

# RENTAL INDEX

QUARTER ONE 2019



## How to spot a bad tenant.

Tracking rental demand in your area.

Continued rental market recovery?

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## Introduction

# POST-ELECTION PREDICAMENT

By the time you read this, the 2019 South African general election will be over.

The lead-up to it has been a major source of uncertainty and volatility, affecting everything from the stock market to the exchange rate and even property prices. But that's not to say things will be more stable now – the ruling party will have a tough job in the months following its win to take a meaningful stand against corruption and failing state-owned enterprises and to clarify its plans around land reform and economic growth.

How does this affect you, you might wonder? Generally, uncertainty decreases consumer confidence, which could leave property buyers reluctant to commit in coming months, effectively dampening demand and putting downward pressure on prices.

Meanwhile, all these prospective buyers need to live somewhere, and they'll most likely be forced to rent a property, thus increasing demand for rental properties and pushing up prices. We believe that we'll see further rental market recovery in 2019 – read all about it in this issue of the PayProp Rental Index.

Until next time – it will be fascinating to see what rental market data comes out of the next quarter! ■

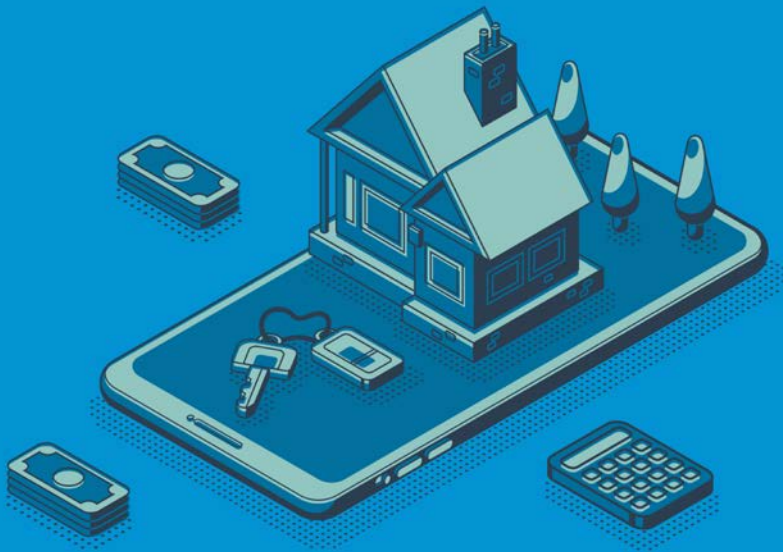


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All these prospective buyers need to live somewhere, and they'll most likely be forced to rent a property, thus increasing demand for rental properties and pushing up prices.

# Efficient growth through automation



PayProp can help you automate your entire rent collection process, freeing you up to grow your lettings business without the extra staff overhead.

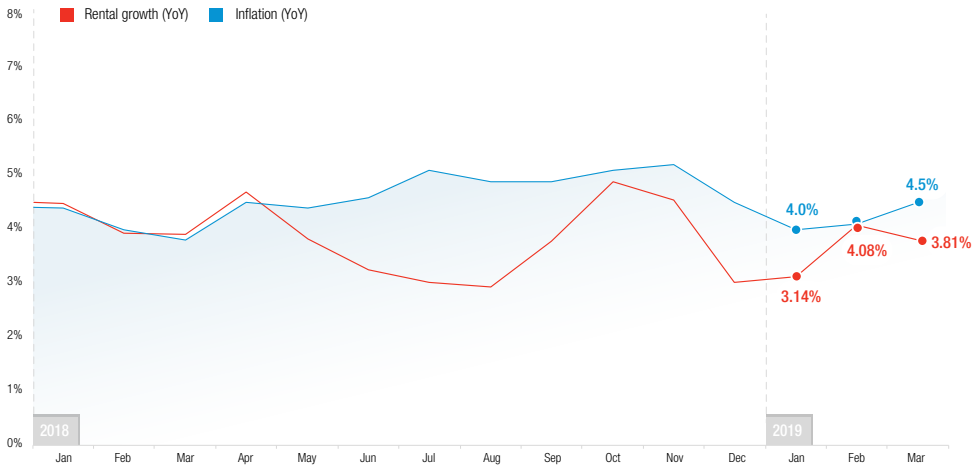
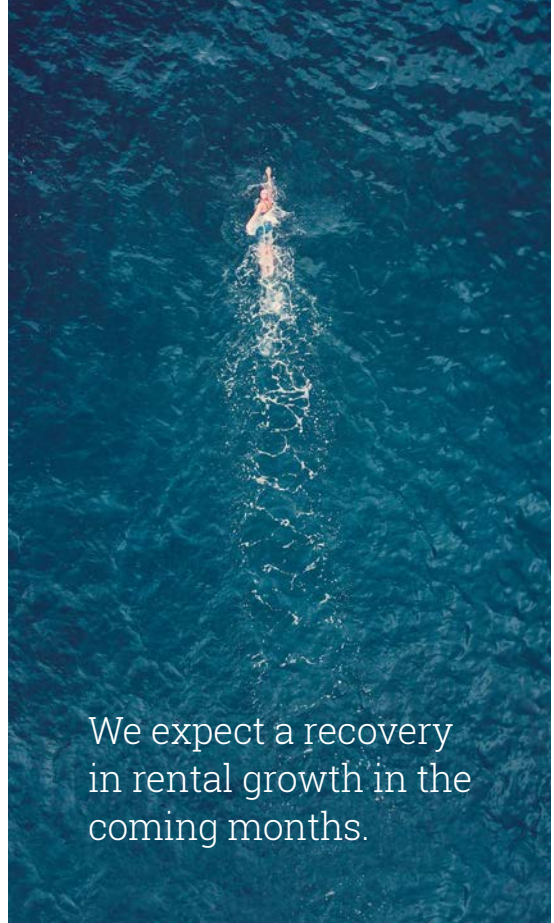
## National rent statistics

# SMOOTH SAILING

We've become so used to seeing a downward-trending rental growth graph that flat growth almost feels wrong – but it definitely marks a welcome change!

