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MARKET ANALYTICS AND
SCENARIO FORECASTING
UNIT

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PROPERTY BAROMETER

FNB House Price Index

The FNB House Price Index's growth is experiencing a mild "uptick", but we remain of the view that it will be a short-term phenomenon.

In October 2015, the FNB House Price Index inflation rate continued its mild uptick of recent months, following a prior gradual slowing rate dating back to early-2014.

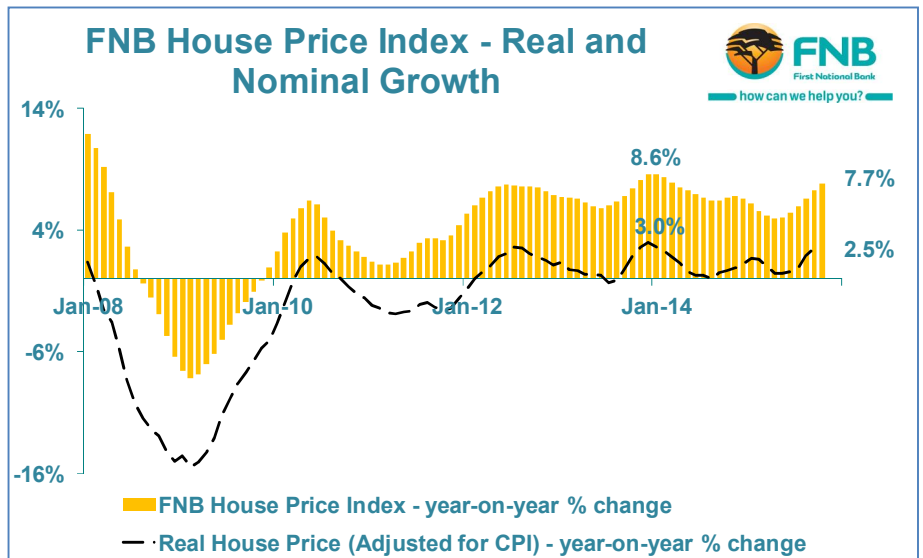
This may come as something of a surprise in what remains a very weak economy, but may be in part explained by indications of significant constraints in residential supply, which could mean that any slight fluctuation in residential demand could move residential price inflation quite easily.

OCTOBER FNB HOUSE PRICE INDEX FINDINGS

The FNB House Price Index for October 2015 rose by 7.7% year-on-year. This is up from a revised 7.2% for September, continuing the mild accelerating price growth trend that has emerged in recent months after a prior gradual slowing trend that started back in early-2014, after house price growth had hit a multi-year high of 8.6% at the end of 2013.

In real terms, when adjusting for CPI (Consumer Price Index) inflation, the rate of house price growth accelerated to 2.5% year-on-year in September (October CPI data not yet available), with CPI inflation of only 4.6% in that month. This September Real House Price Inflation rate was also up on the prior month's revised 1.9%.

The average price of homes transacted in October was R1,043,592



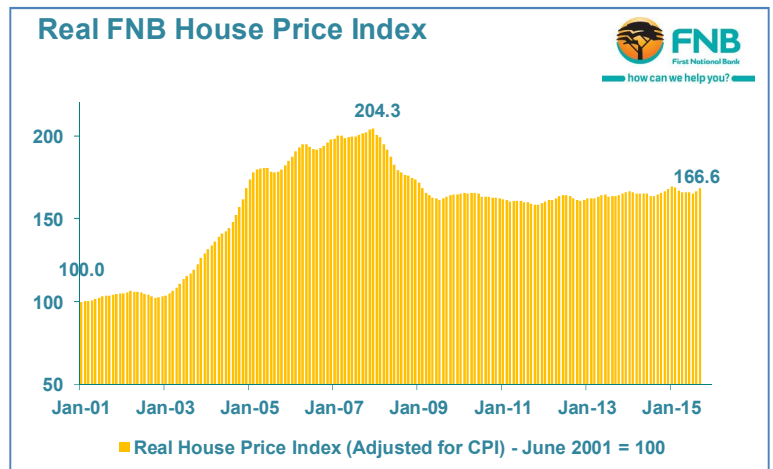
REAL HOUSE PRICE LEVELS

Examining the longer term real house price trend (house prices adjusted for CPI inflation), we see that despite some rise in recent years, (+6.3% since the October 2011 low) the average real house price level remains -17.5% below the all time high reached in December 2007 at the back end of the residential boom period.

