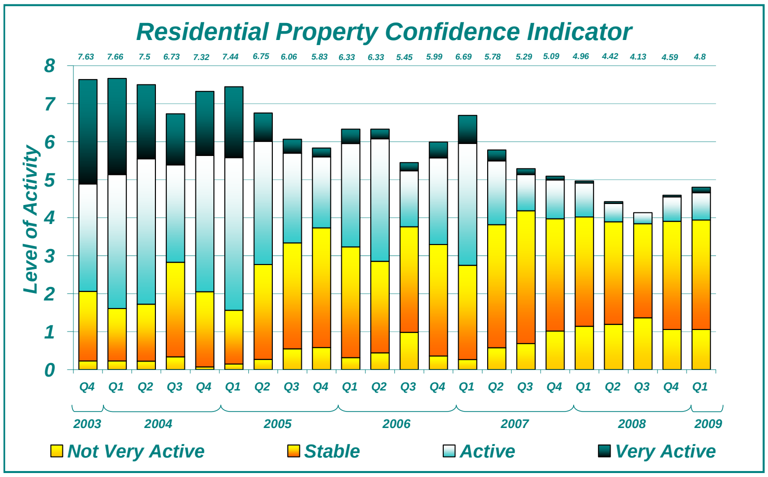
DEMAND ACTIVITY RISES AND EMIGRATION SELLING FALLS



FNB PROPERTY BAROMETER

– 1st QUARTER 2009

- Estate agents reporting further improvement in demand activity, and drop in emigration selling, but the overall survey picture remains unconvincing as yet

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SECTION 1: SUMMARY – ACTIVITY UP BUT LIMITED "GREEN ON THE SCREEN"

SUMMARY OF PROPERTY BAROMETER SURVEY RESULTS	Quarter 1 2009	Previous quarter	Year ago	Recent Smoothed trend
Demand Activity Level	4.8	4.59	4.96	↑
Average time on the market (weeks and days)	17.4	15.3	11.4	↑
Percentage of sellers having to drop their price	86	81	83	→
First time buyers as a percentage of total buyers	15	17	14	→
Buy-to-let buyers as a percentage of total buyers	11	12	13	↓
Percentage of sellers selling to downscale due to financial pressure	26	26	15	→
Percentage of sellers selling to upgrade	7	9	13	↓
Percentage of sellers selling to emigrate	11	14	12	↓

Deteriorating trend | Sideways trend | Improving trend

The FNB Residential Property Barometer is a quarterly survey of a sample of estate agents in the country's major urban regions, aimed at obtaining their opinion on a wide range of issues pertaining to conditions in the residential property market. The main question asked pertains to how they experience demand activity levels on a scale of 1 to 10. For the second successive quarter this level rose mildly from 4.59 in the final quarter of 2008 to 4.8 in the 1st quarter of 2009.

The only other significantly positive result from agents surveyed was a significant decline in emigration selling as a percentage of total selling for the second consecutive quarter (see box on next page). This aside, the picture remains unconvincing. The 4 "headline indicators", namely average time on the market, percentage of sellers having to drop their price, first time buyers and buy-to-let buying all showed quarterly deteriorations and these numbers remain weak.

The Barometer also points to affordability remaining a key issue in a weak economic environment, and resulting in the household sector doing away with the "luxuries" in a bid to stabilise its financial situation. These include a further decline in holiday home buying as a percentage of total buying, renovations and maintenance are increasingly limited to the basic essentials with little value adding investment in homes by owners, downscaling due to financial pressure is said to be the single most common reason for selling, and selling in order to upgrade declined further in significance from quarter to quarter.

41% of agents expect activity levels to increase further in the second quarter, compared to only 25% in the first quarter a year ago. The start of interest rate cuts, and expected further cuts, is the key driving force behind this more positive expectation at the start of 2009, but the optimism remains cautious. Strict bank credit criteria at present are cited as a key negative factor inhibiting a market recovery, while agents are also mindful of global events, and cite negative sentiment related to a weak global and local economic growth situation as problematic too.

Can the bank criteria situation change in the near term? Probably slowly at best. Lower loan-to-value ratio limits are the result of recent price deflation and the resultant losses in the case of default becoming an issue. While demand may well be on the rise, albeit mildly, the Barometer still points to affordability issues and high levels of selling due to financial strain, which suggests the ongoing existence of an oversupply in the market. This suggests that price deflation may continue in the near term. In addition, the global economic crisis is impacting on the South African economy, and in the current recessionary environment job losses are a further risk to default rates in the near term.

Nevertheless, from the low base created last year, it is still realistic to expect some demand recovery, as affordability of loans must surely improve for a significant group whose income is not negatively impacted by the adverse economic conditions.