Since the start of 2018 and for the first three months of 2019, inflation has continued to outperform the year-on-year rental growth rate into the new year.

The latter is still subdued but at least trending sideways – and as the next section looking at quarterly growth explains, we expect a recovery in rental growth in the coming months. ■



Weighted average national rental growth rate (YoY) vs. inflation since January 2018

Source: PayProp

## Quarterly national growth

# IS THE MARKET RECOVERING?

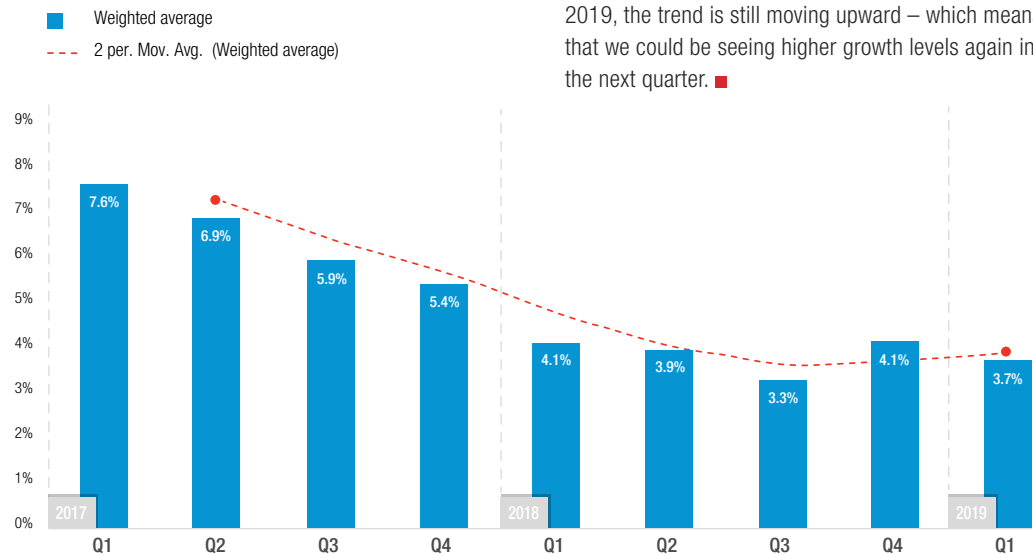
Q4 2018 brought the first uptick in the national rental growth rate in two years – the quarterly figure, measured year-on-year (YoY), encouraging 4.1% growth rate – up from 3.3% in Q3. For six consecutive quarters before that, growth trended downward, with each quarter's number being lower than the one before!


With the quarterly YoY growth rate for Q1 2019 coming in at 3.7% (vs 4.1% in Q4 2018), what does that mean for market recovery? Good things, as it turns out.

### Growth outlook – a moving target

Moving averages are often used to forecast trends, because they look at the average movement over longer, overlapping periods of time.

We arrived at that conclusion at the hand of a moving average trendline in the quarterly growth graph, which plots the average of each pair of two consecutive quarters. This line shows a turning point in Q4 2018, but it doesn't stop there. Even with lower growth in Q1 2019, the trend is still moving upward – which means that we could be seeing higher growth levels again in the next quarter. ■



 Quarterly year-on-year national growth rate with a moving average trendline  
Source: PayProp



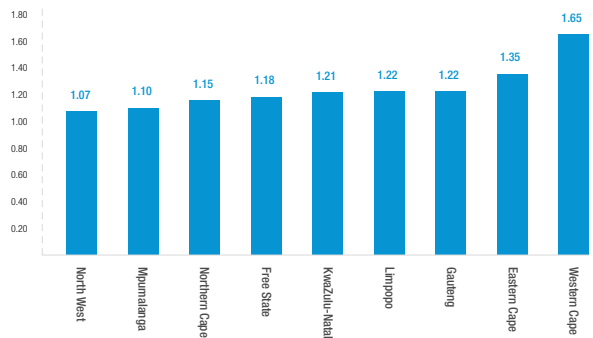
## Damage deposit ratios

# PROTECT YOUR LANDLORDS

The concept of insurance has been around for centuries. And in essence, that is exactly what a damage deposit is – landlord ‘insurance’ or protection against damage to their property, caused by a tenant.

As can be seen below, different provinces have different average damage deposit ratios – ranging from 1.07 to 1.65. This means tenants pay at least 1.07 times their monthly rent in upfront damage deposit ‘insurance’, and at most 1.65 times.

What is the average damage deposit ratio for your portfolio relative to your province? ■



 Damage deposit ratios per province for Q1 2019  
Source: PayProp

### Affordability ratio

$$\text{Damage deposit ratio} = \frac{\text{average damage deposit held}}{\text{average rental invoiced}}$$



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## Provincial statistics

# RENT DISTRIBUTION

As noted in the last PayProp Rental Index, the average national rent moved up into the R7,500 – R10,000 price band for the first time in Q4 2018. Nevertheless, almost a third of rents processed by PayProp still fell into the R5,000 – R7,500 category.

With that being the case, all provinces' average rent fall within one of these two rental bands.