Looking back longer though, the average real price remains 64.6% above the July 2000 level, the date when the index started, and a time back just before boom-time price inflation started to accelerate rapidly.

Real house price levels thus remain at “boom time” levels in our view, despite having lost some ground since the end of 2007.

In nominal terms, when not adjusting for CPI inflation, the average house price in October 2015 was 289.2% above the July 2000 level.



WHAT FNB'S VALUERS AND THE ECONOMY SAY

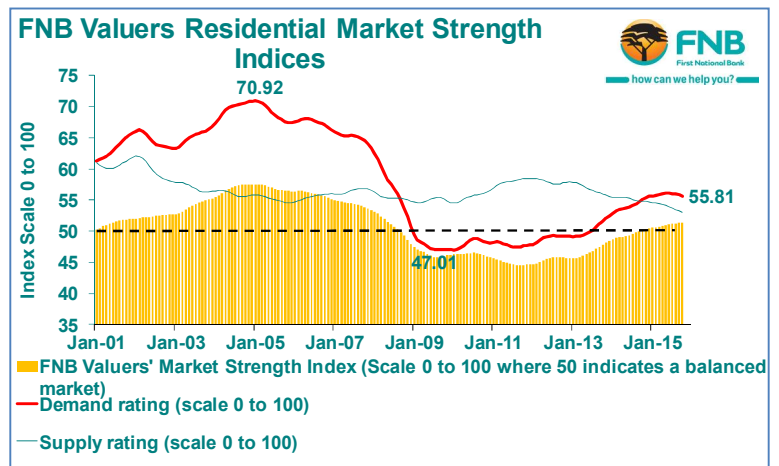
According to FNB's valuers as a group, the residential market remains very well balanced, with demand still stronger than supply, so it should not be too surprising to see continued real house price growth from this point of view, despite our expectation that a weak economy should ultimately cause this market balance to deteriorate.

The valuers also appear to suggest that constrained supply is at the heart of sustaining positive real house price growth.

The level of the Residential Demand Rating (explanatory notes on Market Strength Index on page 14) remains relatively solid at 55.81 on a scale of 0 to 100 in October.

Simultaneously, the valuers as a group rate supply at a lower level of 53.06.

With the Supply Rating being lower than the Demand Rating, this translates into a Market Strength Index (MSI) above the crucial 50 level at a 51.3 reading for October. Above a 50 level in Market Strength implies demand still being stronger than supply in the eyes of FNB's valuers as a group.



Examining the MSI's year-on-year growth rates, we see slowing year-on-year growth in the Residential Demand Rating, but negative year-on-year growth in the Residential Supply Rating still translates into positive year-on-year increase in the overall MSI.

However, this does not appear to explain the recent acceleration in real house price growth, because the rate of increase in the Market Strength Index has been slowing of late.

Rather, what seems to be the case is that we may be seeing the lagged impact of a slight acceleration in the year-on-year rate of increase in the MSI back around the 2nd quarter of 2015, prior to the more recent renewed slowing. Back in the 2nd quarter, demand growth temporarily stopped slowing, and the MSI's growth rose slightly.

