't expect demand in this outlier province to be so manifest, but what we saw in towns like Lephalale, Limpopo was exactly that. When industrial development meets limited rental stock, rentals values shoot up dramatically. This has been a recurrent theme in the cases of Limpopo, and later in the year, the Northern Cape.

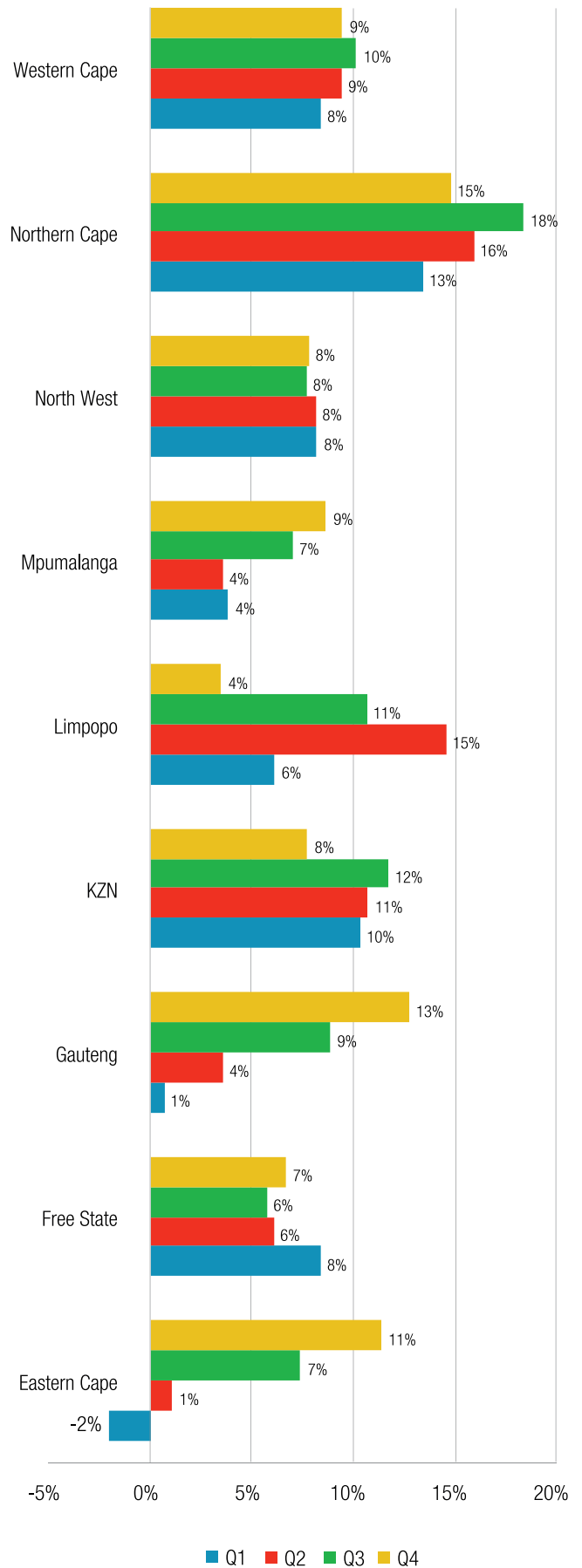
It is interesting to see that while Mpumalanga is currently still in the lead on an annualised basis, it was briefly overtaken by Limpopo for the duration of Q2, a feat repeated by Gauteng in Q4.

When casting our minds ahead it is useful to look at growth in provincial rentals. The Northern Cape is the clear leader in sheer velocity of growth, a fact corroborated by the ABSA House Price Index for 2013. Based on that, we expect average rental values in that province to exceed those in the Western Cape and KZN within the next two quarters.

Another trend to take note of is the decline in quarterly growth rates in Limpopo. A more in-depth study is needed to understand why, but one possible explanation is the impact of continuing strikes in the mining industry on industrial activity, and, accordingly, on demand for rental accommodation.



Provincial average rentals  
Source: PayProp



Provincial growth rates  
Source: PayProp

# Getting down to towns

Analysing town data typically yields more erratic results than provincial equivalents, because sample sizes are smaller and more likely to fluctuate as a result of prevailing dynamics. For example, a student town like Stellenbosch shows dramatic rental increases in October and November each year, as new student leases are negotiated for the following year. A subsequent but unrelated dip often follows at the end of the first term, as students drop out and landlords are forced to drop their prices.

