



PROPERTY BAROMETER

FNB House Price Index

The FNB House Price Index continues its broad slowing growth trend as economic stagnation bites

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The FNB House Price Index inflation rate for August 2015 slowed mildly further, continuing a broad price growth slowdown starting back in early-2014. The further slowing is hardly surprising, coming on the back of ongoing economic stagnation with a rising risk of recession, and gradually rising interest rates.

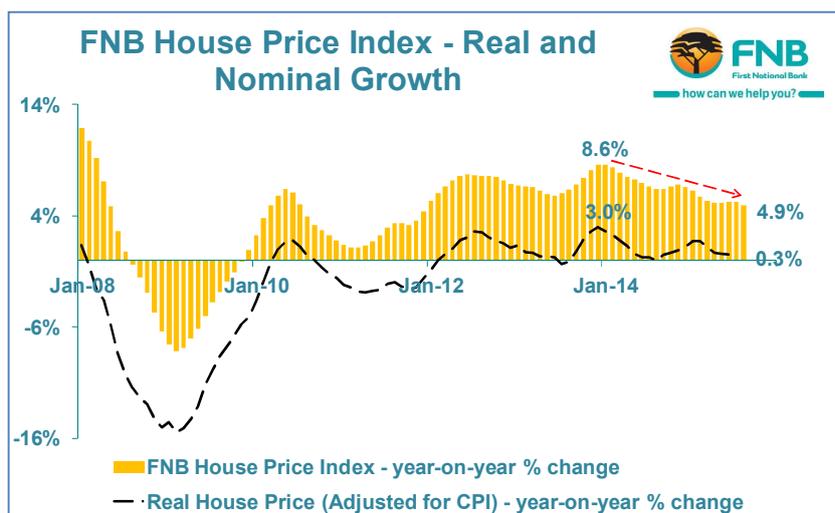
AUGUST FNB HOUSE PRICE INDEX FINDINGS

In the past month, little has changed in terms of the broader growth trend in the FNB house price index. Since way back in 2014 we have made mention of a broad slowing trend in average house price growth, in response to the combination of a multi-year weakening in economic growth along with the start of interest rate hiking early in 2014.

The FNB House Price Index for August 2015 rose by 4.9% year-on-year. This is down from the revised 5.2% for July, continuing the broader slowing price inflation trend that started back early in 2014 where 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 had slowed to 0.3% year-on-year in July (August CPI data not yet available), with rising CPI inflation of 5% only marginally lower than July house price inflation. It is likely that the real house price rate of change in August will come in at zero or even negative, given slowing house price inflation and rising CPI inflation.

