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PROPERTY BAROMETER – RESIDENTIAL BUILDING OUTLOOK

Despite some poor Residential Building Completions figures in 2014 to date, we expect a return to moderate growth in the remainder of 2014 and 2015.

JOHN LOOS:
HOUSEHOLD AND PROPERTY
SECTOR ECONOMIST
011-6490125
John.loos@fnb.co.za

PLANNED RESIDENTIAL BUILDING ACTIVITY CONTINUES TO GROW IN 2014....

StatsSA Residential building statistics during the 1st half of 2014 have surprised us “on the downside”, showing year-on-year decline for the year-to-date after some moderate growth for the years 2012 and 2013 as a whole.

This has taken place while our FNB Estate Agent Survey has steadily pointed to increasing residential stock constraints in the existing home market. In addition, the square metreage of residential building plans passed has continued to rise in 2014 too.

This has led us even to sometimes wonder whether the Residential Plans Completed data has some “issues” of late, and is perhaps not recording the level of building completions as it should. However, this possibility would be difficult to ascertain.

Whether or not the completions data accurately reflects the recent trend or not, it would appear that the environment is ripe for some further mild growth in residential building activity in the remainder of 2014 and into 2015. But the emphasis is on “mild”.

Growth trends in residential building activity generally lag trend changes in demands for existing residential property by a considerable margin due to the lengthy “planning and preparation” period for new building. Therefore, after the 2nd leg of the “Double Dip” in new residential mortgage loans granted, in 2011, a recovery in new mortgage lending growth through 2012 to 2013 was followed by a return to positive growth in square metreage of Residential Building Plans Passed, with a lag, in 2013 and 2014-to-date.

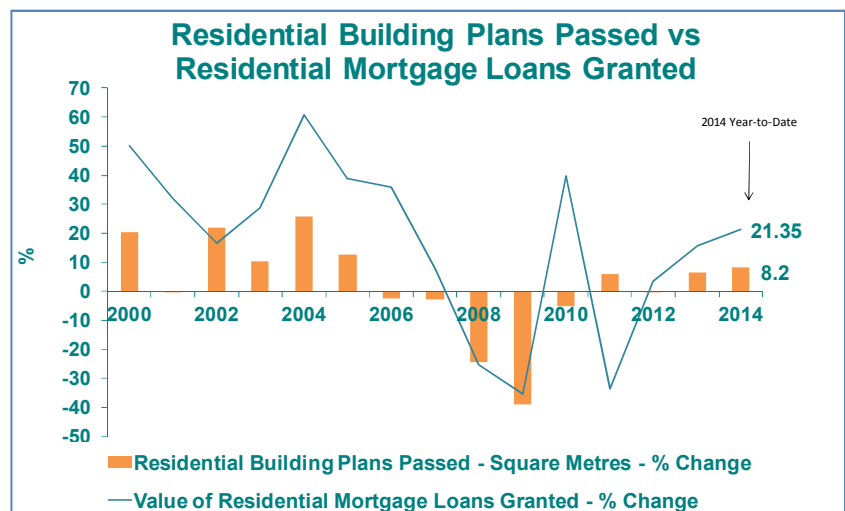
For the 1st quarter of 2014, the value of new residential mortgage loans granted had reached growth of 21.35% year-on-year, and the response of the Residential Building Sector had been 8.2% year-on-year growth in square metres of plans completed for the 1st 5 months of 2014, up from 6.4% growth for 2013 as a whole.

The statistics indicate, therefore, that in 2014 the Residential Development Sector has planned to grow new residential building at a faster rate than its planned rate in 2013.

THEO SWANEPOEL:
PROPERTY MARKET
ANALYST
FNB ASSET FINANCE
011-6320604
tswanepoel@fnb.co.za