A consistent top performer is the Limpopo town of Lephalale, which has held its position of demanding the country's highest rentals for two years. It is another remarkable example of rapid industrial expansion in an area with low rental supply, causing dramatic shifts in the market. Below Lephalale we see the usual suspects – traditionally affluent neighbourhoods such as Hout Bay, Bryanston etc.

Top Towns	Q1	Q2	Q3	Q4
Lephalale	R 15 688	R 15 465	R 16 003	R 19 052
Bryanston	R 13 426	R 24 925	R 22 752	R 16 655
Musina	R 8 902	R 13 356	R 16 523	R 16 052
Sea Point	R 17 554	R 12 246	R 14 645	R 16 332
Umhlanga Rocks	R 11 425	R 12 542	R 13 451	R 14 436
Hout Bay	R 10 253	R 12 149	R 12 127	R 11 771
White River	R 7 793	R 8 100	R 8 637	R 10 641
Green Point	R 11 886	R 11 889	R 13 311	R 10 145
Claremont	R 9 496	R 8 733	R 9 080	R 9 567
Nahoon	R 8 150	R 8 945	R 9 259	R 9 252
Randpark Ridge	R 8 649	R 8 569	R 8 980	R 9 755
Gardens	R 7 347	R 7 123	R 7 900	R 10 504



## Top town analysis

Source: PayProp



# What's the damage?

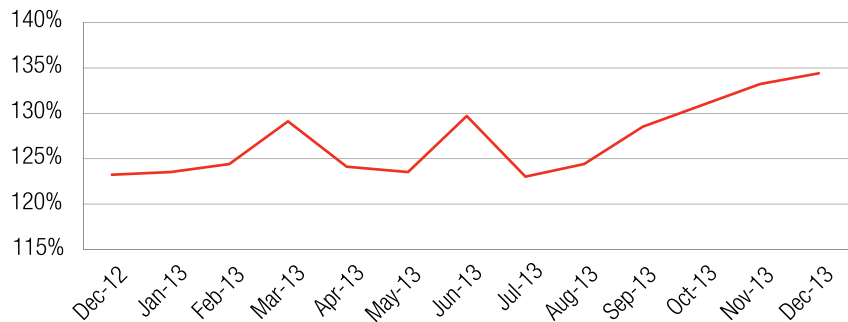
Another function of supply and demand is the quantum of damage deposits which a landlord can extract from tenants, relative to the value of rentals. The natural inclination for landlords is to hedge as much as possible against tenant damage, while that of the tenant is to commit as little money as possible, to free up cash. Thus the damage deposit ratio is the level at which these two points meet.

The theory emerging from our research is that the deposit-to-rental ratio can be higher in areas where there is more demand than supply.

There has been marked growth in this ratio at national level – from 123% in January to 134% in December. In other words, landlords are able to extract higher deposit levels than before. In keeping with our theory, this points to a situation where demand for rental properties outstrips supply nationally. This corresponds with our clients' experience in the market.

Provincial data provides other interesting insights. As the table shows, agents in the Western Cape currently get more than 1.5 times the average rental value as deposit, followed closely by the Eastern Cape (which has seen a recent uptick in growth), and, as one might expect, Limpopo.

The concern for tenants with 'high' damage deposits is the high level of upfront costs required to obtain occupation of a property. Using the national average rental value of R5 867 and the example of the Western Cape, a tenant would need to have R9 387 available for an upfront deposit in addition to the first month's rental of R5 867 – a total amount of R15 254.20.



National damage deposit ratio

Source: PayProp

This scenario shows why deposit guarantee products<sup>1</sup> have become so popular over the last year. In essence, they offer landlords the security of an underwritten policy in the case of damage to the property, while giving tenants the alternative of a much cheaper premium.