The average price of homes transacted in August was R1,002,665

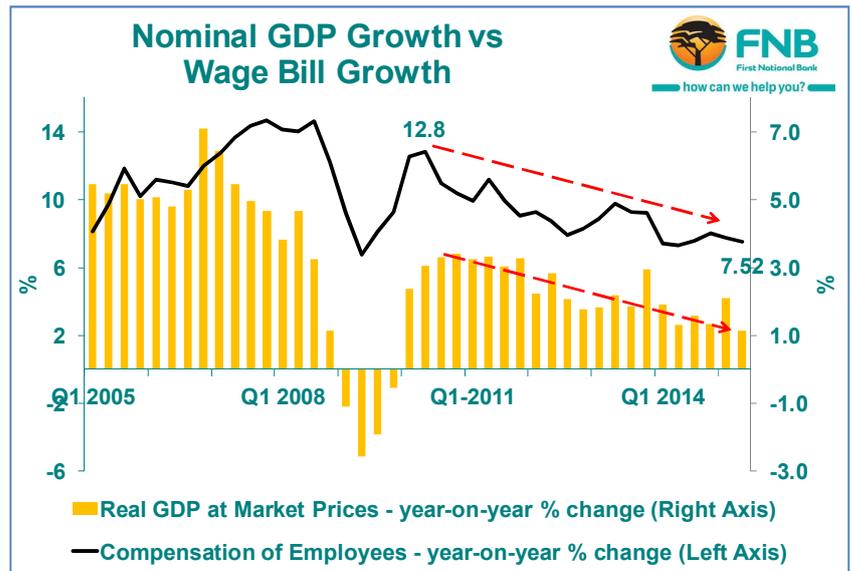


KEY FACTORS SLOWING PRICE GROWTH: POTENTIALLY FROM THE DEMAND AS WELL AS SUPPLY SIDE

Until recently, the key drivers of the broad year-and-a-half slowing house price growth trend have emanated from the demand side of residential property, but more recently we may have seen signs that supply side factors are also just beginning to play a role..

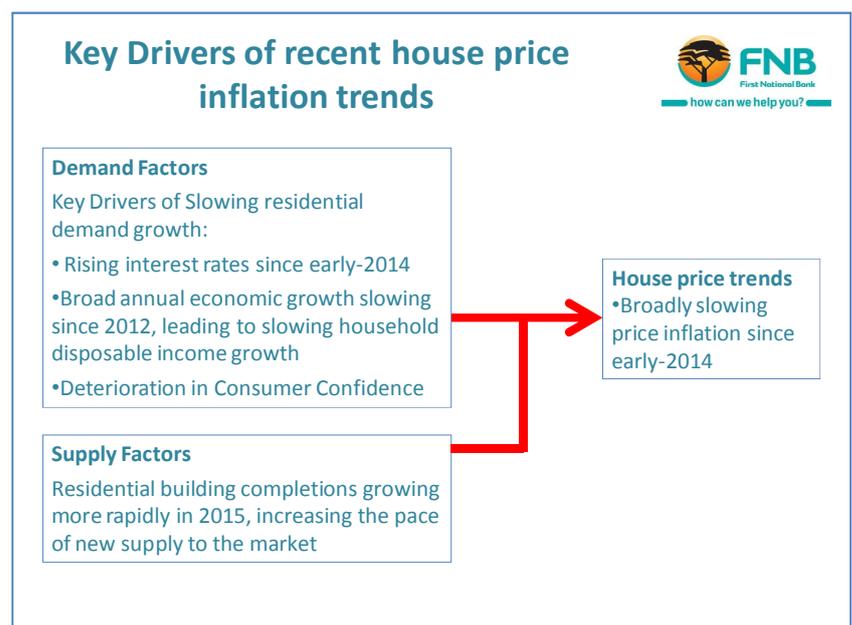
The key factors suppressing residential demand growth, we believe, are:

- Firstly, the Reserve Bank began its gradual interest rate hiking cycle in January 2014, and has hiked by a total of 1 percentage point over the 1st year-and-a-half, the most recent 25 basis point hike being in July 2015. While the small magnitude to date does not break the bank, it arguably leads to a little bit more caution in home buying, taking a bit away from residential demand.
- Secondly, the economy continues its broad multi-year stagnation, causing GDP (Gross Domestic Product) growth to slow, from a post-recession high of 3.2% in 2011, to 1.5% in 2014, and the indications are that 2015 may be even slower. This has slowed employment and wage bill growth. 2nd quarter 2015 GDP numbers were particularly bad, showing 1.2% year-on-year growth while contracting by -1.3% on a quarter-on-quarter annualized basis.



- Thirdly, Recent quarters have seen a dramatic drop in Consumer Confidence levels. The FNB-BER Consumer Confidence Index dropped to a negative level of -15, the lowest level in 15 years. This may not only be a function of a deteriorating economy, but also driven by concerns over the longer term future of South Africa, given a raft of bad news relating to economic management and the conditions of state owned enterprises, especially in the area of electricity supply.

On the supply-side, an acceleration in growth in residential buildings completed, to 31.9% year-on-year in the 2nd quarter, has the potential to begin to alleviate residential supply constraints in certain areas where they exist, should positive growth be sustained through the 2nd half of the year.