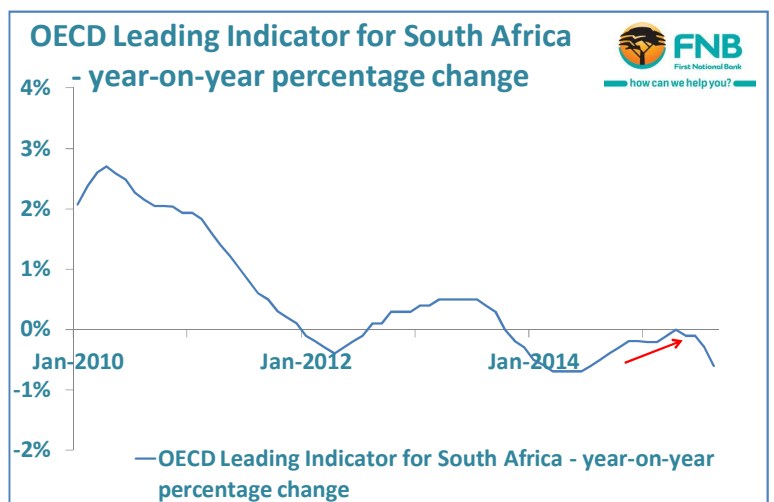
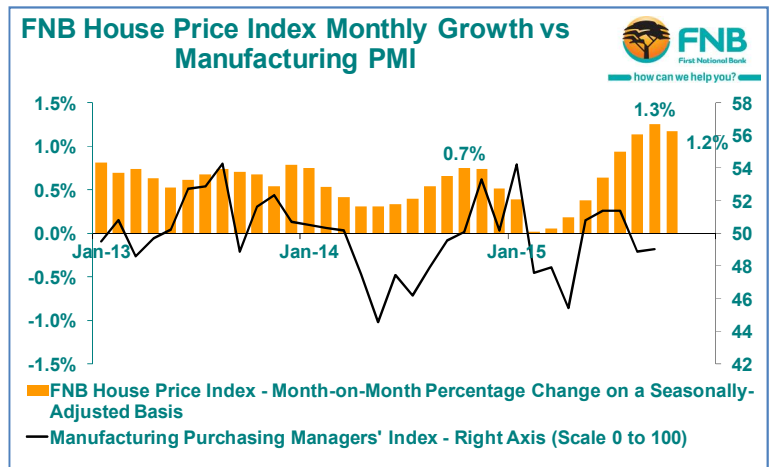
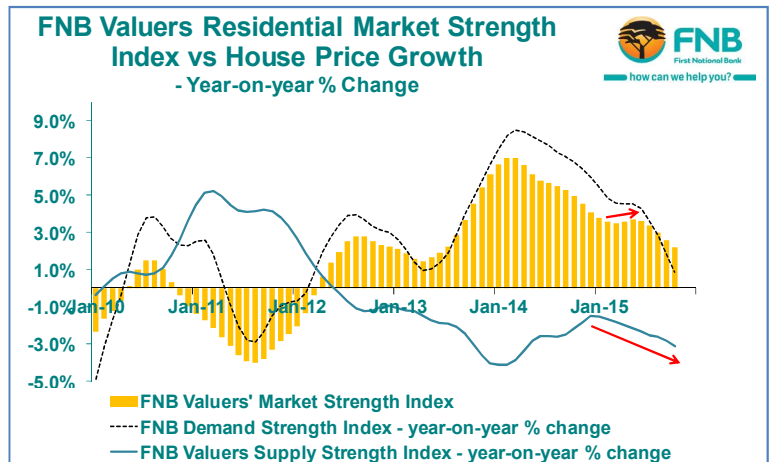
This theory is perhaps supported by examining the month-on-month percentage change (seasonally adjusted) in the FNB House Price Index. This rate often shows short term fluctuations that appear to co-incide with movements in certain key high frequency economic indicators, the all-important Manufacturing Purchasing Managers' Index (PMI) being a key one.

A brief surge in the PMI in the 2nd quarter back to above the 50 level(50 being the dividing line between expansion and contraction), was accompanied by a surge in month-on-month growth in house prices.

So, an apparently briefly better (though far from wonderful) economic period in the 2nd quarter, compared to the economic contraction in the 1st quarter of 2015, may have briefly turned the residential market slightly stronger, and the lagged (delayed) impact of that may be seen in the more recent rise in year-on-year house price inflation.

The Leading Indicator for South Africa (OECD version), too, showed a "less negative" year-on-year decline (reaching zero by April 2015) around the 2nd quarter of this year, before turning worse once more in the 3rd quarter.

So, there were some hints of a slightly less negative economic situation around the 2nd quarter, and this may have just been enough to cause a lagged acceleration in house price growth shortly thereafter. The subsequent deterioration in such indicators suggest, however, that it may not last long.



CONCLUSION

The further mild uptick in average house price growth in the October data may appear somewhat “out of place”, given many indications of a very weak and broadly stagnating economy.

Certainly, given the multi-year broad deterioration in South Africa’s economic growth, and the likelihood of this deteriorating trend continuing, we would not foresee an uptick in house price growth continuing for any great length of time.