Damage Deposit Percentages	Q1	Q2	Q3	Q4
Eastern Cape	124%	125%	124%	131%
Free State	103%	105%	105%	104%
Gauteng	103%	104%	104%	110%
KZN	113%	109%	110%	113%
Limpopo	121%	126%	127%	129%
Mpumalanga	104%	105%	108%	108%
North West	98%	102%	104%	118%
Northern Cape	100%	96%	87%	93%
Western Cape	150%	150%	148%	160%



Damage Deposit Percentages

Source: PayProp

<sup>1</sup> The PayProp DepositGuarantee provides landlords with cover equal to 2.5 times the monthly rental, while initially costing the tenant a premium of 1/3rd of the rental value. Should there be no damage to the property and therefore no claim, the tenant receives 40% of premium contributions back in the form of a cash bonus.

Colin Habberton, the CEO of PayProp Capital, says "the progressive upward trend in damage deposit ratios leaves room for the DepositGuarantee to radically reduce the upfront costs to tenants, while offering enhanced asset protection to landlords and managing agents."

# How many rental contracts fall through because the tenant can't afford a damage deposit 1½ times the monthly rental – or more?



PayProp DepositGuarantee offers innovative insurance for landlords at rates that tenants can afford. It is an alternative to the costly and sometimes inadequate damage deposit arrangement. Underwritten by RMB Structured Insurance, your protection is as assured as cash in the bank.

To find out how PayProp DepositGuarantee can give you protection you can trust, call 087 820 7260 to speak to one of our specialists.

PayProp Capital (Pty) Ltd is an authorised financial services provider – FSP 43441

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TRUSTED PROTECTION

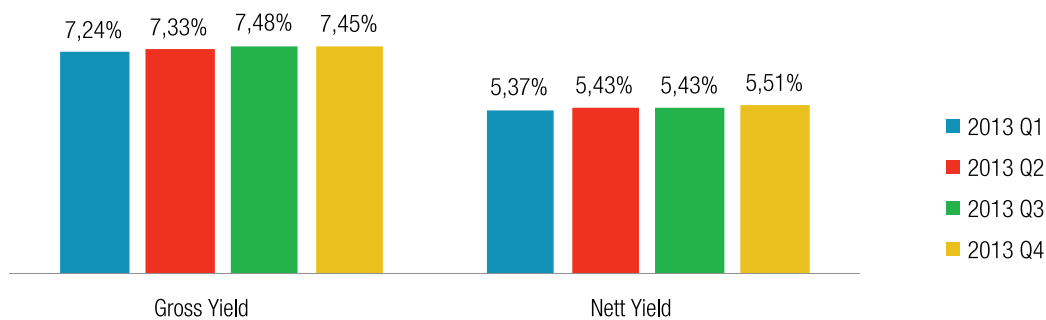
# Yields picking up for investors

Over the past few years we have spent a lot of time refining our yield calculation – a hugely important number for investors. We eventually settled on a comparison of values invoiced to tenants with actual values paid into owner accounts. Using actual income along with the ABSA House Price Index, we have been able to arrive at highly accurate gross (before landlord costs) and net (after landlord costs) yields, on a national as well as provincial level.