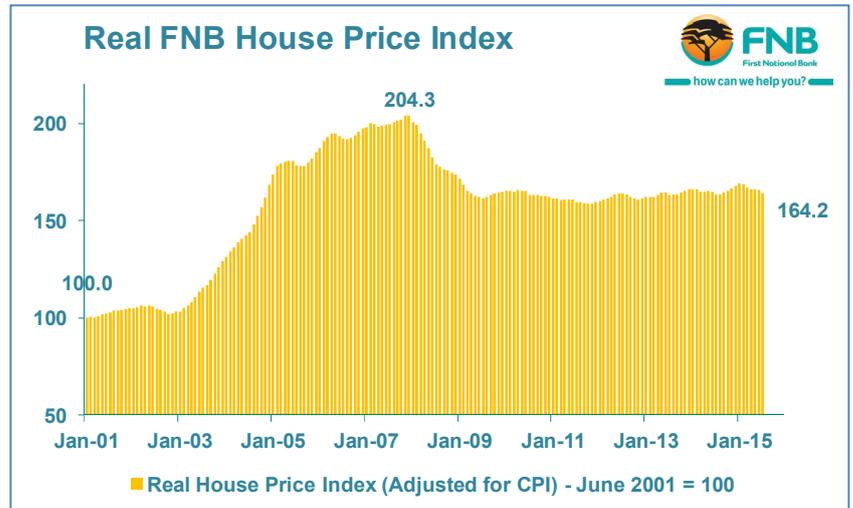
REAL HOUSE PRICE LEVELS

Examining the longer term real house price trend (house prices adjusted for CPI inflation), we see that despite some rise in recent years, (+3.5% since the October 2011 low) the average real house price level remains -19.6% below the high reached in December 2007 at the back end of the residential boom period.

Looking back longer though, the average real price remains 64.2% above the January 2001 level, 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 July 2015 was 272.5% above the January 2001 level.



OUTLOOK

The worse than expected 2nd quarter GDP figure, an alarming drop in the 2nd quarter FNB-BER Consumer Confidence Index, and recently a sharp month-on-month decline in the FNB Valuers Residential Demand Rating, suggests that a recession has become a distinct possibility

Our most recent average house price growth forecast is 5.4% for 2015 as a whole, slowing to 4.2% in 2016.

However, those forecasts are based on low positive economic growth continuing in South Africa during 2015/2016. This is an increasingly hazardous assumption to make as China's economic cracks widen, and SA's own structural constraints get seemingly worse.

We would thus say that the house price forecast risks lie very much to the downside of the recent forecast. In a China “Hard Landing” scenario, and a resultant domestic recession, the risk of house price deflation becomes very possible.

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.*

Some reasons for our choice of data source in compiling the Average FNB House Price data series:

The Average FNB House Price data series is compiled using transaction price data obtained from home transactions by purchasers applying for their home finance through FNB. As such, it is a very significant sample of South Africa's residential market, which we believe to be large enough to be "statistically representative". The key reason for deciding to utilize the FNB price data as opposed to the larger Deeds Office data set is:

- *The FNB data is more current/up to date than Deeds data which is updated with a considerable lag.*
- *The FNB data is purely residential. Deeds data, by comparison, does not distinguish between commercial and residential properties, thus requiring certain "filtering" and "cleaning" measures before use.*
- *The FNB data possesses a variety of home characteristics, captured with each property valuation done, which enables the grouping of home transactions by segment based on home characteristics. This is essential for our methodology of fixing the weights of the sub-indices in the overall house price index, so as to limit the impact of frequent volume activity shifts across segments, which can impact on the overall average price reading.*

In short, therefore, we choose a smaller sample size by using FNB data in the compilation of the FNB National House Price Index, but do so in order to be more up to date, and to have detail regarding properties.

What the FNB House Price Index represents:

Important to understand when using the FNB House Price Index is that it is NOT an estimate of the average value of all properties in South Africa. Rather, it is an estimate of the average price of those homes transacted. There is a very big difference, because the lower income groups tend to buy and sell homes far less frequently than those households towards the higher priced end of the market. High income/highly skilled people possess more financial resources to relocate more frequently as well as being generally more mobile job-wise.

