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MARKET ANALYTICS AND  
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## PROPERTY BAROMETER

### FNB Property Monthly

*The FNB House Price Index's year-on-year inflation rate speeds up, perhaps reflecting a slightly better economy, and a strong Western Cape*

In May 2016, the FNB House Price Index recorded a 7.4% year-on-year rate of increase, which is slightly faster than the 7.0% revised rate of the prior month.

Given CPI (Consumer Price Index) inflation of 6.2% in April, in real terms average house price inflation was a modest 0.7% year-on-year in that month, reflecting a still-well balanced market.

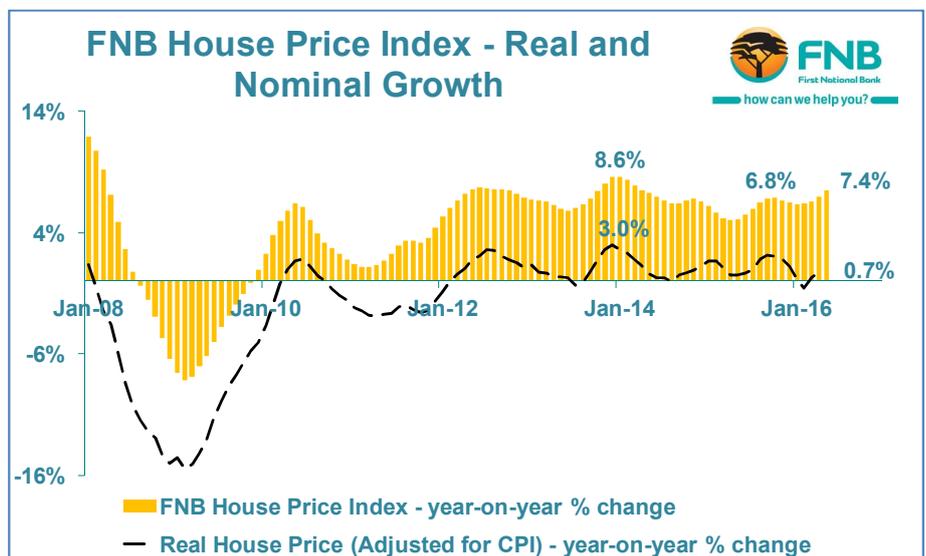
Higher nominal house price inflation may be partly the lagged effect of a shift to a higher economy-wide inflation environment since a year ago. However, it may also reflect a slightly better economic environment in the 2<sup>nd</sup> quarter of 2016, after a dismal start to the year in the 1<sup>st</sup> quarter. Furthermore, we believe that the national house price growth average currently receives strong support from the Western Cape region, which has bucked the slowing trend recently observed in other provinces to record double-digit house price growth early in 2016.

#### MAY FNB HOUSE PRICE INDEX FINDINGS

##### MAY AVERAGE HOUSE PRICE GROWTH

The FNB House Price Index for May 2016 rose by 7.4% year-on-year. This is slightly faster than the revised 7.0% rate recorded for April, implying an acceleration in nominal house price growth for the past 4 months using the latest revised data.

In real terms, when adjusting for CPI (Consumer Price Index) inflation, however, the rate of house price growth remains not too far from the zero level, having recorded 0.7% real year-on-year growth in April, slightly up from 0.3% in the prior month.



The return to slightly positive real growth in recent months was the result not only of rising average house price growth, but also due to some receding in CPI (Consumer Price Index) inflation, from 7% year-on-year in February to 6.2% by April (May CPI data not yet available).

Just above zero percent real house price inflation would continue to suggest a market still very well balanced between supply and demand. While demand has not been spectacular since the 2008/9 Recession, supply constraints have been reported widely, and building levels of new homes have remained muted, contributing greatly to the market balance.

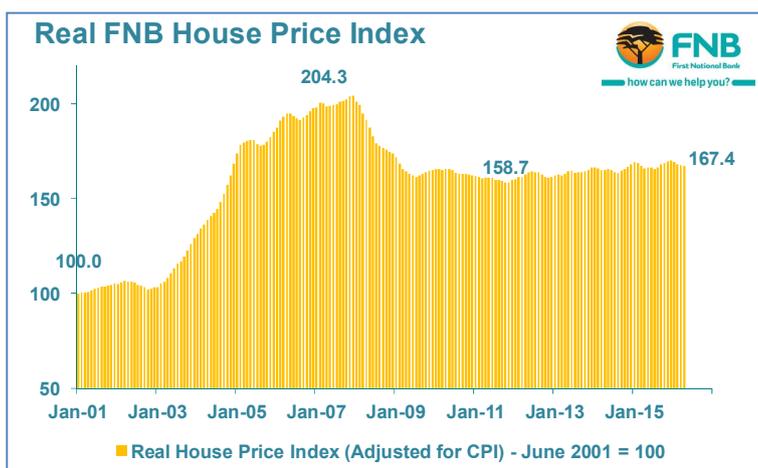
The average price of homes transacted in April was R1,075,033.