In this section, we unpack the spread across rental categories for each province. This gives an indication of the rental properties that are in demand to guide landlords looking to invest in a buy-to-let property. ▶▶

Province	Average rent	Category
North West	R5,031	R5,000 – R7,500
Eastern Cape	R5,694	R5,000 – R7,500
Free State	R6,054	R5,000 – R7,500
Limpopo	R7,117	R5,000 – R7,500
Mpumalanga	R7,298	R5,000 – R7,500
<b>National average</b>	<b>R7,551</b>	<b>R7,500 – R10,000</b>
Northern Cape	R7,817	R7,500 – R10,000
KwaZulu-Natal	R7,975	R7,500 – R10,000
Gauteng	R8,000	R7,500 – R10,000
Western Cape	R9,030	R7,500 – R10,000



Average national distribution of properties across price bands

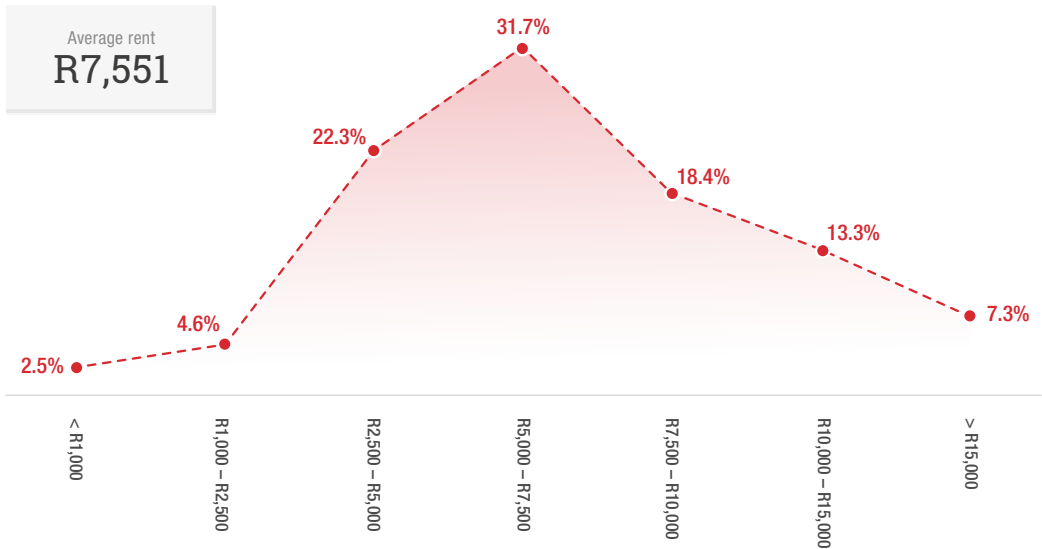
Source: PayProp




## Provincial statistics

# NATIONAL

Most properties administered via PayProp are still in the R5,000 – R7,500 category (31.7%). It is further interesting to note that there are more properties in the >R15,000 bracket than in the two lowest categories combined (<R1,000, and R1,000 – R2,500)<sup>1</sup>.



 Average national distribution of properties across price bands  
Source: PayProp

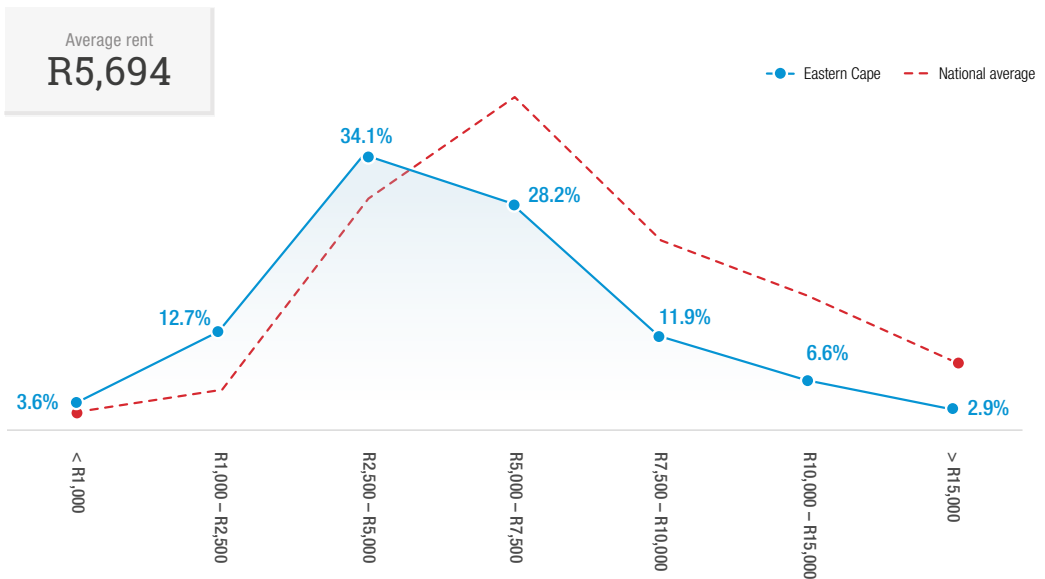
<sup>1</sup> The average distribution is a breakdown of all properties managed through PayProp, whereas the average rent is calculated using provincial GDP contributions as a weighting.



## Provincial statistics

# EASTERN CAPE

Although the average rent in the Eastern Cape is R5,694, 34% of rents in the province fall within the R2,500 – R5,000 category. Over 62% are between R2,500 – R7,500. The Eastern Cape has the highest percentage of rentals below R2,500 out of all the provinces.