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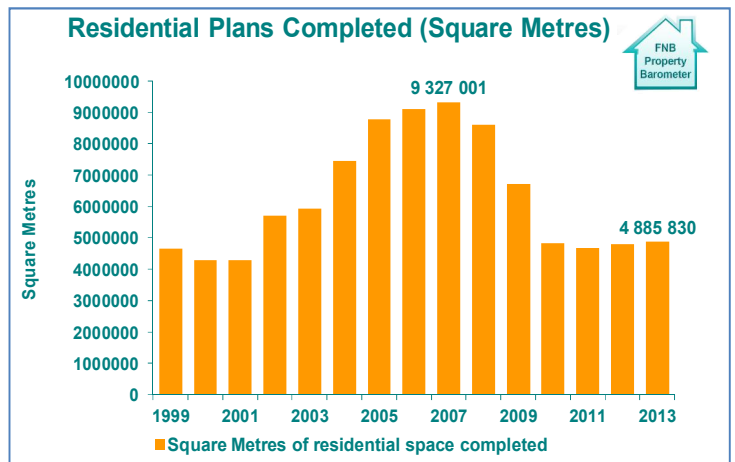
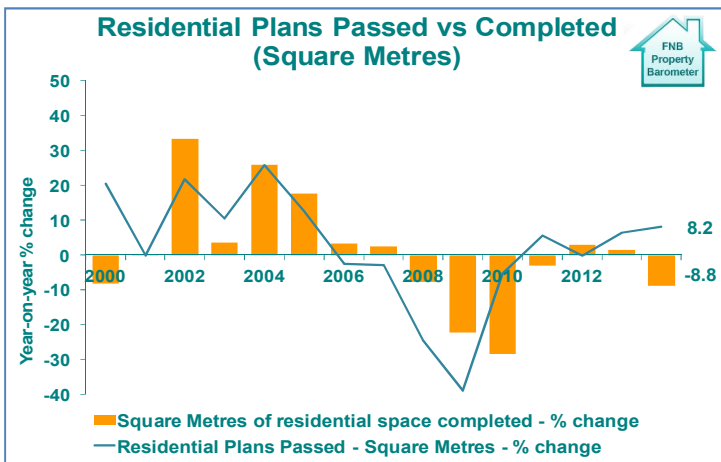


...AND WE WOULD EXPECT RESIDENTIAL BUILDING COMPLETIONS TO FOLLOW SUIT

However, despite the level of building plans passed continuing to grow in the 1st 5 months of 2014, Residential Buildings Completed data shows a very different picture, with the square metreage of completions declining significantly by -8.8% year-on-year for the period.

This may seem at odds with the data simultaneously pointing to growth in plans passed. But it is also possible that it is the lagged effect of the 2nd leg of the Double Dip in residential demand back in 2011 (causing a mild dip in building plans passed in 2012) which is still filtering through.

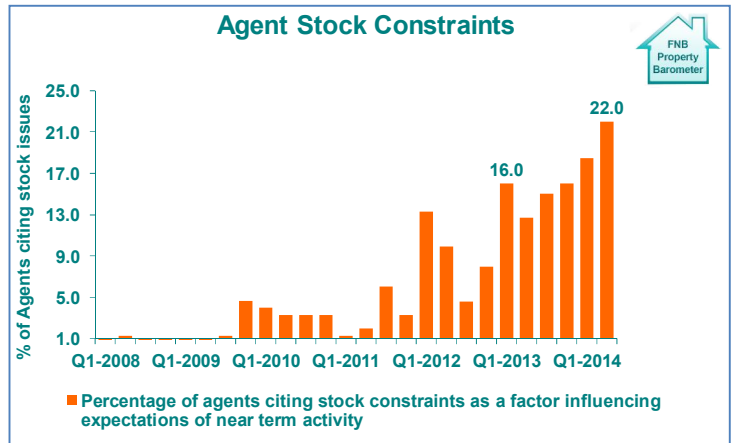
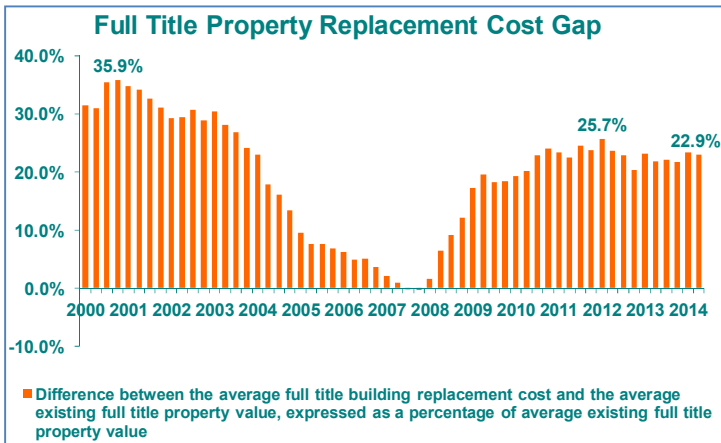
Nevertheless, we do still foresee positive growth in residential building activity returning in the 2nd half of 2014, and continuing into 2015. The reasoning for this expectation is based, firstly, on the fact that data points to strengthening in growth in plans passed in the 1st stages of 2014, and with a lag we expect that this has to likely filter through into growth in building completions. In addition, the level of residential building activity for 2013 as a whole remained at a level little more than half of what it was in 2007, which was the peak of the last building boom, and at a level not significantly higher than that at the end of the 1990s despite the economy these days being substantially larger.