### REAL HOUSE PRICE LEVELS

Examining the longer term real house price trends (house prices adjusted for CPI inflation), we see that the level as at April 2016 was +5.3% up on the October 2011 post-recession low.

However, the average real house price level remains -18.2% below the all time high reached in December 2007 at the back end of the residential boom period.

Looking back further though, the average real price currently remains 67.4% above the January 2001 level, just over 15 years ago, and a time back just before boom-time price inflation started to accelerate rapidly. We therefore still regard current real price levels as very high.



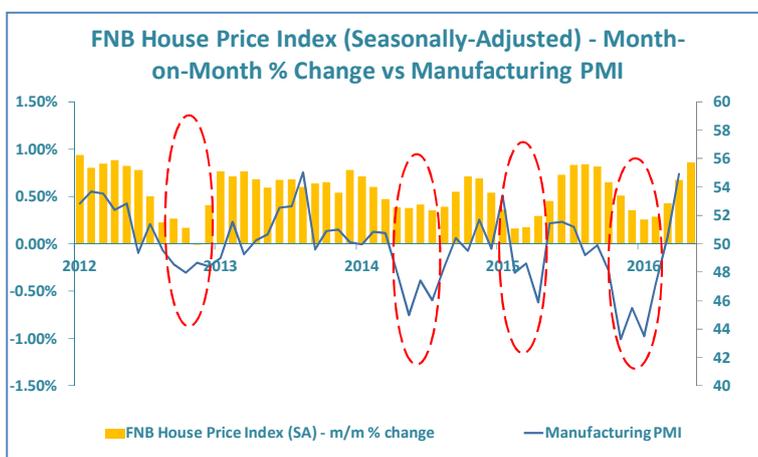
In nominal terms, when not adjusting for CPI inflation, the average house price in May 2016 was 298.8% above the January 2001 level.

### WHAT MAY BE THE KEY DRIVERS OF THE RECENT ACCELERATION IN AVERAGE HOUSE PRICE GROWTH

There are 3 possible key drivers of this perhaps surprising mild acceleration in average house price growth, at a time when interest rates have been rising.

Firstly, it is possible that some of this rise is the lagged impact of a higher general inflation environment which has set in in South Africa of late. After a low of 3.9% year-on-year in February 2015, CPI inflation gradually made its way higher through much of last year, to reach 7% in February 2016. It is possible that higher house price inflation is in part reflective of a higher general inflation environment.

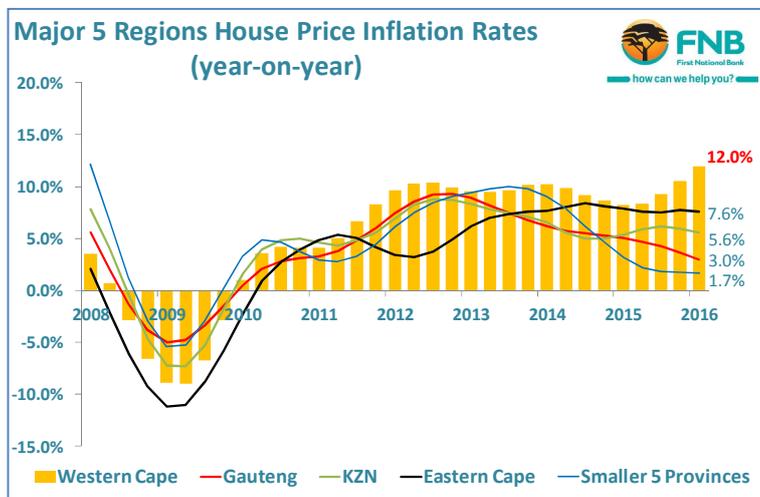
Secondly, however, we do believe that the acceleration may also be due to a slightly better economic environment setting in during the 2<sup>nd</sup> quarter of 2016, after a dismal starting quarter of the year. Viewing FNB House Price Index growth on a month-on-month seasonally adjusted basis, we see that in recent years the noticeable dips in the month-on-month rate of change in the House Price Index more-or-less co-incident with equally noticeable dips in the Manufacturing Purchasing Managers Index (PMI) – one of the key up to date indicators of short term economic movements).