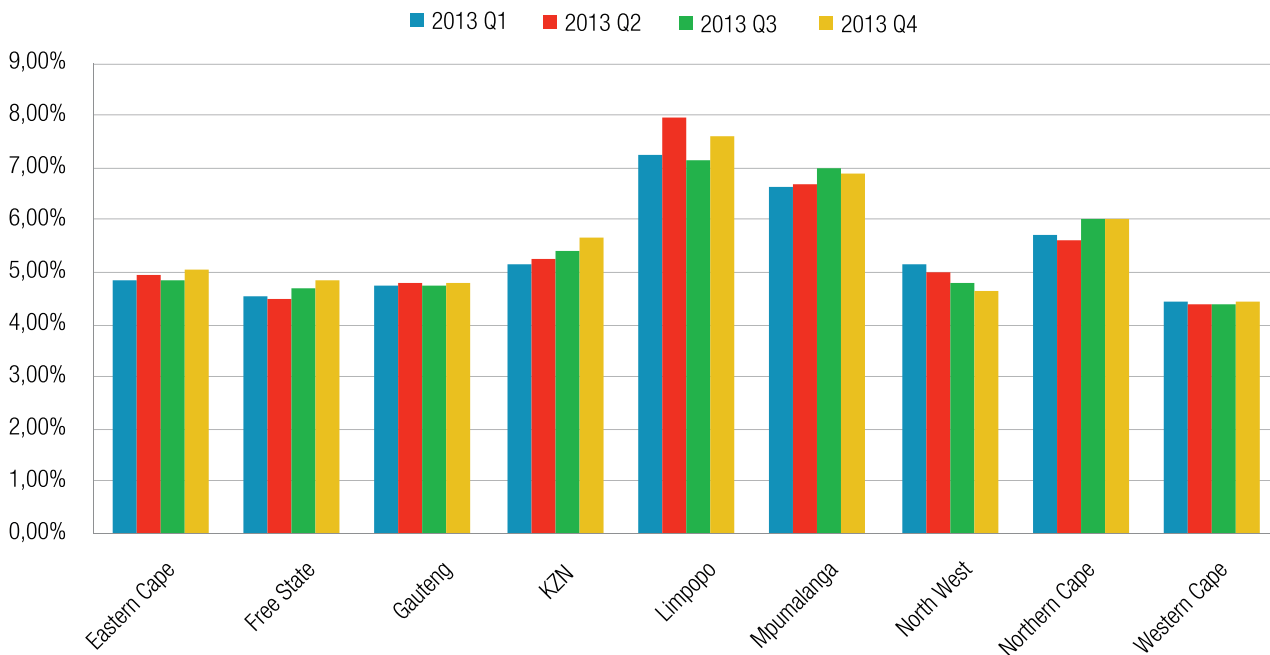
The graph below records slow improvements in national gross and net yields. Gross yields grew by 2.95% between January and December – a number not in line with average rental increases (almost 5% over the same period). This merits further explanation. The yield number tells us what type of return an owner would get if they bought a house right now, not necessarily what yield owners are getting who bought before.

An owner who bought last year is likely to achieve a higher yield because his asset was most likely acquired at a lower cost than the sum paid by someone getting into the market now.

Gross yield is one thing, but after deducting landlord costs such as agent commissions, rates and taxes and repairs from the rental amount, owners are earning just 5.51% in net yield. This return has grown by 2.6% since January 2013, slightly slower than the gross number. The reason for this is that landlords' expenses have grown faster than their ability to demand rental increases. Provincially the picture differs as dramatically as with other indicators. As expected, given the high rentals in these areas, we see much higher percentage yields for landlords in areas like Limpopo, the Northern Cape and Mpumalanga than in the rest of the country.



**National gross and net yields**  
Source: PayProp



**Provincial net yields**  
Source: PayProp

## How many are enough?

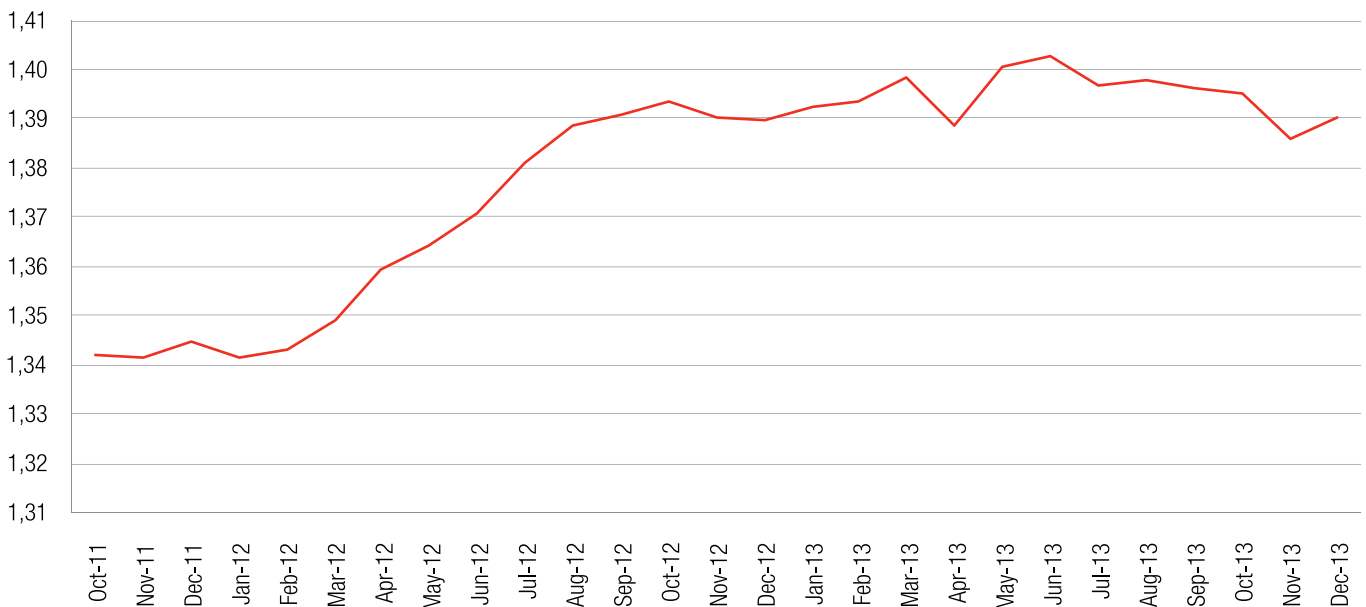
The improving yield numbers may further explain why there is a gradual upwards trend in the number of properties owned per investor.

