how can we help you?

3 June 2013

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PROPERTY BAROMETER – RESIDENTIAL PROPERTY MONTHLY

May house price growth shows further acceleration. But for how long in a weak economic environment?

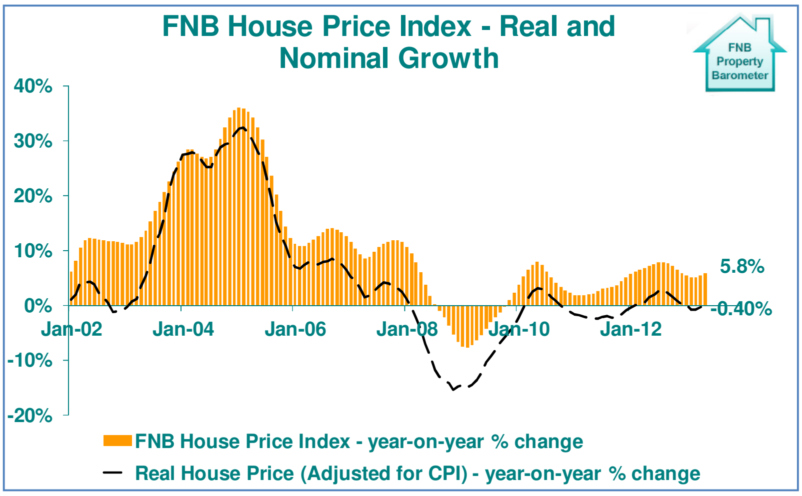
SUMMARY

The renewed acceleration in house price growth, which resumed early in 2013 after a lull late in 2012, continued in the May version of the FNB House Price Index.

The average house price for May showed year-on-year growth of 5.8%, up from April's revised 5.4%.

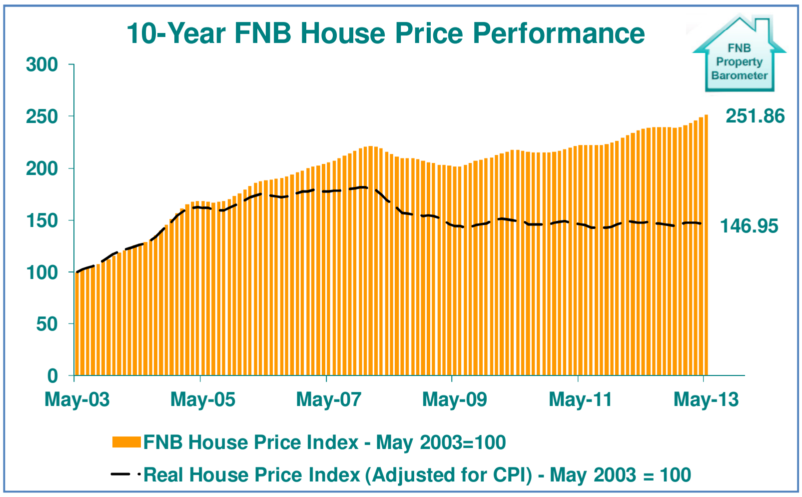
The average value of homes transacted in the FNB House Price Index was R885,773.

In real terms (adjusting house prices for general inflation in the economy using the CPI), as at April we were still seeing very slight year-on-year decline to the tune of -0.4%, with consumer price inflation at 5.86% year-on-year in that month still slightly higher than house price inflation.



Evaluating longer term performance of the FNB House Price Index, in real terms the index is -19.2% down on last decade's real price peak reached in November 2007, while in nominal terms it is a mere 14.9% higher.

However compared to May 2003, 10 years ago, the index is up 49.8% in real terms and 151.9% in nominal terms, suggesting that the price effects of last decade's residential demand boom have far from worn off .despite a significant downward real correction since late-2007.