This implies that the Average House Price as estimated in the compilation of the FNB Average House Price series will generally be far higher than the average value of all formal homes that exist in South Africa, due to a smaller ratio of homes transacted/homes that exist on the lower end implying "under-representation" of the lower end in the transaction data sample.

This does not render an average house price data series useless. Rather, it is very useful in determining the national house price inflation/deflation trend over time, but less useful in determining the average value of all homes in the country. In an ideal world we would value every single existing home in South Africa every month. But in reality that is impractical.

Is a national house price index of any use, given that each segment or area market behaves differently?

Yes, a national house price index is very useful. We get this question frequently, often by disgruntled property investors who would often like to believe that their area is very different to the national average. True, areas do have their differences in characteristics and popularity, and therefore don't all perform the same at any given time. However, their house price inflation graphs over time are far more similar than some would expect, we have found. This is because of two factors:

- *Firstly, the housing market is highly credit-driven. Interest rate cycles are thus a key driving factor, and the entire country's market is subject to the same interest rate trend.*

- *Secondly, South Africa's economy is highly integrated, with the same currency and interest rates within its borders, no boundaries on trade or business between or within regions. Therefore, certain economic events may well be unique to a certain region of South Africa. However, such events would easily filter out to other regions, albeit perhaps in a watered down form. In a country with no significant economic boundaries, therefore, the economic cycles of the different regions are fairly well correlated.*

Nevertheless, there are some differences. For instance, while the shape and timing of Gauteng and the Western Cape's economic cycles is very similar to other regions, their longer term economic growth rates are a little higher than the rest, which can possibly mean higher longer term average house price growth than other regions.

To this effect, we do compile a set of segment and regional house price data, in order to capture the differences in price performance that may exist.



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	353.16	7.2%
Jun-02	116.8	11.6%	Jun-06	249.3	12.5%	Jun-10	284.0	6.1%	Jun-14	353.51	6.9%
Jul-02	117.0	11.2%	Jul-06	249.9	13.0%	Jul-10	282.7	5.0%	Jul-14	353.78	6.6%
Aug-02	117.2	10.9%	Aug-06	251.1	13.5%	Aug-10	282.1	3.9%	Aug-14	354.59	6.4%
Sep-02	117.4	10.7%	Sep-06	252.9	13.8%	Sep-10	282.4	3.2%	Sep-14	356.58	6.4%
Oct-02	117.9	10.7%	Oct-06	255.1	13.6%	Oct-10	282.9	2.7%	Oct-14	359.30	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	364.54	6.6%
Jan-03	121.1	9.9%	Jan-07	263.9	12.1%	Jan-11	282.8	1.4%	Jan-15	366.46	6.2%
Feb-03	123.2	9.8%	Feb-07	266.3	11.0%	Feb-11	284.2	1.2%	Feb-15	367.90	5.7%
Mar-03	125.7	10.2%	Mar-07	268.1	9.8%	Mar-11	286.1	1.2%	Mar-15	369.24	5.3%
Apr-03	128.5	11.1%	Apr-07	269.7	9.0%	Apr-11	287.8	1.3%	Apr-15	370.45	5.2%
May-03	131.1	12.5%	May-07	271.9	9.2%	May-11	289.3	1.7%	May-15	371.44	5.2%
Jun-03	133.6	14.4%	Jun-07	274.8	10.2%	Jun-11	290.3	2.2%	Jun-15	372.10	5.3%
Jul-03	136.3	16.5%	Jul-07	277.7	11.1%	Jul-11	291.0	3.0%	Jul-15	372.33	5.2%
Aug-03	138.6	18.3%	Aug-07	280.6	11.8%	Aug-11	291.5	3.3%	Aug-15	371.98	4.9%
Sep-03	140.9	20.0%	Sep-07	283.6	12.1%	Sep-11	291.7	3.3%			
Oct-03	143.6	21.8%	Oct-07	287.0	12.5%	Oct-11	291.9	3.2%			
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%			