PROPERTY BAROMETER – RESIDENTIAL PROPERTY MONTHLY

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June house price growth shows further mild acceleration.

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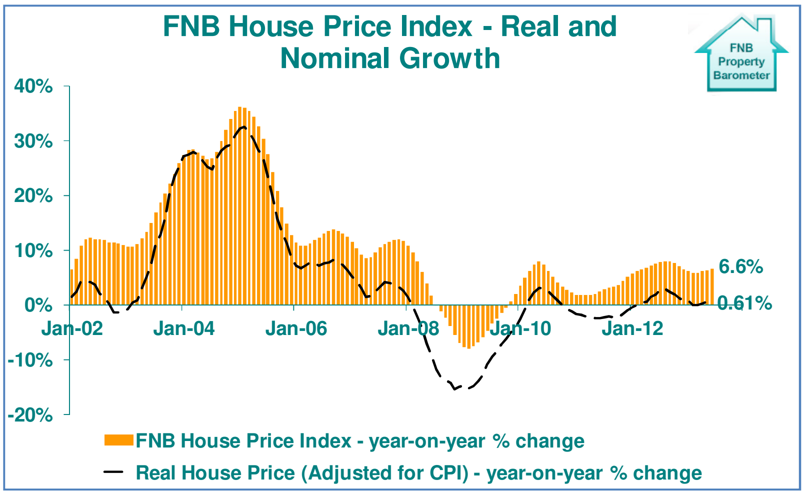
SUMMARY

The renewed acceleration in house price growth, which resumed early in 2013 after a lull late in 2012, continued in the June version of the FNB House Price Index.

The average house price for June showed year-on-year growth of 6.6%, up from May's revised 6.2%.

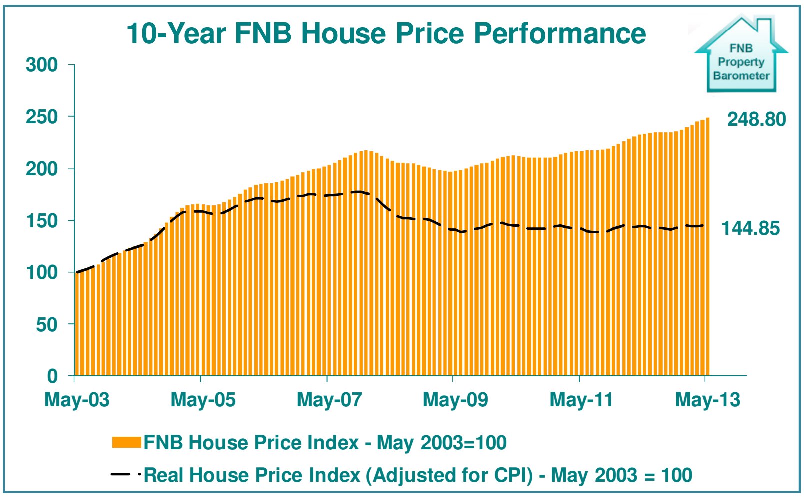
The average value of homes transacted in the FNB House Price Index was R891,266.



In real terms (adjusting house prices for general inflation in the economy using the CPI), as at May we were seeing very slight year-on-year increase to the tune of -0.61%, with consumer price inflation at 5.6% year-on-year in that month being slightly lower than house price inflation.

Evaluating longer term performance of the FNB House Price Index, in real terms the index is -18.6% down on last decade's real price peak reached in November 2007, while in nominal terms it is a mere 15.7% higher.

However compared to June 2003, 10 years ago, the index is up 44.8% in real terms and 148.8% in nominal terms, suggesting that the price effects of last decade's residential demand boom have far from worn off .despite a significant downward real correction since late-2007.



OUTLOOK - DESPITE RECENT IMPROVEMENT, HOUSING OUTLOOK MAY STILL BE A MEDIOCRE ONE WITH AN ECONOMY REMAINING UNDER SIGNIFICANT PRESSURE

The key data release in June was the SARB (Reserve Bank) Quarterly Bulletin, which confirmed our expectation that real household disposable income growth had slowed further in the 1st quarter from a prior quarter's 2.4% quarter-on-quarter annualised rate to 2.2%. This has a bearing on residential buyer purchasing power growth, and largely explains the recent steady deterioration in Consumer Confidence in recent quarters.

In addition, interest rates continue to move sideways, with prime rate having remained at 8.5% since the 3rd quarter of last year., thus offering no additional demand stimulus since then. The combined impact of no interest rate cutting as of late and slowing disposable income growth could have constraininge implications in terms of growth in residential demand in the near term, with economic growth looking set to battle to exceed 2% for 2013 as a whole.

The current level of interest rates set by the SARB is at multi-decade lows, and indeed the stability of interest rates at these low levels has helped to gradually strengthen residential demand through 2012 and early-2013. But it is questionable whether this residential demand strengthening can continue at a time of clear economic weakness, and where we have already seen a steady slowing in growth in the area of real consumer demand as a result.

For 2013 as a whole, therefore, a weak economy and resultant weakened disposable income growth leads to the ongoing expectation that house price growth will continue to remain largely in single-digit territory in the near term, due to potential pressure on demand, not far outpacing consumer price inflation of near to 6%.

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 "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.

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.*

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.*