Rather, we believe it could be driven by very short economic fluctuations. It could thus be the result of a slightly and temporarily better economy in the 2nd quarter of 2015, compared to the contraction of the 1st quarter, coupled with a still-constrained residential supply, feeding through into year-on-year house price growth with a lag.

However, in the 3rd quarter, we saw key up to date indicators such as the Manufacturing PMI, as well as the year-on-year rate of change in both the OECD and SARB Leading Indicators start to deteriorate once more, suggesting that this average house price inflation uptick will probably be short lived.

For the 1st 10 months of 2015, the average year-on-year house price inflation was 6%. Despite the recent months’ strengthening, this remains moderately slower than the 7.1% for 2014, and we expect it to remain so when 2015 is complete.

Monthly FNB House Price Index (Jan 2001 = 100)



how can we help you?

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	339.18	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	348.06	8.3%
Mar-02	114.1	12.6%	Mar-06	244.2	11.2%	Mar-10	282.8	4.9%	Mar-14	350.62	7.9%
Apr-02	115.6	12.9%	Apr-06	247.4	11.6%	Apr-10	284.0	5.8%	Apr-14	352.26	7.5%
May-02	116.5	12.4%	May-06	248.9	12.1%	May-10	284.5	6.4%	May-14	353.17	7.2%
Jun-02	116.8	11.6%	Jun-06	249.3	12.5%	Jun-10	284.0	6.1%	Jun-14	353.52	6.9%
Jul-02	117.0	11.2%	Jul-06	249.9	13.0%	Jul-10	282.7	5.0%	Jul-14	353.79	6.6%
Aug-02	117.2	10.9%	Aug-06	251.1	13.5%	Aug-10	282.1	3.9%	Aug-14	354.61	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	362.13	6.8%
Dec-02	119.8	10.3%	Dec-06	260.8	12.9%	Dec-10	282.6	1.8%	Dec-14	364.46	6.5%
Jan-03	121.1	9.9%	Jan-07	263.9	12.1%	Jan-11	282.8	1.4%	Jan-15	366.25	6.2%
Feb-03	123.2	9.8%	Feb-07	266.3	11.0%	Feb-11	284.2	1.2%	Feb-15	367.49	5.6%
Mar-03	125.7	10.2%	Mar-07	268.1	9.8%	Mar-11	286.1	1.2%	Mar-15	368.62	5.1%
Apr-03	128.5	11.1%	Apr-07	269.7	9.0%	Apr-11	287.8	1.3%	Apr-15	369.71	5.0%
May-03	131.1	12.5%	May-07	271.9	9.2%	May-11	289.3	1.7%	May-15	370.91	5.0%
Jun-03	133.6	14.4%	Jun-07	274.8	10.2%	Jun-11	290.3	2.2%	Jun-15	372.47	5.4%
Jul-03	136.3	16.5%	Jul-07	277.7	11.1%	Jul-11	291.0	3.0%	Jul-15	374.72	5.9%
Aug-03	138.6	18.3%	Aug-07	280.6	11.8%	Aug-11	291.5	3.3%	Aug-15	377.85	6.6%
Sep-03	140.9	20.0%	Sep-07	283.6	12.1%	Sep-11	291.7	3.3%	Sep-15	382.39	7.2%
Oct-03	143.6	21.8%	Oct-07	287.0	12.5%	Oct-11	291.9	3.2%	Oct-15	387.17	7.7%
Nov-03	146.8	23.6%	Nov-07	290.8	12.9%	Nov-11	292.9	3.6%			
Dec-03	150.4	25.5%	Dec-07	293.9	12.7%	Dec-11	294.9	4.4%			
Jan-04	154.1	27.2%	Jan-08	295.3	11.9%	Jan-12	297.8	5.3%			
Feb-04	158.1	28.3%	Feb-08	294.9	10.7%	Feb-12	301.3	6.0%			
Mar-04	161.9	28.8%	Mar-08	292.6	9.1%	Mar-12	305.1	6.6%			
Apr-04	165.1	28.5%	Apr-08	289.0	7.1%	Apr-12	308.5	7.2%			
May-04	167.6	27.9%	May-08	285.2	4.9%	May-12	311.0	7.5%			
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.*