Although the growth has been gradual, the average owner on PayProp now owns just under 1.4 properties compared to when we started the rental index, when the number was just above 1.3. This may point to first-time investors becoming more confident in the ability of secondary property to generate returns and acting on it.

## Tenant total cost

Many lease agreements place the obligation for monthly levies and municipal accounts on the tenant. Gauteng, in particular, is an extremely expensive area for tenants to stay in.

On average, over and above their R6 252 average rental, tenants also pay R852 in municipal costs as well as R954 in levies, bringing the total average monthly bill to R8 058 per month. In contrast, the Free State is the cheapest province to live in, at a total cost of occupation of only R5 496 per month.



Average properties per owner  
Source: PayProp

# Still using a highlighter and bank statements to puzzle out which tenants have paid and which ones' cheques are 'in the mail'?

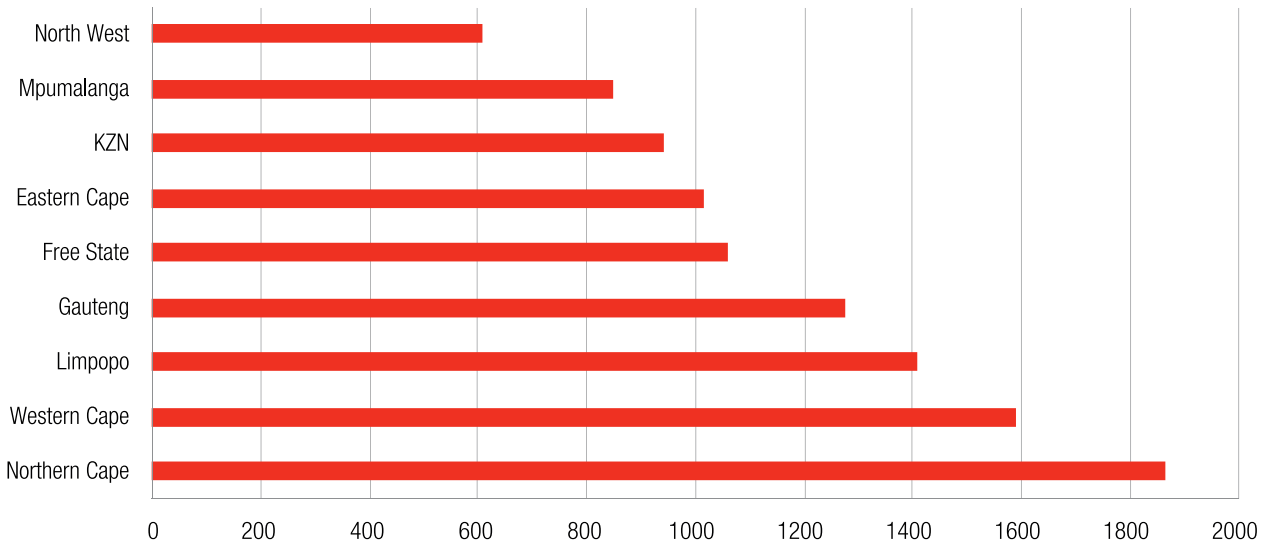


PayProp provides its clients with a state-of-the-art audited trust account platform that smoothly integrates banking, accounting and property management.

