PROPERTY BAROMETER – HOUSE PRICE INDICES BY SIZE

Increasingly, in the residential property market, size counts, but it is smaller that is increasingly proving to be better. This has much to do with the sharply rising costs related to homes, along with a more financially constrained Household Sector since the end of last decade's boom years

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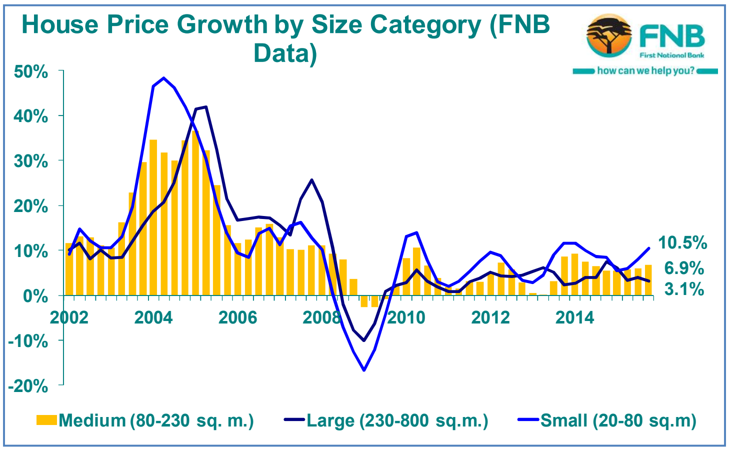
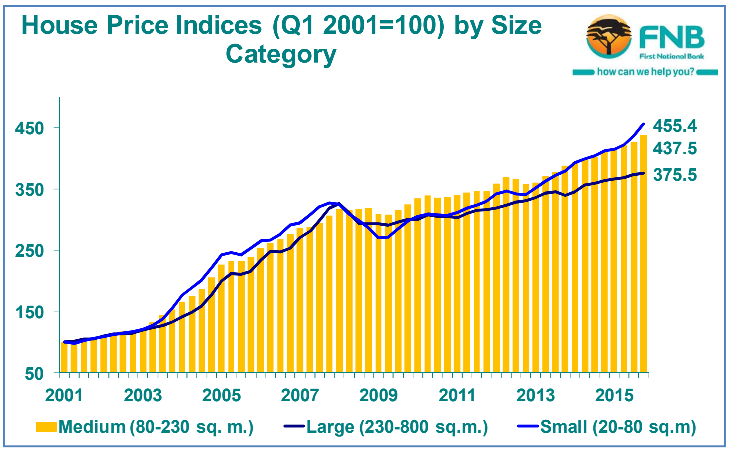
Size counts for many home buyers these days, due to a number of housing-related affordability constraints, so there are no prizes for guessing that "small-sized" houses have shown the strongest house price inflation in recent times, according to the FNB House Price Indices according to size category.

One of the market segmentations that we do is according to home size. Our 3 size categories are the Small-sized segment (homes 20-80 square metres in size), Medium-sized homes (80-230 square metres in size) and the Large-sized homes segment (230-800 square metres).



As at the 4th quarter of 2015, the Small-Sized Homes category showed an average house price increase of 10.5% year-on-year, which was up from the prior quarter's 9%. Many of these homes fall into the so-called "Affordable Housing" market, with a price average of R593,323 for the 4th quarter. This relative strength ties in with our FNB Estate Agent Survey, where agents in the so-called Lower Income Area Segment have been the most upbeat on market strength of all the segments' survey respondents.

By comparison, the Medium Sized Home (average price R1,076,155) segment showed average house price inflation of 6.9%, while the Large Sized segment (average price R1,907,588) had recently slowed to average a mere 3.1% increase for the final quarter of 2015.



Examining broader long term trends, we see that since the 1st quarter of 2001, the Small-Sized Home segment has outperformed the 2 larger categories, having inflated cumulatively by 355.4% up to the end of last year, a 15 year period. By comparison, the Medium-Sixed category rose by 337.5%, and the Large-Sized segment by a lesser 275.5%.

But the superior performance of small sized homes has been more a post-boom phenomenon (the "boom" having been over the years prior to 2008). Examining the cumulative house price growth from the 1st quarter of 2001 up until the 4th quarter of 2007, the Small-Sized segment recorded 227.2%. This is ahead of the Medium-Sized category's 207.2% but insignificantly so compared with the Large-Sized segment's 218.2%.

Then, in the slump of 2008, the Small-Sized segment showed the most extreme price drop, to wipe out any relative boom time "lead" on the other segments.

Since the post-recession recovery started, though, it appears to have been the Small-Sized segment that has had the strongest price growth almost throughout, inflating cumulatively by 68.4%, ahead of the Medium-Sized segment's 41.7% and the Large-Sized category's 28.2%.

The noticeable differential in segment inflation rates can be explained by a number of affordability-related factors:

- *Firstly, the boom period left the Household Sector with far higher indebtedness levels, while slower economic growth since the end of the boom years has meant slower household disposable income growth. In short, the Household Sector has had more significant financial limits in the post-boom period. Smaller thus becomes better just purely from a lower average house price point of view.*
- *Secondly, the boom period left us near to the highest real house price levels in recorded history, and this has not "corrected" much since the end of the boom. High house prices add to the affordability challenge, further contributing to greater demand for smaller and cheaper homes.*
- *It goes further than income and home affordability, however, to certain home-related cost increases, especially Municipal rates and Utilities Tariffs (Eskom most notably), which have been rising significantly faster than overall Consumer Price Inflation. Electricity and water costs can be contained by owning a "smaller" home with less frills such as water-guzzling swimming pools.*
- *Fourthly, we would mention urban densification, which drives congestion. Whereas 30 years or so ago, a middle class family may have looked to settle further out of a city where space was plentiful, today it becomes a challenge not only due to a lack of new urban expansion but also due to commuting times and costs as a result of rising congestion. The limits on urban sprawl often drive residential demand towards smaller sized units which may be reasonably well-located. In short, location becomes increasingly important in a congested city while living space becomes less important.*

In the near term, with the economy weakening and interest rates expected to rise further, the financial constraints on the Household Sector may become still more significant. That could play into the hands of the smaller-sized home segment to an extent, provided the country is not hit by a severe economic downturn, as more households are forced to "cut their coat according to the cloth".

However, this only works to a point. Lower income households are more financially "fragile than higher income ones, and should the economic or interest rate "shocks" become too severe, they would suffer to a greater degree, and the small-sized home segment could then end up performing worst of the 3 due to financial stress in this market. This was the case around 2008/9 in that short but sharp recession, where interest rates peaked at 15.5% Prime Rate, leading to severe financial pain for a highly indebted household sector.

For the time being, though, "Smaller is Better" it appears.

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