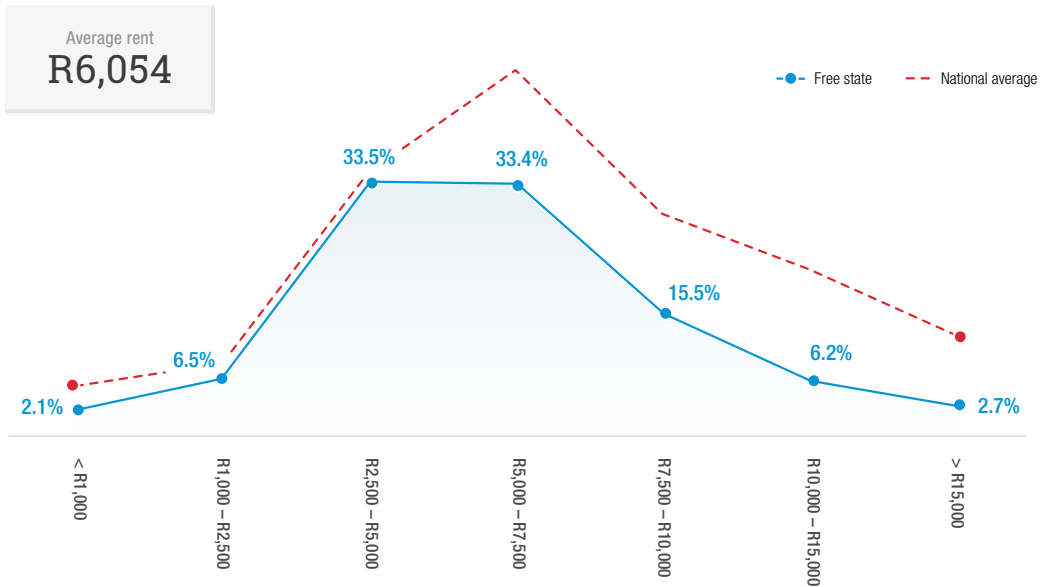
 The Eastern Cape's distribution of rentals across price bands  
Source: PayProp



## Provincial statistics

# FREE STATE

At R6,054, the average rent in the Free State falls within the R5,000 – R7,500 category, and yet a third of all rentals in the province fall within in the bracket below. Over two-thirds of rental properties are rented for R2,500 – R7,500.



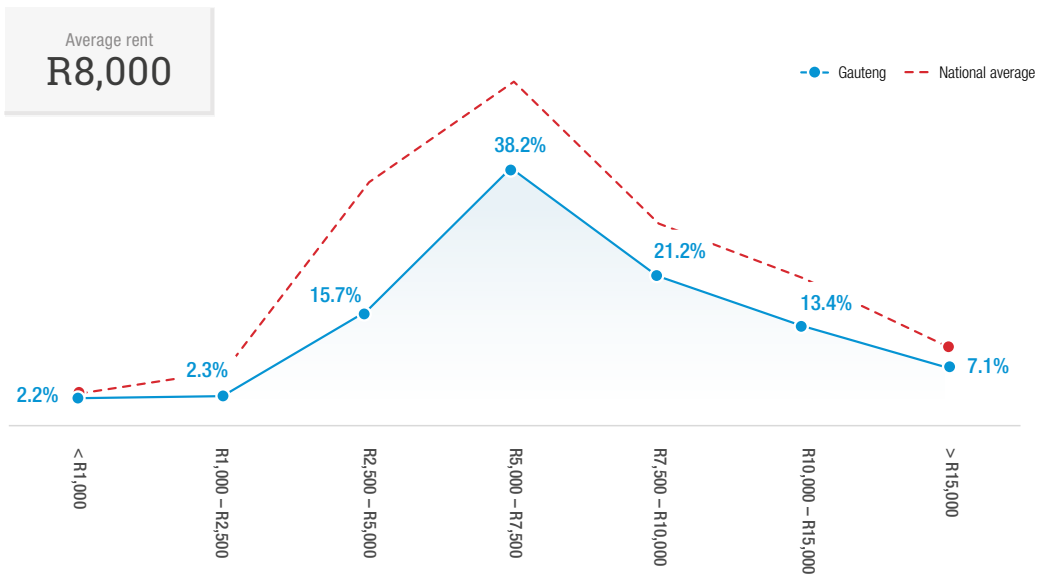
 The Free State's distribution of rentals across price bands  
Source: PayProp




## Provincial statistics

# GAUTENG

In a similar picture to the Free State, almost 40% of Gauteng rentals are priced between R5,000 – R7,500, and yet the average rental is R8,000, the second-highest of all the provinces in Q1 2019. Over 20% of rentals in the province are priced higher than R10,000.



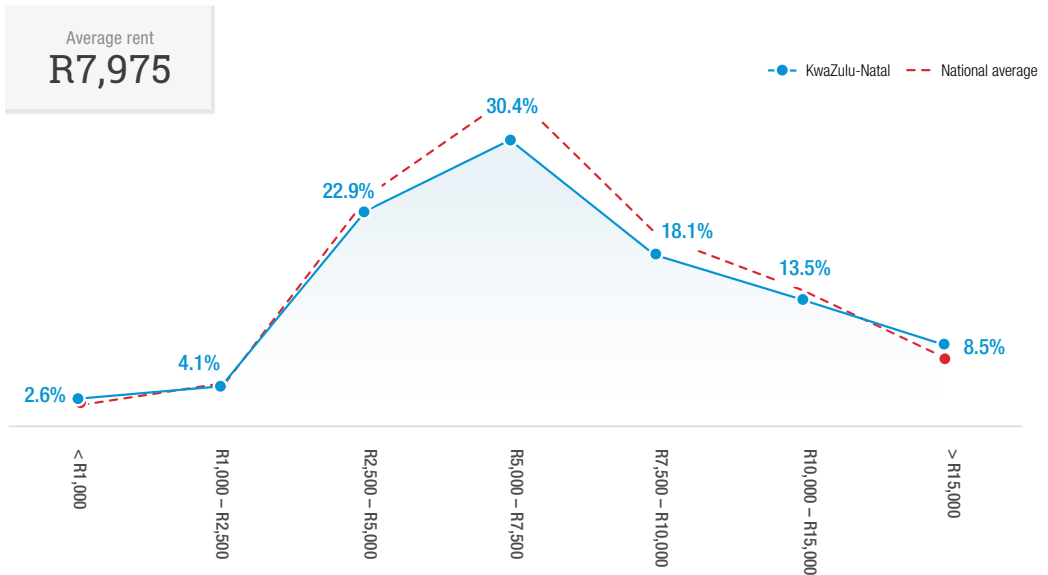
 Gauteng's distribution of rentals across price bands  
Source: PayProp



## Provincial statistics

# KWAZULU-NATAL

KwaZulu-Natal is the third most expensive province to rent in, but while the average rental falls within the R7,500 – R10,000 bracket at R7,975, only 18% of rentals in the province are in this bracket. KZN has the second biggest percentage of rentals priced over R15,000.