To find out how PayProp can help you run a safer and more efficient rental portfolio, visit [www.payprop.co.za](http://www.payprop.co.za) or call 087 820 7368.

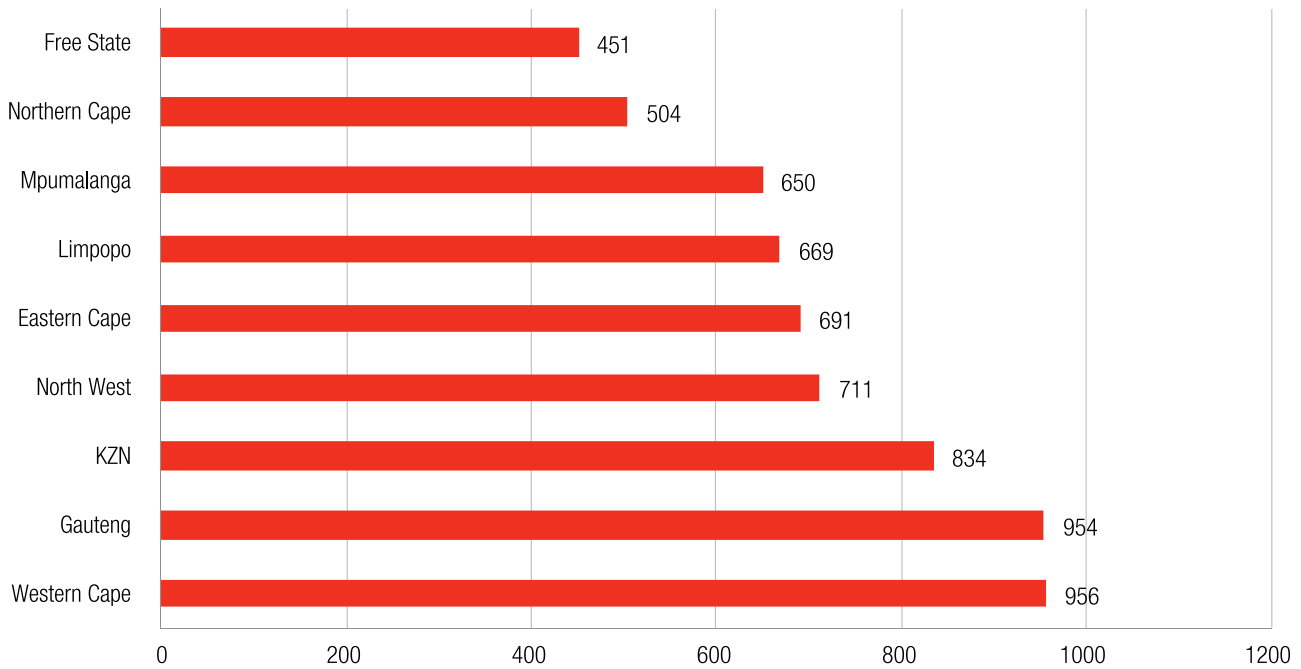


# Danger looming on the horizon



Average municipal costs per province

Source: PayProp



Average levy per province

Source: PayProp

# Something's got to give

While the data looks positive on the whole, we do feel concern for some of the underlying dynamics alluded to in our figures.

As we mentioned in our Q3 report, it is great for landlords and agents to see rentals increasing at rates above inflation, but this does not necessarily flow from a position of comfort for consumers. In fact, we believe that the shortage of rental properties is leading to owners asking and getting higher rentals than affordability dictates. All the supporting economic data — inflation, declining retail sales etc. — points to consumers increasingly being under financial strain.

On the other hand, landlords are not better off either. As mentioned above, while gross yields have grown by 2.90%, net yields have only increased by 2.6%, which means that landlords' costs of ownership have grown even faster than rentals. Landlords are essentially playing catch-up and have merely been fortunate that the market structure has enabled them to do so.