Recently, however, in the past 2 months' data (March and April) we saw the PMI shooting up back to above the crucial 50 level, suggesting some possible mild economic improvement. Such improvement may also be reflected in the rise in month-on-month house price growth.

Thirdly, however, we believe that a key contributor in holding up the National House Price Index growth rate is the strong recent performance of the Western Cape region's housing market. A lot of positive sentiment exists in this region, the country's 2<sup>nd</sup> largest economic and residential property region after Gauteng Province, and along with a significant land constraint this has boosted the province's house price growth into double-digits.

The FNB Western Cape House Price Index recorded 12% year-on-year growth during the 1<sup>st</sup> quarter (we only produce the provincial indices on a quarterly basis)



By comparison, the other major regions were significantly slower. Eastern Cape Province recorded 7.6% year-on-year house price inflation in the 1<sup>st</sup> quarter, KZN 5.6%, Gauteng, the country's largest region, rose 3%, and the Smaller 5 Provinces a mere 1.7%.

It would, therefore, appear to be very much a Western Cape story in recent times.



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## Monthly FNB House Price Index (Jan 2001 = 100)

Date	Index	y/y % change	Date	Index	y/y % change	Date	Index	y/y % change	Date	Index	y/y % change
Jan-01	100.0		Jan-05	209.7	36.1%	Jan-09	272.8	-7.6%	Jan-13	317.88	6.7%
Feb-01	100.7		Feb-05	215.4	36.3%	Feb-09	270.7	-8.2%	Feb-13	321.34	6.6%
Mar-01	101.4		Mar-05	219.6	35.6%	Mar-09	269.5	-7.9%	Mar-13	325.00	6.5%
Apr-01	102.4		Apr-05	221.7	34.3%	Apr-09	268.6	-7.1%	Apr-13	327.78	6.3%
May-01	103.6		May-05	222.0	32.5%	May-09	267.5	-6.2%	May-13	329.41	5.9%
Jun-01	104.7		Jun-05	221.7	30.4%	Jun-09	267.8	-5.1%	Jun-13	330.66	5.8%
Jul-01	105.3		Jul-05	221.1	27.9%	Jul-09	269.2	-3.8%	Jul-13	331.90	6.0%
Aug-01	105.6	10.0%	Aug-05	221.3	25.0%	Aug-09	271.4	-2.9%	Aug-13	333.38	6.3%
Sep-01	106.0	9.2%	Sep-05	222.3	21.9%	Sep-09	273.8	-2.0%	Sep-13	335.14	6.8%
Oct-01	106.5	8.9%	Oct-05	224.5	19.1%	Oct-09	275.5	-1.1%	Oct-13	337.06	7.4%
Nov-01	107.3	9.0%	Nov-05	227.3	16.2%	Nov-09	276.6	-0.2%	Nov-13	339.17	8.1%
Dec-01	108.6	9.5%	Dec-05	231.0	13.9%	Dec-09	277.6	0.9%	Dec-13	342.06	8.6%
Jan-02	110.2	10.2%	Jan-06	235.3	12.2%	Jan-10	278.9	2.3%	Jan-14	344.98	8.5%
Feb-02	112.2	11.4%	Feb-06	240.0	11.4%	Feb-10	281.0	3.8%	Feb-14	348.07	8.3%
Mar-02	114.1	12.6%	Mar-06	244.2	11.2%	Mar-10	282.8	4.9%	Mar-14	350.63	7.9%
Apr-02	115.6	12.9%	Apr-06	247.4	11.6%	Apr-10	284.0	5.8%	Apr-14	352.28	7.5%
