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PROPERTY BAROMETER –FNB HOUSE PRICE INDEX – JULY

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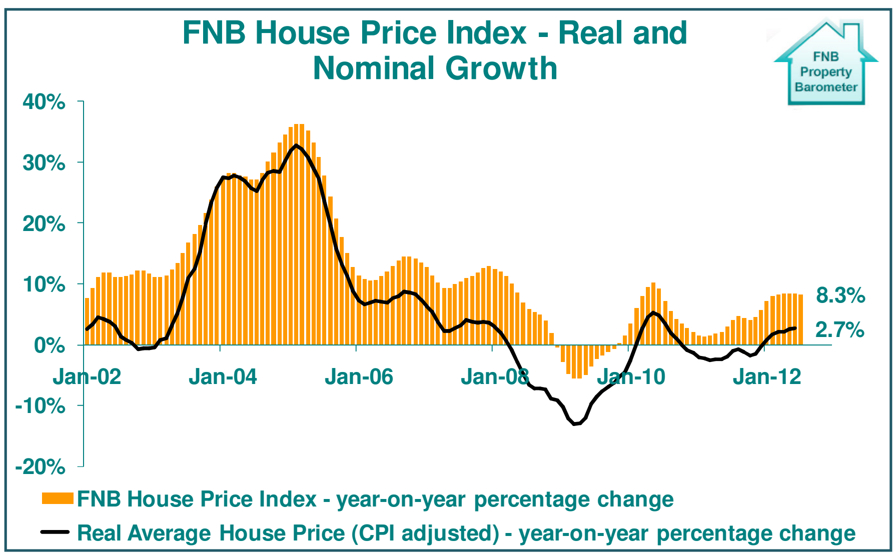
July FNB House Price Index shows year-on-year growth slowing, which may be beginning to reflect a slowing economy since earlier this year.

YEAR-ON-YEAR HOUSE PRICE GROWTH SLOWED MILDLY IN JULY

The FNB House Price Index showed a slight decline in its year-on-year growth rate in July, from a revised 8.4% rate in June to 8.3% in July. The start of a slowing year-on-year growth rate has been anticipated in recent months, due to the fact that the month-on-month seasonally-adjusted growth rate has been broadly losing steam since a January peak.

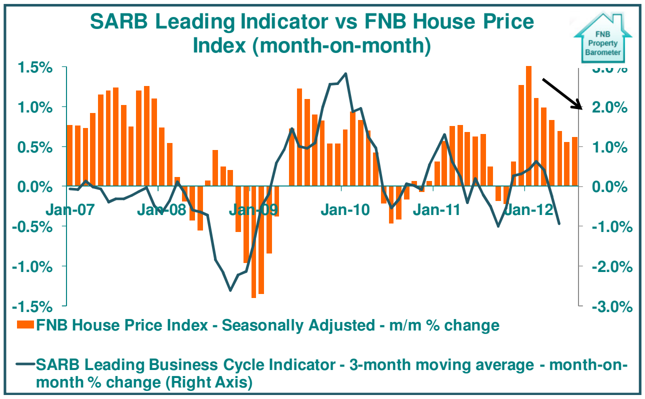
In real terms, adjusted for consumer price inflation, as at June the index showed a slightly year-on-year growth increase to 2.7%, from 2.6% in May, helped on by a further decline in consumer price inflation from 5.7% in May to 5.5% in June.



This means that since the "boom-period" real house price peak reached in February 2008, real house prices (house prices adjusted for CPI inflation over the period) were -12.4% lower at June 2012, while in nominal terms they were +14.7% higher than February 2008, as at July 2012.

However, compared to price levels at the inception of the FNB House Price Index back in July 2000, real prices were still 70.6% higher as at June 2012, while nominal price levels were +235.8% higher as at July 2012.

The start of a loss of price growth momentum is believed to be the result of a slowing economic growth rate in South Africa. After 3.2% quarter-on-quarter annualized gross domestic product (GDP) growth in the final quarter of 2011, the 1st quarter growth rate slowed to 2.7%, and certain high frequency economic indicators suggest a good possibility that the 2nd quarter may have been an even slower growth quarter.*



And it was during the 1st quarter, when the slowing economic growth rate commenced, that slowing month-on-month growth in the house price index also commenced, using seasonally-adjusted data.

From a peak of 1.72% month-on-month house price growth in January 2012, the rate has slowed to 0.62% as at July. This is very slightly higher than the 0.56% of June, but we would not read much into one month's acceleration.

The month-on-month trends in the house price index broadly correlate to the SARB Leading Business Cycle Indicator, and the trend in the 3- month moving average of the Leading Indicator has also been significantly down month-on- month in recent times.

CONCLUSION

While house price growth on a year-on-year basis is still at a relatively healthy level of 8.3%, it is believed that the above-8% levels of recent months reflects the peak in the recent resurgence in house price growth which originated during the summer months, and that a broad slowing is once more the order of the day in the near term.

This belief is brought about by perceptions of a weak global and domestic economy. Besides a declining SARB Leading Indicator, recent months have seen a broad decline in global purchasing managers' indices, while consumer related indicators such as domestic real retail sales have also been showing a broad slowing growth trend in the early stages of 2012.

Some may argue that the July interest rate cut will breathe some life into the residential market. It will indeed be a minor stimulus, and one may see a month or two's slight acceleration in month-on-month house price growth. But beyond that, we don't think it will totally offset the negative impact of a slowing domestic economic growth rate, and with it a slowing wage bill growth rate.

All considered, therefore, we anticipate a slower house price growth rate towards year end, and although recent year-on-year growth rates have been up above 8%, we anticipate a year-on-year growth rate of around 5-6% by year end.

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 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 "suburban segment volumes remain unchanged from one month to the next, but former Black Township (the cheapest areas 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.

The FNB House Price Index's main features are as follows:

- *The weightings of the 10 sub-segments were determined by their relative transaction volumes over the 5 years from 2003 to 2007. The weightings are fixed (to be revised periodically):*

- *Sectional Title:*
  - *Less than 2 bedroom (Weight – 0.0718)*
  - *2 Bedroom (Weight – 0.2106)*
  - *3 Bedroom (Weight – 0.101)*
  - *4 Bedrooms (weight – 0.0031)*
  - *More than 4 Bedrooms (Weight – 0.0002)*
- *Full Title:*
  - *Less than 2 Bedrooms (Weight – 0.053)*
  - *2 Bedrooms(Weight – 0.1092)*
  - *3 Bedroom(Weight – 0.3561)*
  - *4 Bedroom (Weight – 0.0811)*
  - *More than 4 Bedroom(Weight – 0.0139)*

- *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.*