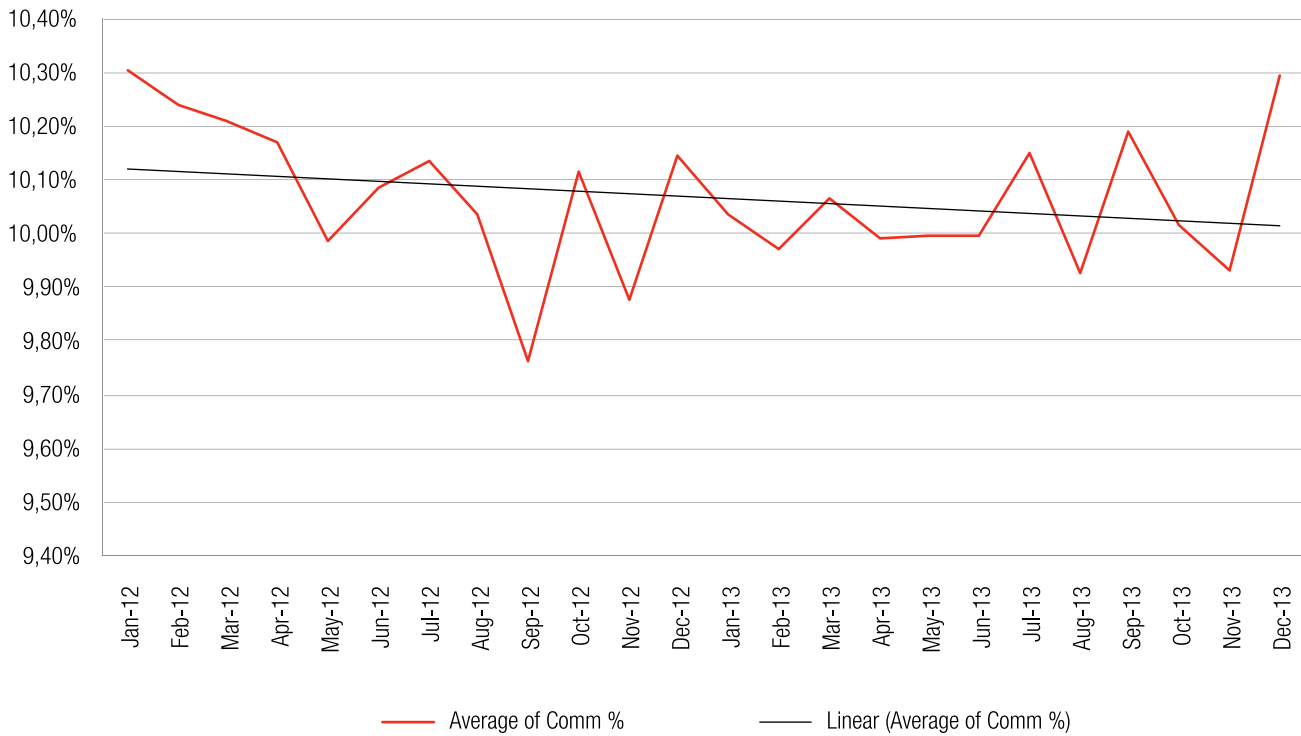
What does this mean for the future? Our concern is that the cracks may soon start to show. The risk is that tenants agreed to higher rentals than they can afford, in order to secure a property, and the growing cost of living may yet lead to them defaulting on payments.

One light at the end of this tunnel is that the nature of tenancy allows for a quicker scale-down decision than is possible with a purchased home. With the advent of the Consumer Protection Act, making a 20-day notice period by tenants a right, it is much easier and faster for a tenant under pressure to move to a smaller or more affordable home.

# Agent commissions remain stable

Estate agents, who sometimes get the short end of the stick, have successfully defended their commissions the past financial year. Commissions have stayed pretty stable at the 10% level since January, with a slight uptick in December – probably the result of seasonal rentals, which usually attract higher commissions.

This means the average PayProp client earns an estimated R50 762 in commission per month <sup>2</sup>.



Average agent commission  
Source: PayProp

<sup>2</sup> Based on average portfolio size. Bear in mind that PayProp clients usually have slightly larger portfolios. When compared to the norm of a 5% sales commission, this represents the equivalent of selling a R1m home each month, which speaks volumes for the value added by PayProp in saving managing agents time and allowing them to grow their portfolios.



