RESEARCH
Industrial Vacancy Report
KEY FINDINGS

As at June 2019, the national industrial vacancy rate as recorded was 3.4% as measured by the MSCI Annual Property Index – unchanged on the revised December 2018 figure. The industrial sector vacancy rate has now been below 4% since 2012Q1 barring a temporary development-driven blip in the first half of 2017 underlining the sector’s high level of occupancy despite a challenging macroeconomic backdrop.

The low & stable vacancy rate has see the sector’s base rental growth remain closely tied to inflation which suggests that little excess supply remains in the marketplace. During the first half of 2019, base rental growth increased to 5.3% from 4.7% as at December 2018.

This basic rental growth of 5.3% hasn’t filtered through to an equal level of capital growth which suggests that valuers are still taking a slightly cautious view on future earnings and instead preferring to leave some return on the table. That said, industrial sector capital growth at 2.4% outstripped the retail (0.9%) and office (0.2%) sectors over the last year.

Industrial property fundamentals have benefited from relatively constrained supply, stable capacity utilisation, and steady (though not spectacular) growth in manufacturing volumes despite an unfavourable macroeconomic climate.

Historically, there has been a 12-24 month lag between economic data releases and meaningful shifts in industrial property fundamentals. For that reason, the level of building completions and manufacturing production recorded for the rest of 2019 will be critical to the sector’s short term fortunes.

In July 2019, building completions reached a 9 year high (on a 12 month rolling basis) and manufacturing volumes recorded one of its worst single-month drop in the last five years. If this signals the start of a softening trend, industrial property fundamentals might deteriorate while a rebound in production and moderation in supply will likely see the sector continuing its outperformance.

All industrial segments saw their vacancy rates improve further during the year to June 2019 – with the exception of Industrial Multiparks which saw a 120bp from 5.6% to 6.8%. The vacancy rate of manufacturing property at 0.3% is the lowest among the industrial segments suggesting that the improved manufacturing output of 2018 has had a positive impact on the segment’s occupancy.

The vacancy rate of Warehouse & Distribution related property improved 50bps to 4.0% with its base rental growth declining to 4.2% from 5.6%. This suggests that landlords are having to trade off rental growth in favour of filling vacant space.

Analysing industrial property by box size reveals a mixed picture. Small units below 2.5k sqm and large units of above 25k sqm saw its vacancy rates rise in the year to June 2019. So too units with a GLA of between 5k and 10k sqm.

It would appear as if occupiers in the 5-10k sqm and >25k brackets are trading down into smaller boxes as the challenging macroeconomic environment and sideways trending capacity utilisation has occupiers searching for consolidation benefits and operational efficiency gains.
NATIONAL INDUSTRIAL VACANCY & RENTAL GROWTH TREND

As at June 2019, the national industrial vacancy rate as recorded was 3.4% as measured by the MSCI Annual Property Index – unchanged on the revised December 2018 figure. The industrial sector vacancy rate has now been below 4% since 2012Q1 barring a temporary development-driven blip in the first half of 2017 underlining the sector’s high level of occupancy despite a challenging macroeconomic backdrop. Among the three major property sectors, industrial’s vacancy rate is currently lower than that of retail (4.7%) and office (12.8%).

The low & stable vacancy rate has see the sector’s base rental growth remain closely tied to inflation which suggests that little excess supply remains in the marketplace. During the first half of 2019, base rental growth increased to 5.3% from 4.7% as at December 2018.

This basic rental growth of 5.3% hasn’t filtered through to an equal level of capital growth which suggests that valuers are still taking a slightly cautious view on future earnings and instead preferring to leave some return on the table. That said, industrial sector capital growth at 2.4% outstripped the retail (0.9%) and office (0.2%) sectors over the last year.
ECONOMIC DRIVERS OF THE INDUSTRIAL SECTOR

Manufacturing Production
y/y change; constant price terms

Private sector employment-
Manufacturing
y/y change

Industrial Capacity Utilisation
percentage

Industrial building plans passed & completed
square meters; 12-months moving average

Source: SA Reserve Bank, StatsSA

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PERFORMANCE BY INDUSTRIAL SEGMENT

All industrial segments saw their vacancy rates improve further during the year to June 2019 – with the exception of Industrial Multiparks which saw a 120bp from 5.6% to 6.8%. The vacancy rate of manufacturing property at 0.3% is the lowest among the industrial segments suggesting that the improved manufacturing output of 2018 has had a positive impact on the segment’s occupancy.

Manufacturing production pulled back during the 2nd quarter of 2019 which could see heightened pressure on the segment’s vacancy in the short to medium term given the lag that exists between the economy and property fundamentals.

The vacancy rate of Warehouse & Distribution related property improved 50bps to 4.0% with its base rental growth declining to 4.2% from 5.6%. This suggests that landlords are having to trade off rental growth in favour of filling vacant space. Anecdotally, this segment has seen the most speculative development which likely is a factor in this trend.