May-02	116.5	12.4%	May-06	248.9	12.1%	May-10	284.5	6.4%	May-14	353.20	7.2%
Jun-02	116.8	11.6%	Jun-06	249.3	12.5%	Jun-10	284.0	6.1%	Jun-14	353.54	6.9%
Jul-02	117.0	11.2%	Jul-06	249.9	13.0%	Jul-10	282.7	5.0%	Jul-14	353.81	6.6%
Aug-02	117.2	10.9%	Aug-06	251.1	13.5%	Aug-10	282.1	3.9%	Aug-14	354.62	6.4%
Sep-02	117.4	10.7%	Sep-06	252.9	13.8%	Sep-10	282.4	3.2%	Sep-14	356.61	6.4%
Oct-02	117.9	10.7%	Oct-06	255.1	13.6%	Oct-10	282.9	2.7%	Oct-14	359.32	6.6%
Nov-02	118.7	10.6%	Nov-06	257.7	13.4%	Nov-10	282.8	2.2%	Nov-14	362.14	6.8%
Dec-02	119.8	10.3%	Dec-06	260.8	12.9%	Dec-10	282.6	1.8%	Dec-14	364.47	6.6%
Jan-03	121.1	9.9%	Jan-07	263.9	12.1%	Jan-11	282.8	1.4%	Jan-15	366.28	6.2%
Feb-03	123.2	9.8%	Feb-07	266.3	11.0%	Feb-11	284.2	1.2%	Feb-15	367.56	5.6%
Mar-03	125.7	10.2%	Mar-07	268.1	9.8%	Mar-11	286.1	1.2%	Mar-15	368.75	5.2%
Apr-03	128.5	11.1%	Apr-07	269.7	9.0%	Apr-11	287.8	1.3%	Apr-15	369.93	5.0%
May-03	131.1	12.5%	May-07	271.9	9.2%	May-11	289.3	1.7%	May-15	371.21	5.1%
Jun-03	133.6	14.4%	Jun-07	274.8	10.2%	Jun-11	290.3	2.2%	Jun-15	372.78	5.4%
Jul-03	136.3	16.5%	Jul-07	277.7	11.1%	Jul-11	291.0	3.0%	Jul-15	374.87	6.0%
Aug-03	138.6	18.3%	Aug-07	280.6	11.8%	Aug-11	291.5	3.3%	Aug-15	377.47	6.4%
Sep-03	140.9	20.0%	Sep-07	283.6	12.1%	Sep-11	291.7	3.3%	Sep-15	380.91	6.8%
Oct-03	143.6	21.8%	Oct-07	287.0	12.5%	Oct-11	291.9	3.2%	Oct-15	383.85	6.8%
Nov-03	146.8	23.6%	Nov-07	290.8	12.9%	Nov-11	292.9	3.6%	Nov-15	386.17	6.6%
Dec-03	150.4	25.5%	Dec-07	293.9	12.7%	Dec-11	294.9	4.4%	Dec-15	387.93	6.4%
Jan-04	154.1	27.2%	Jan-08	295.3	11.9%	Jan-12	297.8	5.3%	Jan-16	389.39	6.3%
Feb-04	158.1	28.3%	Feb-08	294.9	10.7%	Feb-12	301.3	6.0%	Feb-16	390.94	6.4%
Mar-04	161.9	28.8%	Mar-08	292.6	9.1%	Mar-12	305.1	6.6%	Mar-16	392.92	6.6%
Apr-04	165.1	28.5%	Apr-08	289.0	7.1%	Apr-12	308.5	7.2%	Apr-16	395.65	7.0%
May-04	167.6	27.9%	May-08	285.2	4.9%	May-12	311.0	7.5%	May-16	398.83	7.4%
Jun-04	169.9	27.2%	Jun-08	282.0	2.6%	Jun-12	312.6	7.7%			
Jul-04	172.8	26.8%	Jul-08	279.9	0.8%	Jul-12	313.2	7.6%			
Aug-04	177.0	27.7%	Aug-08	279.4	-0.4%	Aug-12	313.5	7.6%			
Sep-04	182.3	29.4%	Sep-08	279.3	-1.5%	Sep-12	313.8	7.6%			
Oct-04	188.5	31.3%	Oct-08	278.6	-2.9%	Oct-12	313.7	7.5%			
Nov-04	195.6	33.3%	Nov-08	277.1	-4.7%	Nov-12	313.9	7.2%			
Dec-04	202.9	34.9%	Dec-08	275.1	-6.4%	Dec-12	315.1	6.9%			

## ADDENDUM - 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 “Full Title 3 Bedroom volumes remain unchanged from one month to the next, but Sectional Title 1 Bedroom and Less (the cheapest segment 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.

#### **ADDENDUM - NOTES:**

**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.