Property Barometer.

June 2019

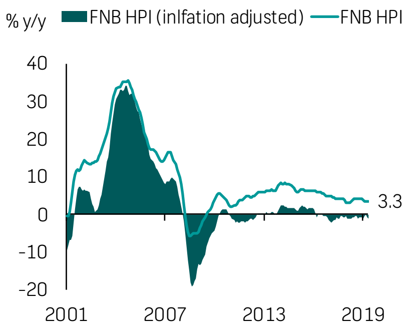
+3.3% y/y FNB HPI

+0.4% m/m FNB HPI

49.06 FNB Valuers' Market Strength Index

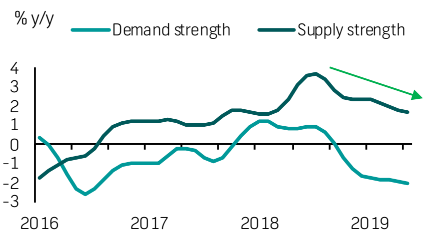
House prices moved sideways in May, growth skewed towards the lower end

Figure 1: FNB HPI at 3.3% y/y in May



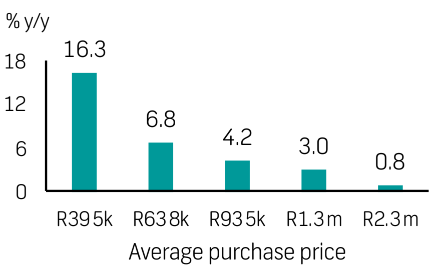
Source: FNB

Figure 2: Supply-Demand trends



Source: FNB

Figure 3: HPI by value band: 1Q19



Source: FNB

Downward adjustment continues

The FNB HPI moved sideways in May, recording 3.3% y/y from 3.4% y/y in April. This takes the year-to-date nominal house price growth to 3.4% y/y, marginally better than the 3.3% recorded in the same period in 2018. In real terms, average house prices continued declining, which we read as a continuation of a downward adjustment in line with subdued economic activity and lower disposable income levels. The FNB Market Strength Index continues to gauge the market as moderately oversupplied, particularly in the middle to upper income areas. However, the pace at which properties are entering the market has been adjusting to lower demand in recent months. By property type, the index gauges sectional title properties to be oversupplied (more on this below), while demand and supply of freestanding properties to be more or less evenly balanced.

Growth is skewed towards the lower end

Using data from the Deeds Office, we segment all towns into five value bands (deciles) based on their average home values. These bands range from Low income areas (which corresponds to the bottom 20%) to the Luxury area value band (which corresponds to the top 20%).

The 1Q19 home transactions data shows that growth in house prices is skewed towards lower value bands, while higher value bands are under relative pressure. The Low-income area band (average purchase price R395 900) grew by an average 16.3% y/y, while the Lower-middle segment (average purchase price R638 200) averaged 6.8%. The Middle segment, which corresponds to homes in the middle 20% of the price spectrum (average purchase price R935 000), registered 4.2% in 1Q19. On the higher end of the spectrum, Upper-income value (average purchase piece R1.3 million) and Luxury value bands (average purchase price R2.3 million) registered 3.0% and 0.8% y/y respectively.

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These are largely reflective of supply-demand imbalances across price segments—excess demand in the lower end and excess supply in the higher end. To be sure, the Estate Agents survey estimated that virtually all properties exceeding the value of R3.6m transacted at less than the initial asking price in 1Q19. This implies buyers have a disproportionately high negotiating power in those segments.

Sentiment sensitive segments are recovering

While the uncertainty associated with elections has somewhat lifted, paving a way for improved sentiment, it may take a while longer before that filters through to real economic activity. For the residential property market, excess supply in the higher end segments must clear before we see an overall house price acceleration. Pent up demand will likely green-shoot in the more "sentiment sensitive" sub-segments such as holiday home buying and investment property purchases. In fact, recovery in these segments may have already begun—the proportion of these transactions ticked up marginally to a combined 9.6% in 1Q19 from a trough of 9.4% in 4Q18, as shown by the Estate Agents survey results. Figure 4 shows the slight recovery in holiday home buying has in turn translated into an acceleration in holiday home price as buyers take advantage of relatively attractive prices.

