

Rental demand on the rise, but landlords should note the risks

In the current high-interest rate environment, rental demand continues to rise, according to Ynnis Willson, head of the Rentals Division at Jawitz Properties, as consumers struggle to navigate the prevailing cost-of-living crisis and prospective home buyers delay purchases.



Ynnis Willson, head of the Rentals Division at Jawitz Properties

“Consumers are facing significant financial constraints after the prime lending rate rose rapidly from 7% in 2020 to 11.75% by May 2023,” she explains.

In the tougher economic climate, where inflation continues to increase the cost of living, consumers have less disposable income.

“Consumers are consequently spending less and taking a conservative approach until the economy stabilises. Concerns about continued high interest rates, economic instability, and affordability issues are driving more people, particularly those under the age of 35, to rent instead of buy.”

Data from Absa echoes Willson's view, showing that buyer and seller sentiment both declined in Q4 2022 and Q1 2023, with buy-rather-than-rent sentiment dropping to its lowest level on record (61%) in Q1 2023.

Rental yields showing improved growth

While these factors are negatively impacting property values, TPN data shows that rental yields are showing improved growth due to a rationalisation from rising rental income and stagnant property values.

“Although interest rates remained unchanged at the latest MPC meeting, we are not out of the woods, as the Reserve Bank's approach remains cautious. It is unlikely that rates will decrease in the near future, and this continues to drive rental demand,” says Willson.

“In addition, many current renters are considering downscaling to areas that offer better value.”

However, with no shortage of supply, particularly in major centres like Johannesburg and Pretoria, rental escalations are struggling to keep up with inflation. The most recent *TPN Residential Rental Monitor* revealed an increase from 3.02% to 3.56% between Q3 and Q4 2022.



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Rental growth stronger in higher rental brackets

According to the TPN data, rental growth is stronger in higher rental brackets, with properties over R12,000/month experiencing the most growth at 4.38%. Sectional title properties offered the highest rental yields at 10.18% in Q4 of 2022 compared to just under 7% for freehold properties.

“Despite the rising demand, landlords face various challenges as higher interest rates increase bond repayments, the increase in property rates and taxes as a result of the updated valuation roll and other cost escalations mean expenses exceed the rental income, which impacts yield,” explains Willson.

In this environment, Willson cautions landlords against implementing above-inflation rental escalations to cover the shortfall.

“With strong rental supply, particularly from developers that are struggling to sell units in new developments and can afford to undercut rental prices, landlords need to weigh the opportunity cost associated with having no tenant versus the cost of covering a shortfall.”

In addition, landlords must consider the value that retaining a long-term reliable tenant offers in the current economic climate.

“Pushing for above-inflation rental escalations could force existing tenants to consider downscaling,” continues Willson. “There are also costs and risks associated with securing and vetting prospective new tenants, and there is no guarantee that landlords will secure a tenant at the higher rental rate in the current market.”



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Understanding tenant risk

Given the current economic climate, understanding tenant risk has never been more important amid the cost-of-living crisis.

“Landlords must perform thorough vetting and credit checks and gain access to all the information they need to make an informed decision,” asserts Willson.

“An experienced rental agent can add immense value in this market by performing these tasks on behalf of landlords, and they have the experience to pick up on trends that raise red flags, like how often a tenant moves.”

A rental agent also provides benefits to tenants by ensuring there is a proper lease agreement in place that protects their rights.

“Conducting impartial and thorough entry and exit inspections also protects the best interests of both the tenant and landlord,” concludes Willson.

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