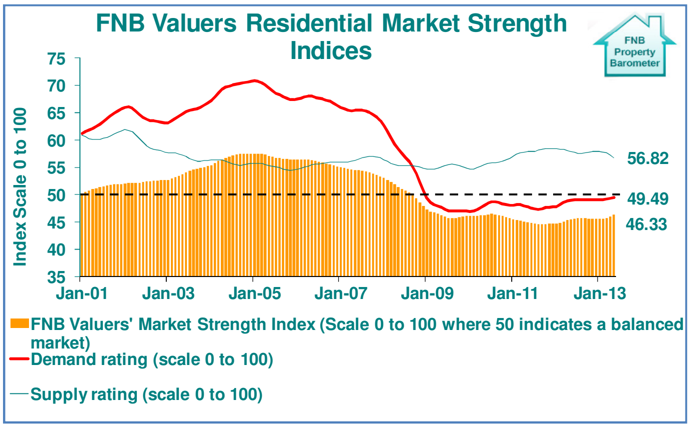


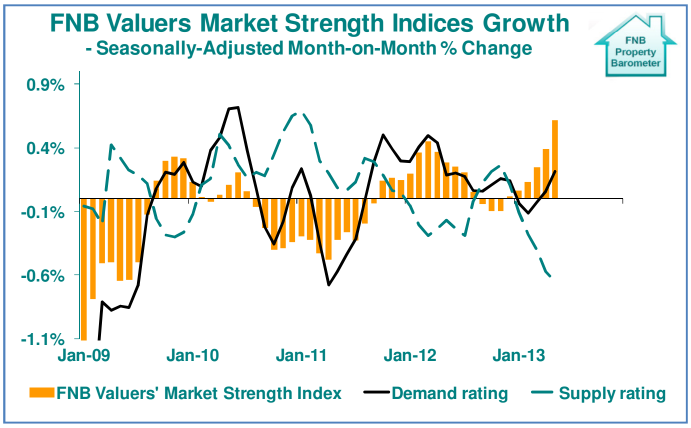
FNB'S VALUERS PERCEIVE AN IMPROVED BALANCE BETWEEN SUPPLY AND DEMAND

Turning to the FNB Valuers'Market Strength Index, FNB's Valuers have indicated that recent relative market strength has been the result of the combination of positive residential demand growth as well as a little more constrained supply of residential stock on the market.

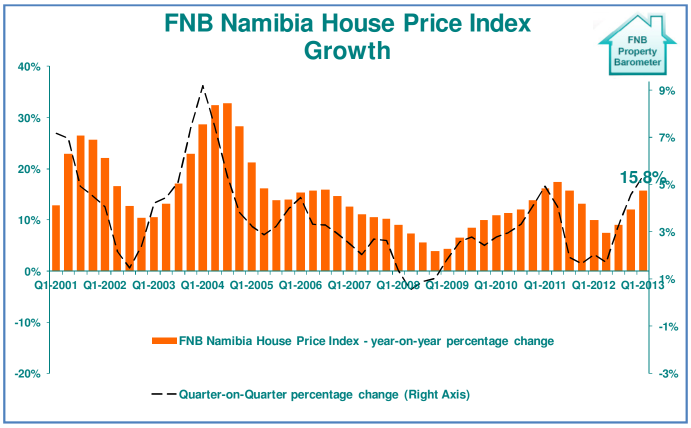
Since early-2012, the FNB Valuers'Market Strength Rating Index has shown gradual positive year-on-year growth after a 2011 decline. It remains below the crucial level of 50, at 46.33, implying that the residential demand rating at 49.5 is still weaker than the 56.8 Residential Supply Rating, arguably explaining why we have not yet seen strong house price growth in real terms.

On a month-on-month seasonally adjusted basis, however, we have seen the valuers perceiving positive month-on-month growth in demand and month-on-month declines in supply in recent months, narrowing the gap between supply and demand.





IN NAMIBIA, THE 2ND LARGEST RAND AREA ECONOMY, THINGS HAVE BEEN EVEN BETTER OF LATE



In the 2nd largest economy within the Common (Rand) Monetary Area, i.e. Namibia, our FNB Namibia Average House Price shows a slightly better situation than in South Africa. Namibia has experienced a stronger economic growth rate than South Africa in recent times. In addition, its major residential market, Windhoek, experiences significant vacant land constraints and thus more constrained supply, it would appear, than SA's cities.

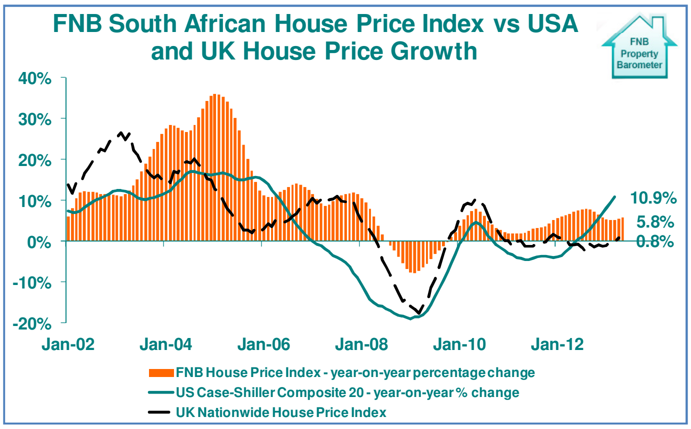
The apparent result is that, while the shape and direction of Namibia's cycles don't look too dissimilar to SA, the magnitude of its house price growth has been better of late, with its 1st quarter average house price growth estimated at 15.8%, impressive compared to South Africa's lower 5.2% as at the 1st quarter of this year.