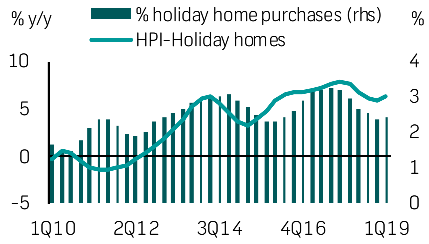
Supply of new flats soaring

The first three months of the year saw a solid increase in the volume of private sector financed residential buildings completions. While the increased activity was seen across all sub-components, supply (i.e. completions) of flats and townhouses was exceptionally strong, up 90.6% versus the corresponding period last year. Against this backdrop, flat vacancies are estimated to be on the rise, which in turn has kept a lid on rental inflation. The rest of the segments, namely houses smaller than 80m2 and houses larger than 80m2 recovered by 5.2% and 17.9% respectively in the first three months of 2019 versus 2018. Interestingly, the proportion of new flats and townhouses (as % of total new housing units) is trending significantly above its long-term average of around 30%. Year-to-date, these units have accounted for approximately 60% of new stock, up from 29% in 2015 and 13% in 2000. This could be explained by the increasingly urbanising population, rising densification in the metros, as well as the changing consumer preferences (e.g. buyers are now more security conscious in their buying decisions).

Outlook

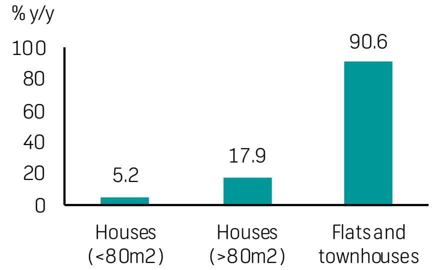
On the positive side, improvement in sentiment combined with an interest rate cut, which we expect in the next MPC meeting in July, will somewhat support demand for mortgages and thus purchasing activity, albeit with a time lag. These will be countered by rising household income pressures, the lack of willingness to commit to substantial financial obligations by consumers, as well as supply-side factors such as lenders' lending standards. In all, we expect house prices to average around the 3.5% mark, versus our inflation projection of 4.6% this year.