# Our five predictions for 2014

We usually leave predictions to economists, but based on our analysis of the range of data we have accumulated, these are the five trends we expect to see in 2014:

1. Average rental growth will peak at 10% and gradually settle between 8% and 10%, as consumer pressure starts mounting.
2. Tenant payment data will deteriorate slightly as the economy tightens.
3. Damage deposit ratios will keep growing despite plummeting affordability, as owners seek protection against tenants ending contracts prematurely, resulting in greater uptake of deposit guarantee products.
4. Property investors will not see yields above 6% this year. Despite the growth in rentals, they are also likely to experience an increase in the cost of ownership.
5. Growth in the Northern Cape rental market is likely to be a strong theme in the months ahead, as the combination of industrial development and property scarcity combine to drive up rentals.

# PayProp Rental Index

The PayProp Rental Index is a quarterly guide on trends in the South African residential rental market, and is compiled from actual transactional data collected by PayProp, the largest processor of residential letting transactions in South Africa. This edition details market conditions for the four quarters of 2013 combined.

## Contact details

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

## Sign up for PayProp

If you would like to know more about using PayProp to manage your rental portfolio, please visit [www.payprop.co.za](http://www.payprop.co.za).

### Disclaimer

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# The benefits of PayProp



## GROWTH

Computerise all your back office admin so that your team can focus on signing new landlords and growing the business.



## ALERTS

Receive notifications when tenants haven't paid rent. PayProp warns you 2 months before tenancies end, so you can advertise early and avoid losses.



## ACCOUNTS

Your accountant will love PayProp as it provides detailed accounting records including contractor invoices.



## AUTOMATIC

Forget spreadsheets and bank statements, PayProp automatically reconciles all rent payments clearly showing who has and hasn't paid rent.



## ACCURATE

Reduce errors with ring-fenced funds. Only when money has been paid into a property can it be paid out.



## EFFICIENT

Once set up, PayProp runs on its own, invoicing tenants every month and paying money to landlords on collection, freeing you to focus on your business.



## TRANSPARENT

Receive clarity on the trust account status with bank data that is refreshed every 30 minutes.



## TEAM

Create unlimited free users, set their permissions to ensure control and track their performance.



## CLOUD BASED

No new servers or hardware needed, easy set up and friendly contract and notification terms.



## FAST

On receipt, collected rent can automatically be paid to landlords in 24 hours.



## SIMPLE

Monthly invoices are automatically sent by email & SMS to tenants, reducing arrears. Landlords receive automatically generated rental statements every month.



## SUPPORT

Receive unlimited free support from a locally based specialist team.



## ORGANISE

Set reminders, tagged by property and date, to help stay organised and schedule work.



## SECURITY

Your files, documents and information are safely backed up, easily accessible and protected by bank level security.



## NEXT STEP

To trial PayProp get in contact by emailing [support@payprop.co.za](mailto:support@payprop.co.za)

# MORE AND MORE ESTATE AGENCIES ARE MOVING TO PAYPROP



**JOE VAN ROOYEN**  
Seeff Durbanville



**SANDY WALSH**  
Anne Portrer Knight Frank



**LYNNE HENKENJOHANN**  
My Property Broker



**WERNER DU PLESSIS**  
Just Letting Brackenfell



**TREVOR HARRIS**  
RE/MAX Winelands



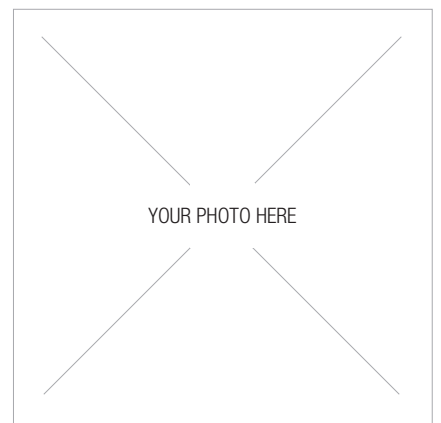
**LUCAS VAN VUUREN**  
Rawson Brackenfell



**MITSIE BOSHOFF**  
Wynland Properties Stellenbosch



**ELSA NAGEL**  
Only Rentals Helderberg



**YOUR NAME**  
Your Agency

To find out how PayProp can help you run a safer and more efficient rental portfolio, visit [www.payprop.co.za](http://www.payprop.co.za) or call 087 820 7368.