 KwaZulu-Natal's distribution of rentals across price bands  
Source: PayProp

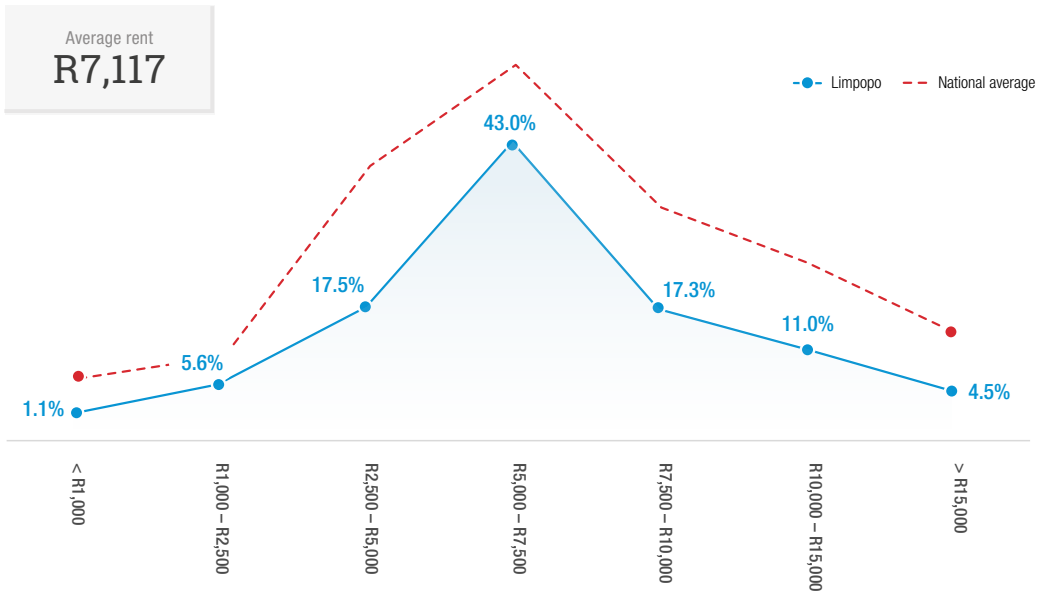





## Provincial statistics

# LIMPOPO

Out of all the provinces, Limpopo's distribution across the various price bands is the most symmetrical. Because of this and the high percentage of rentals in the R5,000 – R7,500 bracket, it's no surprise that the average rent in the province (R7,117) falls within this band as well.



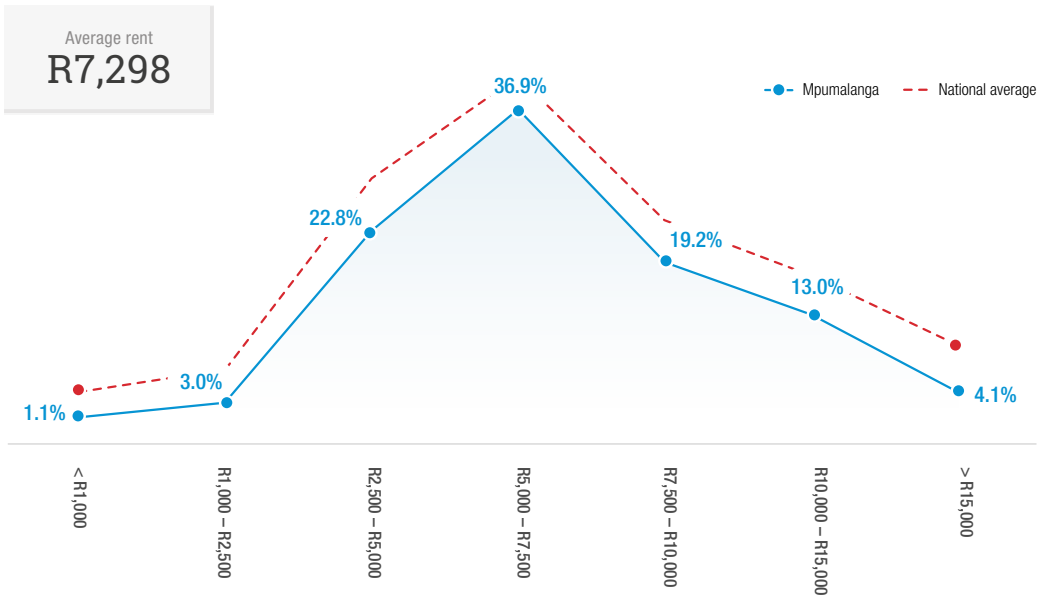
 Limpopo's distribution of rentals across price bands  
Source: PayProp




## Provincial statistics

# MPUMALANGA

More than a third of Mpumalanga's rentals fall within in the R5,000 – R7,500 bracket, which is also where the average rental in the province (R7,298) falls. Mpumalanga's price band distribution is skewed towards more expensive rentals, with over 36% of rentals priced over R7,500.