The ‘Other Industrial’ segment which includes the historically defensive High Tech Industrial segment saw its vacancy rate remain low at 1.7% - down 10bps on a year before. As with the Warehousing segment it seems gains in occupancy are coming at the expense of rental growth. The segment’s rental growth declined from 4.4% to 0.8% during the year.
PERFORMANCE BY BOX SIZE

Analysing industrial property by box size reveals a mixed picture. Small units below 2.5k sqm and large units of above 25k sqm saw its vacancy rates rise in the year to June 2019. So too units with a GLA of between 5k and 10k sqm.

The smallest size bracket saw its occupancy rate soften the most with its vacancy rate rising from 2.3% to 4.5% in the 12 month period. This suggests that there is currently relatively more pressure on the lower end of the size spectrum as the difficult macroeconomic environment weighs heavier on smaller operations.

Industrial units sized between 10k-25k sqm ended the period with a vacancy rate of 2.2% - the lowest among the size segments and an improvement on the 3.2% recorded for June 2018. The vacancy rate of units in this size bracket has trended down ever since reaching a high of 4.8% in mid-2016. Industrial units with a GLA of between 2.5k and 5k sqm has also seen its vacancy rate improve for the 12 months ended June 2019.

It would appear as if occupiers in the 5-10k sqm and >25k brackets are trading down into smaller boxes as the challenging macroeconomic environment and sideways trending capacity utilisation has occupiers searching for consolidation benefits and operational efficiency gains. At the same time, there is seemingly little downside in this for tenants as properties with a rentable area in excess of 2.5k sqm are usually equipped with the same features as larger properties, whether it be on-grade or dock loading and levelers for distribution-focused tenants or three-phase power, on-grade vehicle access and sufficient ablutions for manufacturing concerns.
NODAL PERFORMANCE
SIGNIFICANT VARIANCE ON NODAL LEVEL

As at June 2019, the aggregate industrial vacancy rate remains low at 3.4% while base rental growth increased to 5.3% year-on-year. However, there is still significant variance between the underlying nodes’ vacancy rate and base rental growth.

Some nodes have very limited amounts of space available to let coupled with robust rental growth while elsewhere, excess supply is weighing on rental growth.

The graphic below emphasises this point as the major industrial nodes are well dispersed in their current position in vacancy cycle. Active asset management with a focus on tenant retention and portfolio diversification – via different geographies & property subtypes- remain key at a time when tenants are looking to unlock efficiencies rather than expand.

Centurion is a good example of a node where landlords are prioritising tenant retention, even if it does come at the cost of rental growth. As at June 2019, the node’s vacancy rate was a low 1.6% but a rental growth of -4.3% has see the node’s three year annualised rental growth fall below 5%.

In contrast, the Cape Town industrial area encompassing Epping & Airport Industria also had a vacancy rate of 2.4% as at June 2019 but stronger rental growth of 6.7% over the last 12 months and 11.4% over the last three years.
### Sample Composition as at June 2019

#### By Segment

<table>
<thead>
<tr>
<th>Capital Value</th>
<th>Number of Properties</th>
<th>Owned Area (m²)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Industrial - Manufacturing</td>
<td>21%</td>
<td>52%</td>
</tr>
<tr>
<td>Industrial - Multi Parks</td>
<td>46%</td>
<td>22%</td>
</tr>
<tr>
<td>Industrial - Other</td>
<td>6%</td>
<td>8%</td>
</tr>
<tr>
<td>Industrial - Warehousing &amp; Distribution</td>
<td>21%</td>
<td>25%</td>
</tr>
</tbody>
</table>

#### By Box Size

<table>
<thead>
<tr>
<th>Capital Value</th>
<th>Number of Properties</th>
<th>Owned Area (m²)</th>
</tr>
</thead>
<tbody>
<tr>
<td>All Industrial: 0 - 2 500 m²</td>
<td>1.7%</td>
<td>14.9%</td>
</tr>
<tr>
<td>All Industrial: 2 500 - 5 000 m²</td>
<td>6.8%</td>
<td>19.6%</td>
</tr>
<tr>
<td>All Industrial: 5 000 - 10 000 m²</td>
<td>16.4%</td>
<td>25.6%</td>
</tr>
<tr>
<td>All Industrial: 10 000 - 25 000 m²</td>
<td>35.7%</td>
<td>29.2%</td>
</tr>
<tr>
<td>All Industrial: &gt; 25 000 m²</td>
<td>39.3%</td>
<td>10.7%</td>
</tr>
</tbody>
</table>

#### By Value

<table>
<thead>
<tr>
<th>Capital Value</th>
<th>Number of Properties</th>
<th>Owned Area (m²)</th>
</tr>
</thead>
<tbody>
<tr>
<td>All Industrial: &lt; R10M</td>
<td>1.0%</td>
<td>2.1%</td>
</tr>
<tr>
<td>All Industrial: R10M - R20M</td>
<td>2.4%</td>
<td>4.3%</td>
</tr>
<tr>
<td>All Industrial: R20M - R30M</td>
<td>3.3%</td>
<td>4.0%</td>
</tr>
<tr>
<td>All Industrial: R30M - R50M</td>
<td>9.7%</td>
<td>11.3%</td>
</tr>
<tr>
<td>All Industrial: &gt; R50M</td>
<td>83.6%</td>
<td>46.7%</td>
</tr>
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