Figure 4: Holiday home prices vs purchasing activity



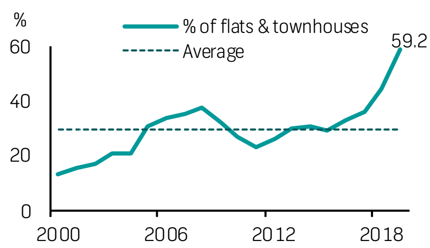
Source: FNB

Figure 5: Units completed: Year-to-date



Stats SA, FNB

Figure 6: New stock: Proportion flats and townhouses



Source: Stats SA, FNB

Monthly FNB House Price Index (%y/y)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2001		-1.7	-0.7	-0.4	-0.5	0.7	3.0	5.9	8.6	10.6	11.6	11.8
2002	11.6	12.0	12.8	13.8	14.2	14.0	13.6	13.1	13.2	13.5	13.8	13.8
2003	14.0	14.5	15.3	16.2	17.1	18.2	19.3	20.3	21.4	22.9	24.7	27.0
2004	29.4	31.3	32.4	33.2	33.7	33.9	34.5	35.1	35.3	35.2	35.3	35.4
2005	34.8	33.8	32.9	31.8	30.7	29.7	28.8	27.9	26.9	25.7	23.9	21.7
2006	19.9	18.5	17.6	17.3	17.3	17.2	16.9	16.5	15.8	15.1	14.4	14.0
2007	14.0	14.3	14.9	15.7	16.3	16.6	16.3	15.5	14.5	13.2	12.0	11.0
2008	9.7	8.0	5.5	2.5	-0.4	-2.9	-4.7	-5.6	-5.8	-5.6	-5.1	-5.1
2009	-5.0	-5.0	-4.5	-3.8	-2.8	-1.8	-0.7	0.0	0.5	0.9	1.2	2.0
2010	3.0	3.9	4.6	5.2	5.6	5.5	5.0	4.7	4.5	4.1	3.7	3.1
2011	2.4	2.1	2.0	2.2	2.5	2.8	3.3	3.6	3.8	3.9	4.1	4.4
2012	4.7	4.8	4.8	4.7	4.6	4.7	4.9	5.2	5.6	5.7	5.8	5.8
2013	5.9	6.0	6.1	6.1	6.1	6.3	6.5	6.4	6.3	6.5	7.0	7.7
2014	8.2	8.3	8.2	8.3	8.4	8.3	8.0	7.8	7.6	7.2	6.8	6.2
2015	5.8	5.9	6.3	6.5	6.6	6.4	6.3	6.2	6.1	6.2	6.3	6.3
2016	6.3	6.2	6.1	6.0	5.9	5.8	5.7	5.6	5.4	5.1	4.8	4.8
2017	4.9	4.9	4.7	4.4	4.2	4.1	4.1	4.2	4.2	4.2	4.2	3.9
2018	3.3	3.1	3.3	3.6	3.9	4.1	4.1	4.0	4.1	4.3	4.4	4.3
2019	3.8	3.4	3.5	3.4	3.3							

Forecast

FNB SA Economic Forecast

Economic Indicator	2016	2017	2018	2019f	2020f	2021f
Household consumption expenditure %y/y	0.6	2.1	1.8	1.5	1.6	1.8
Government consumption expenditure %y/y	2.2	0.2	1.9	0.4	1.1	1.2
Gross fixed capital formation %y/y	-3.5	1	-1.4	0.2	0.5	1.1
Real GDP %y/y	0.4	1.4	0.7	0.9	1.2	1.2
Total exports %y/y	0.4	-0.7	2.6	2.2	1.4	1.8
Total imports %y/y	-3.9	1	3.3	2.1	2.2	2.4
Current account (% of GDP)	-2.8	-2.5	-3.5	-3.8	-3.7	-3.5
CPI (average) %y/y	6.3	5.3	4.6	4.7	5	5.2
CPI (year end) %y/y	6.7	4.7	4.5	5.1	4.9	4.9
Repo rate (year end) %p.a.	7	6.75	6.75	6.5	6.5	6.5
Prime (year end) %p.a.	10.5	10.25	10.25	10.25	10.25	10.25
USD/ZAR (average)	14.7	13.3	13.3	14.1	14.8	15.6

Source: FNB

ADDENDUM - NOTES:
Note on The FNB House Price Index:

The FNB Repeat Sales House Price Index has been one of our repertoire of national house price indices for some years, and is based on the well-known Case-Shiller methodology which is used to compile the Standard & Poor's Case-Shiller Home Price Indices in the United States.

This "repeat sales approach" is based on measuring the rate of change in the prices of individual houses between 2 points in time, based on when the individual homes are transacted. This means that each house price in any month's sample is compared with its own previous transaction value. The various price inflation rates of individual homes are then utilized to compile the average price inflation rate of the index over time.

The index is compiled from FNB's own valuations database, thus based on the residential properties financed by FNB over the past 18 years.

We apply certain "filters" and cut-offs to eliminate "outliers" in the data. They main ones are as follows:

- The maximum price cut-off is R15m, and the lower price cut-off is R20 000.
- The top 5% of repeat sales price growth rates, and the bottom 5% of growth rates are excluded fromthe data set.
- Repeat transactions that took place longer than 10 years after the previous transaction on the same home are excluded, as are repeat transactions that took place less than 6 months after the previoustransaction on the same home.
- 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.