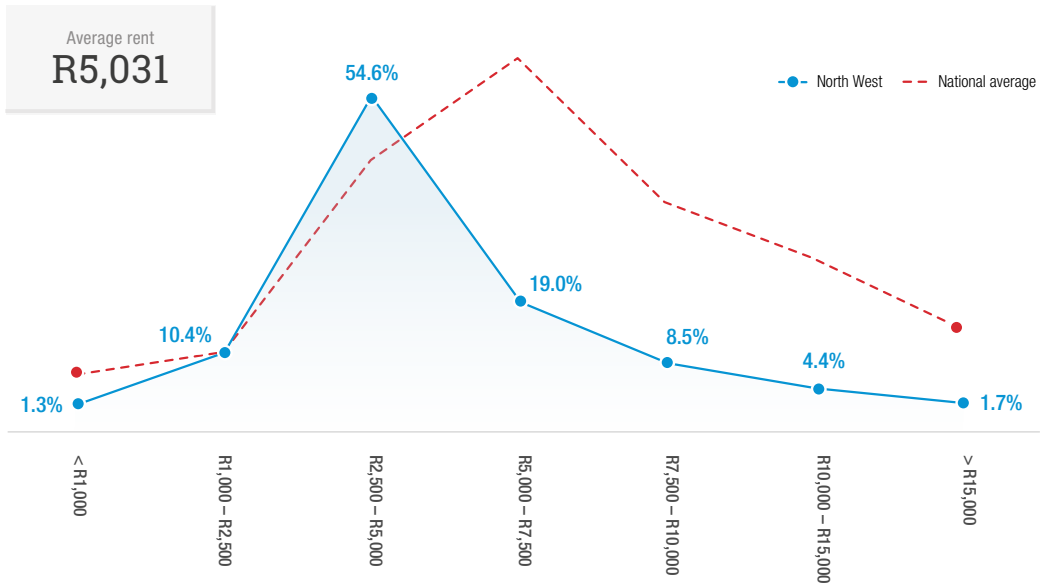
 Mpumalanga's distribution of rentals across price bands  
Source: PayProp




## Provincial statistics

# NORTH WEST

Out of all the provinces, North West has the biggest percentage of renters in any one bracket – 54.6% of tenants in the region rent for between R2,500 – R5,000. It also has the country's lowest average rent (R5,031) and the smallest percentage of rentals over R15,000.



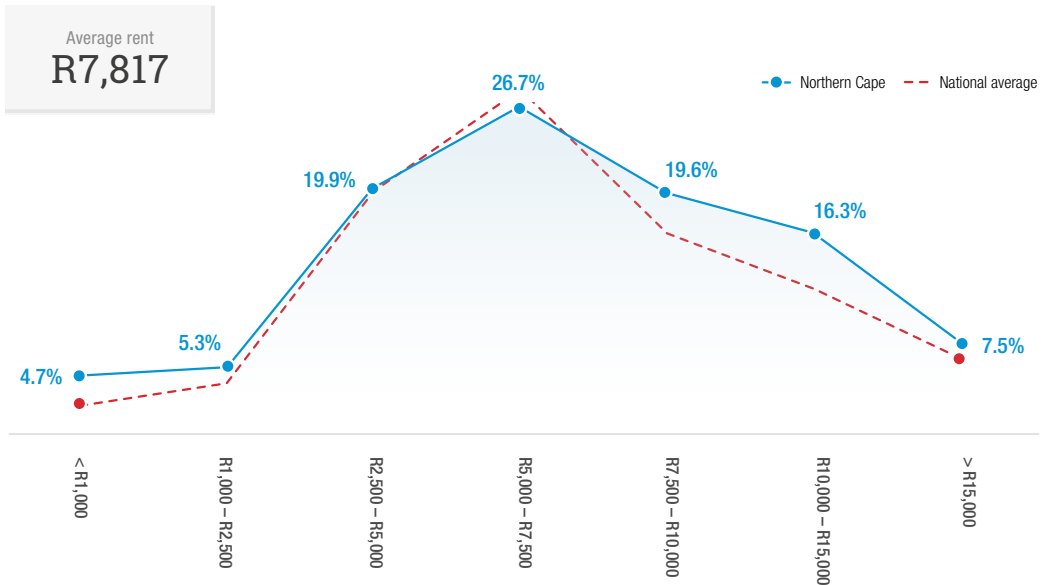
 North West's distribution of rentals across price bands  
Source: PayProp




## Provincial statistics

# NORTHERN CAPE

The Northern Cape has a fairly even price band distribution across the middle ranges, and only 26% of the province's rentals fall within the R5,000 – R7,500 band, the most populous national category. Almost 20% of rentals fall within the brackets on either side, putting almost two-thirds of all Northern Cape rentals in the R2,500 – R10,000 range. Only 10% of rentals are less than R2,500 per month.



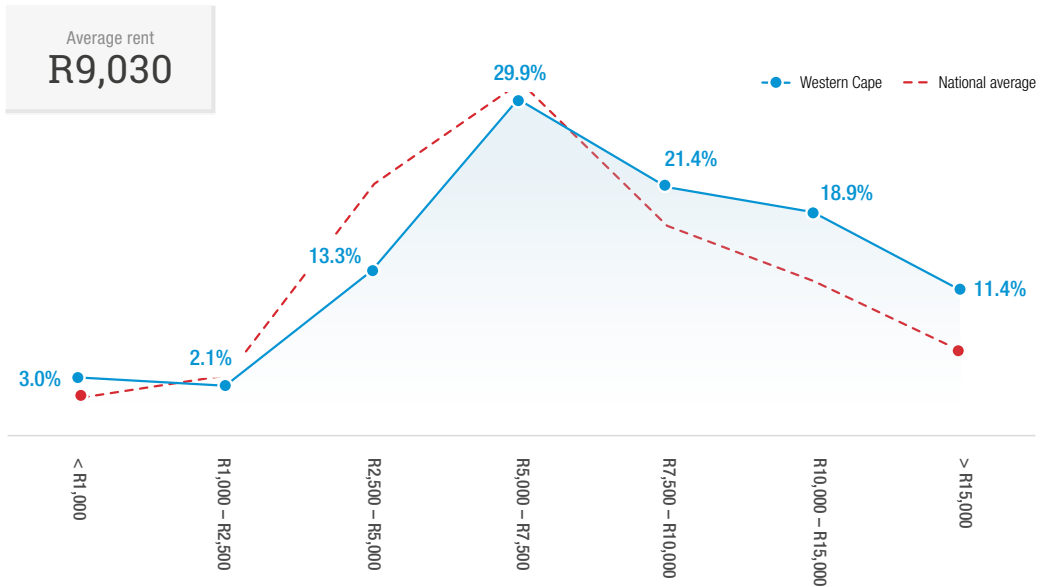
 Northern Cape's distribution of rentals across price bands  
Source: PayProp