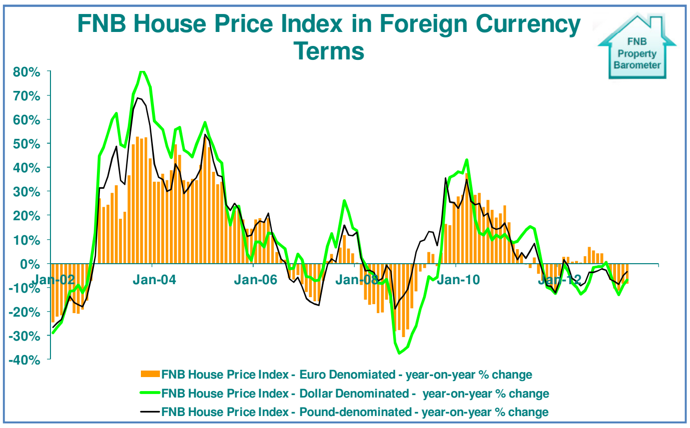
THE LOCAL HOUSING MARKET IN FOREIGN CURRENCY TERMS

The broadly improved period of domestic house price growth since late-2011/early-2012 is not totally out of kilter with economic and housing market developments in the world's largest economy through last year and early-2013, where March saw the US Case-Shiller House Price Index reaching growth of 10.9% year-on-year, after a steady acceleration from a state of negative growth back in 2011.

But there are recent some ominous signs emerging for the local residential market emanating from a somewhat "pressured" domestic economy. In foreign currency-denominated terms, the FNB House Price Index reflects a very different picture, i.e. a domestic residential market dropping in value, as a result of a steady recent deterioration in investor sentiment which has seen a major weakening in the Rand.

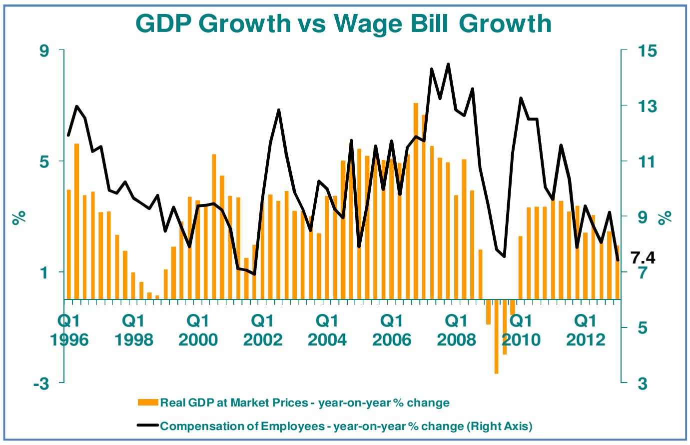
In dollar terms, the May FNB House Price Index declined year-on-year by -6.9%, in Euro terms by -8.4%, and by -3.4% in UK Pound terms. South African property has thus recently become significantly cheaper for aspirant foreign buyers. Will this attract a higher number of foreign buyers? This remains to be seen, but this is not expected, as the cheaper domestic property is a result of a deterioration in investor sentiment it would seem.

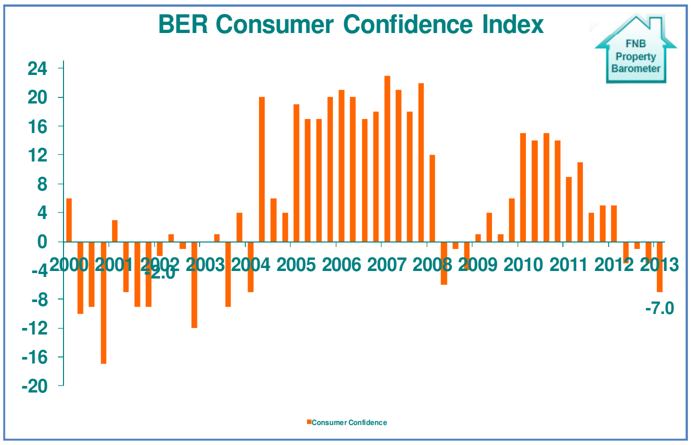




OUTLOOK - DESPITE RECENT IMPROVEMENT, HOUSING OUTLOOK MAY STILL BE A MEDIOCRE ONE WITH MAY DATA RELEASES POINTING TO AN ECONOMY UNDER SIGNIFICANT PRESSURE

The key data release in May which has a bearing on residential buyer purchasing power growth was 1st quarter StatsSA GDP (gross domestic product) data. This revealed a very disappointing quarter-on-quarter annualized real GDP growth rate of 0.9%. This in turn had a negative impact on the estimated total employee remuneration (wage bill) growth, which slowed in nominal terms to 7.4%. This is the lowest nominal wage bill growth rate since the final quarter of 2001, and is now well down on the post-2008/9-recession "Relief Recovery" peak of 13.3% reached in early-2010. This suggests still-further slowdown on disposable income growth early in 2013, which probably largely explains the recent steady deterioration in Consumer Confidence.