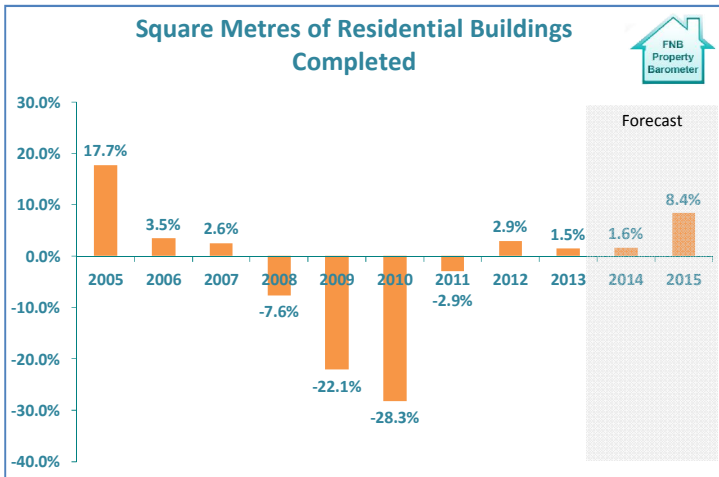
It goes further, though. Admittedly, building costs have been more of a constraint on the supply of new stock in recent years. The FNB Full Title Replacement Cost Gap (i.e. the percentage by which average replacement cost of a home exceeds the average existing home price) rose from zero at a stage of 2007 to 25.7% by early-2012, precipitating the post-2007 slowdown as new home prices became less competitive with a weak existing market at the time.

However, this Replacement Cost Gap has receded mildly to 22.9% by the 2nd quarter of 2014, with recent existing home price inflation positive in real terms as stock constraints grow. Examining our FNB Estate Agent Surveys of recent quarters, which pertain largely to the existing home market, we have seen a mounting scarcity of existing residential stock. By the 2nd quarter 2014 survey, when asking agents for the key factors driving their near term expectations of residential market activity, 22% of agents cited stock constraints as a key issue in their lives. This percentage has been growing steadily since 2012.

One would think that, either residential demand must slow in order to alleviate the stock constraints, or building activity will have to be ratcheted up a notch or 2.



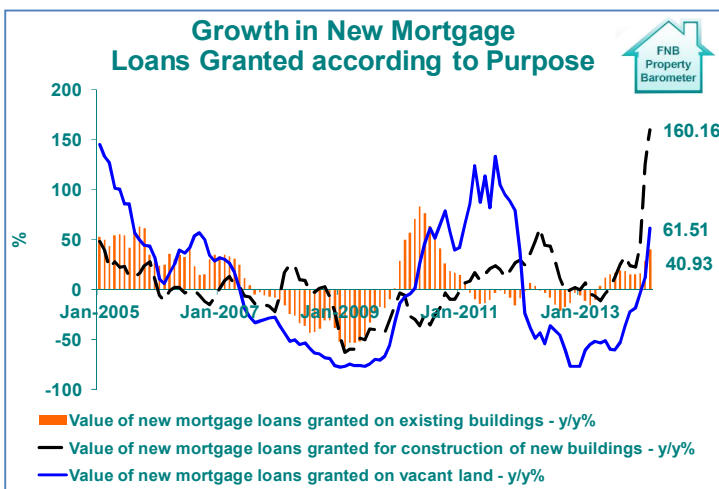
FORECAST – RETURN TO MILD GROWTH IN COMPLETIONS, AND “SMALLER REMAINS BETTER”



We expect a combination of the 2 abovementioned possibilities. The start of gradually rising interest rates is indeed expected to slow growth in residential demand in the near term, but in a very moderate way. However, we expect that stock constraints will remain significant, and this will have to be alleviated by some moderate growth in residential building activity too.

Therefore, we project such a moderate positive growth rate in square metrage of Residential Building Plans Passed, to the tune of 1.6% for 2014 as a whole and 8.4% for 2015.

This higher level of forecast residential building activity is expected to contribute to further mild slowing in house price growth through 2014 and 2015.



Our forecast of a return to growth in the building completion numbers is also informed by the SARB detail for Mortgage Loans Granted by Purpose. The value of new mortgage loans granted for the construction of new buildings accelerated by 160% year-on-year for the 1st quarter of 2014, suggesting significant growth in building activity to come. While this includes commercial building mortgages as well as residential, we expect that the residential component should contribute to some extent to this acceleration.

Finally, the financially constrained household sector is expected to sustain the broad trend towards a smaller average size of residential building completed, a broad trend since 2007. Such financial and affordability constraints are expected to continue to play into the hands of the “Flats and Townhouses” category of property, which has increased its percentage of total completions from 24% in 2011 to 34% for 2014 to date.