## Provincial statistics

# WESTERN CAPE

The Western Cape, which recorded an average rent of R9,030, remains the most expensive province to rent in. However, most rents in the province are between R5,000 – R7,500, with 30% falling in this category. More than 30% of rentals in the province are priced over R10,000, and over 11% is priced above R15,000 – the highest percentage in this band out of all the provinces.



 Western Cape's distribution of rentals across price bands  
Source: PayProp



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High-risk unpacked

# HOW TO SPOT A BAD TENANT



It's important to note that a credit score is not necessarily an accurate indicator of how reliably a tenant will pay their rent.



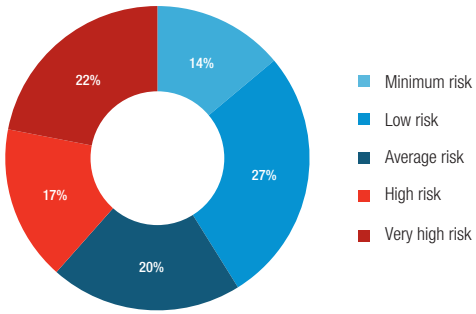
Your credit score is an important metric – it puts you in a 'bucket' indicating to retail stores, banks and other credit providers how trustworthy and responsible you are with your finances.

It's important to note that a credit score is not necessarily an accurate indicator of how reliably a tenant will pay their rent (it tracks their credit payment record, not their rent payment record). However, it is often the only way rental agents have of extrapolating rent payment behaviour.


It is common knowledge that many factors affect a tenant's credit score, and in this section we will attempt to put all the different aspects into the bigger picture. ▶▶

#### Tenant data

Tenant data – including income data – is obtained from Tenant Assessment Reports generated for our clients. The data is not weighted or necessarily indicative of the average tenant currently occupying a property.



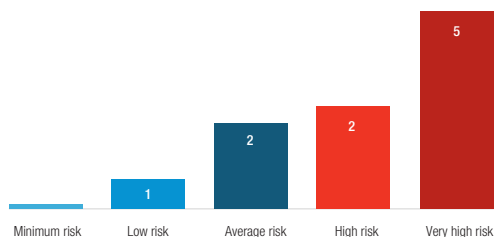
As we can see from the chart on the left, almost 40% of tenancy applicants in Q1 were classified as either high risk or very high risk. This again shows how important it is to vet tenants properly before placing them. ▶▶


 Distribution of applicants across credit risk categories  
**Source: PayProp**



## Credit

Access to credit is often a catch-22 situation – you can't get credit without a good credit score, but you can't build a good credit record without credit. These so-called "thin files" often appear when doing credit checks on young applicants or applicants who just started their first job.

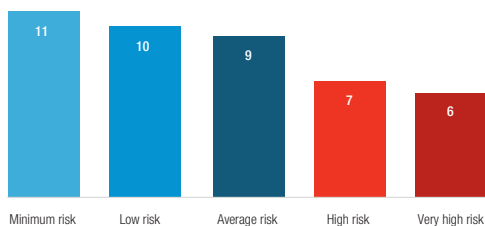



 Average number of NLR accounts per applicant in each risk category

Source: PayProp

## Credit score indicator 1: Type of credit

Not all debt is created equally, and it is important to distinguish the good from the bad. Tenants can have two types of accounts – CPA (Credit Provider Association) accounts and NLR (National Loan Register) accounts. CPA accounts include insurance, cell phone contracts, retail stores and vehicle finance. These are the type of accounts you can reasonably expect someone to have, and they can be seen as 'good debt'.



 Average number of CPA accounts per applicant in each risk category

Source: PayProp

NLR accounts, on the other hand, is something you don't want to see on a credit check. These include short-term loans from micro-lenders, usually with very high interest rates, and can be seen as 'bad debt'.

Two correlations are clear when looking at account types – higher-risk tenants have fewer 'good debt' accounts and more 'bad debt' accounts than other risk categories.

Note the big jump to the right of the second graph – very high-risk tenants have on average five 'bad' accounts, compared to high-risk tenants.

It is also interesting to note that tenants on the low-risk end of the scale tend to have more CPA accounts. ▶▶

## Risky tenants

We usually talk about risky tenants or high-risk tenants in the Rental Index, but that consists of two risk categories – high risk, and very high risk. For the purpose of this analysis, we will keep them separate.



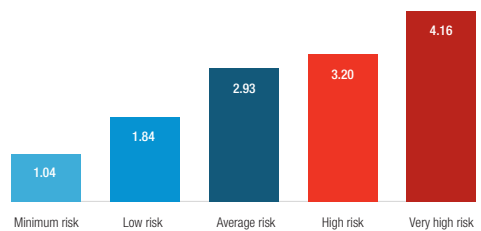
## Over-60s


Over-60s are often pensioners, and their retirement income is usually lower than their final salaried income – which is why the upward trend stops with the 50 – 59 category.