The other key event that took place in May, and which relates strongly to residential property demand, was the Reserve Bank (SARB) decision to leave interest rates unchanged with its Repo rate at 5% and prime rate at 8.5%., thus offering no additional demand stimulus since the 3rd quarter of last year. The combined impact of no interest rate cutting as of late and slowing wage bill growth could have negative implications in terms of growth in residential demand in the near term, with many economic agencies recently revising economic growth forecasts downward, and growth below 2% looking an increasing possibility for 2013.

Certainly the SARB Governor emphasized that growth forecasts risks were very much to the "downside", and CPI inflation forecast risks to the "upside", with bad labour relations and high wage demands posing threats to both growth and inflation. The current level of interest rates set by the SARB is at multi-decade lows, and indeed the stability of interest rates at these low levels has helped to gradually strengthen residential demand.

But it is questionable whether this residential demand strengthening can continue at a time of such economic weakness, and where we have already seen a steady slowing in growth in the area of real consumer demand as a result.

Granted, a still-slow rate of growth in residential buildings completed keeps supply growing at a slow pace. But a weak economy and resultant weakened disposable income growth leads to the ongoing expectation that house price growth will continue to remain largely in single-digit territory in the near term, due to potential pressure on demand, not far outpacing consumer price inflation of near to 6%.

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Notes:

Note on The FNB Average House Price Index: *Although also working on the average price principle (as opposed to median or repeat sales), the FNB House Price Index differs from a simple average house price index in that it could probably be termed a "fixed weight" average house price index.*

One of the practical problems we have found with house price indices is that relative short term activity shifts up and down the price ladder can lead to an average or median price index rising or declining where there was not necessarily "genuine" capital growth on homes. For example, if "suburban segment volumes remain unchanged from one month to the next, but former Black Township (the cheapest areas on average) transaction volumes hypothetically double, the overall national average price could conceivably decline due to this relative activity shift.

This challenge of activity shifts between segments is faced by all constructors of house price indices. In an attempt to reduce this effect, we decided to fix the weightings of the FNB House Price Index's sub-segments in the overall national index. This, at best, can only be a partial solution, as activity shifts can still take place between smaller segments within the sub-segments. However, it does improve the situation.

With our 2013 re-weighting exercise, we have begun to segment not only according to room number, but also to segment according to building size within the normal segments by room number, in order to further reduce the impact of activity shifts on average price estimates.

The FNB House Price Index's main segments are now as follows:

- *The weightings of the sub-segments are determined by their relative transaction volumes over the past 5 years, and will now change very slowly over time by applying a 5-year moving average to each new price data point. The sub-segments are:*

- *Sectional Title:*
    - *Less than 2 bedroom – Large*
    - *Less than 2 bedroom – Medium*
    - *Less than 2 bedroom – Small*

    - *2 Bedroom – Large*
    - *2 bedroom – Medium*
    - *2 bedroom – Small*

    - *3 Bedroom and More - Large*
    - *3 Bedroom and More - Medium*
    - *3 Bedroom and More - Small*

- *Full Title:*
    - *2 Bedrooms and Less - Large*
    - *2 Bedrooms and Less - Medium*
    - *2 Bedrooms and Less - Small*

- *3 Bedroom - Large*
- *3 Bedroom - Medium*
- *3 Bedroom - Small*

- *4 Bedrooms and More - Large*
- *4 Bedrooms and More - Medium*
- *4 Bedrooms and More – Small*

The size cut-offs for "small", medium" and "large" differ per room number sub-segment. "Large" would refer to the largest one-third of homes within a particular room number segment over the past 5 year period, "Medium" to the middle one-third, and "Small" to the smallest one-third of homes within that segment.

- *The Index is constructed using transaction price data from homes financed by FNB.*
- *The minimum size cut-off for full title stands is 200 square metres, and the maximum size is 4000 square metres*
- *The maximum price cut-off is R10m, and the lower price cut-off is R20,000 (largely to eliminate major outliers and glaring inputting errors).*
- *The index is very lightly smoothed using a Hodrick-Prescott smoothing function with a Lambda of 5.*

Note on the FNB Valuers' Market Strength Index: **When an FNB valuer values a property, he/she is required to provide a rating of demand as well as supply for property in the specific area. The demand and supply rating categories are a simple "good (100)", "average (50)", and "weak (0)". From all of these ratings we compile an aggregate demand and an aggregate supply rating, which are expressed on a scale of 0 to 100. After aggregating the individual demand and supply ratings, we subtract the aggregate supply rating from the demand rating, add 100 to the difference, and divide by 2, so that the FNB Valuers' Residential Market Strength Index is also depicted on a scale of 0 to 100 with 50 being the point where supply and demand are equal.*