## Credit score indicator 2: Credit enquiries

When tenants apply for credit, it could be a sign that they aren't able to get by with their salary. When they apply for credit often, it indicates that either the credit they received initially wasn't enough, or the credit wasn't granted, leading the application to re-apply somewhere else.

There are exceptions, of course – a tenant could simply be shopping around for the best interest rate for vehicle finance, for example. Overall, though, we see a correlation between riskiness of a tenant and the number of credit enquiries done through various institutions.



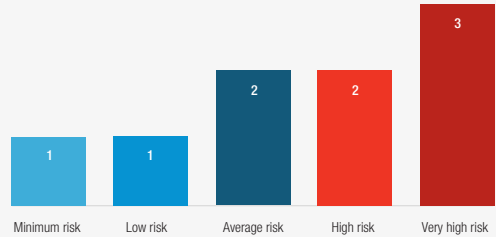
 Average number of recent credit enquiries per applicant in each risk category


Source: PayProp

### Credit score indicator 3: Payment behaviour

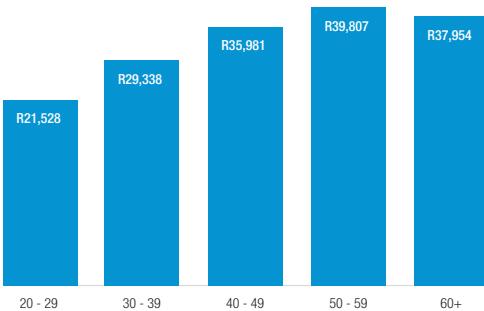
Most accounts have to be paid monthly, usually by a set date. Failure to make timeous payments will negatively affect a credit score.


As we see on the right, tenants on the risky end of the spectrum have had more accounts in arrears in the last year than those on the low-risk end.



 Average number of accounts in arrears per applicant in each risk category

Source: PayProp



 Average net income per applicant in each age bracket

Source: PayProp

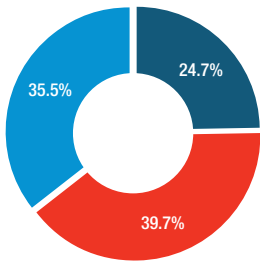
### Other factors to consider:

Sometimes multiple cellphone numbers or even addresses can be indicative of poor creditworthiness, as it could indicate that an applicant is trying to avoid debt collectors.

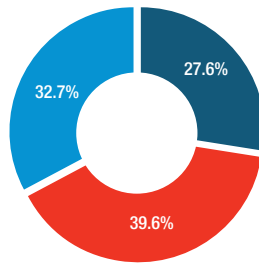
### The age-income link

It stands to reason that younger employees typically earn less money, and this is borne out by the data. The exception to this can be found in tenants over 60. But the correlation between age, income and risk is not cut and dried. Younger tenants can indeed pose minimum risk and older tenants with higher incomes can post a high risk – as we say, many factors affect a credit score. Generally, though, there's a strong link between risk and affordability. ▶▶



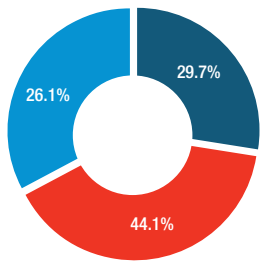


Minimum risk

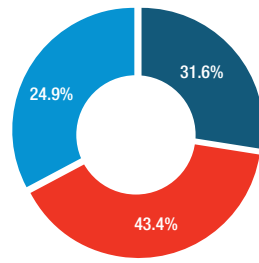


Low risk

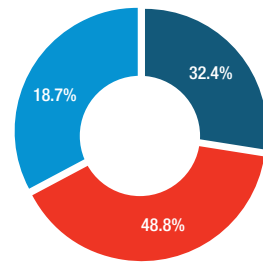
- Rent
- Disposable income
- Debt



Average risk

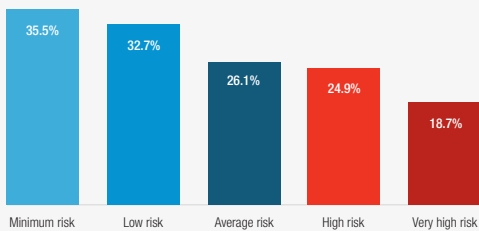


High risk



Very high risk

■ Distribution of net income per risk category  
Source: PayProp



If we ignore the rand value of income it is evident that riskier tenants spend a higher percentage of their income on rent and debt repayments, and ultimately have a smaller percentage of their net income left as disposable income. ■

■ Disposable income as a percentage of net income in each risk category  
Source: PayProp

# THE PAYPROP RENTAL RISK RATING



PayProp, together with our credit bureau partner Compuscan, bring you a revolutionary tenant risk measure – the PayProp Rental Risk Rating. It combines rental payment data with tenant's credit profile to give you a more accurate predictor of future tenant behaviour than a credit score.

We are cautiously optimistic about continued recovery in the rental market after the signs we've seen over the last few months.

## Conclusion

# CAUTIOUSLY OPTIMISTIC

While volatility is likely to persist in the rental market and economy in general after the election, things are looking up.

We are cautiously optimistic about continued recovery in the rental market after the signs we've seen over the last few months. After all, 2018 brought an end to the two-year downward trend in rental growth rates!

To do their bit, every agent should focus on placing good tenants, which means knowing how to spot a high-risk tenant.

In all this, affordability is usually the most important factor.

All the best for the rest of 2019!



# PAYPROP RENTAL INDEX

The PayProp Rental Index is a quarterly guide outlining trends in the South African residential rental market, and is compiled from transactional data collected by PayProp, the largest processor of residential letting transactions in South Africa.

## Contact details

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

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