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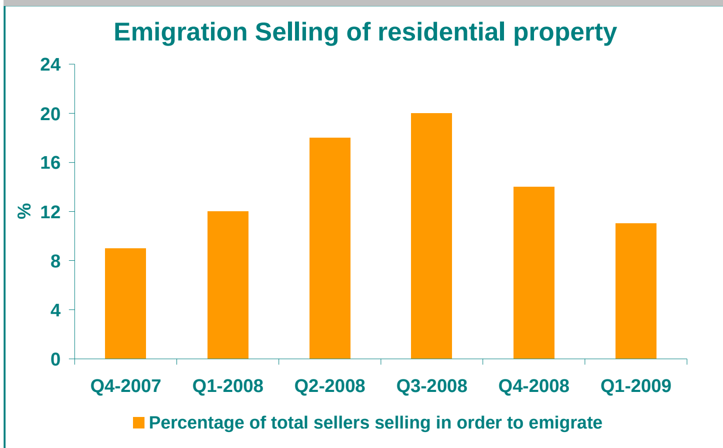
BOX 1. FOCAL POINT: WITHER EMIGRATION SELLING IN 2009, WITH FACTORS ON BOTH SIDES OF THE OCEAN PLAYING A ROLE



In 2008, a wave of emigration selling occurred in the residential property market, at a time when there was already a significant oversupply of stock in the market. According to FNB's Residential Property Barometer survey, as much as 20% of residential selling was believed to be for emigration purposes by the 3rd quarter of 2008, after a sharp rise in this percentage since late-2007.

To give some perspective, it must be understood that this is a thin market we are talking about compared to a few years ago, so absolute numbers of emigrating sellers would probably not be as impressive as some may think, but it is nevertheless believed that there was a rise in the absolute number of emigrants in the first half of last year, and the levels of their selling became quite an important influence on suburban markets.

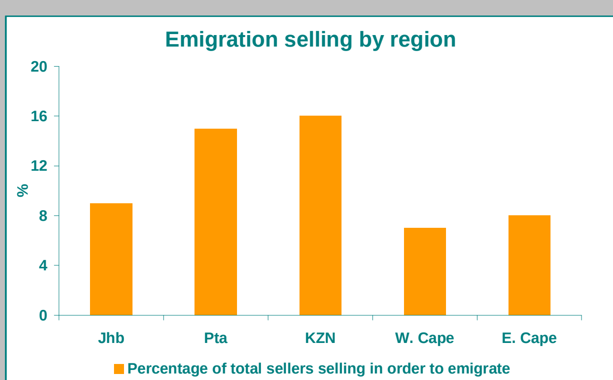
A number of reasons could be advanced for this emigration surge:

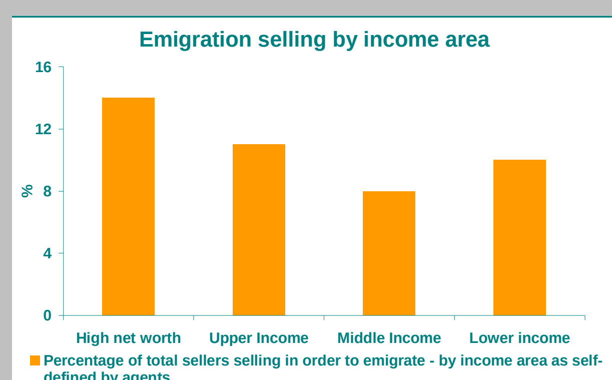
- Last January, the Eskom power crisis did a lot to contribute to a dampening in confidence regarding the country's longer term performance.
- The ANC's Polokwane Conference in late-2007 brought dramatic changes in the party leadership, and such radical political changes can tend to heighten jitters amongst the minority race groups regarding the country's future.
- The Zimbabwe crisis continued to deteriorate, and the Mbeki administration's perceived handling of the crisis did not inspire confidence.
- High profile violent crimes did hit the headlines frequently, and this may have heightened the perception of an increase in violent crime, although it is difficult to ascertain whether there was actually any addition to the already high levels of crime.

Then, in the 4th quarter of 2008 we started to see a decline in the percentage of emigration selling to 14%, and further to 11% in the 1st quarter of this year, according to the estate agents surveyed. This was by-and-large expected, as the "discomfort" surrounding some of the above events was bound to dissipate over time. Eskom's management of power supply has indeed improved dramatically (possibly partly helped by a slowing economy alleviating electricity demand pressures), and over time many people do get used to the political changes that have been made, just as they did post-1994.

But what is perhaps not yet appreciated is just what an impact the global economic crisis can also have in slowing the pace of emigration, and thus emigrant selling of residential property in 2009. With the global economy in its worst crisis in decades, job prospects (generally-speaking) in traditionally popular emigration destinations are unlikely to be rosy during the current year.

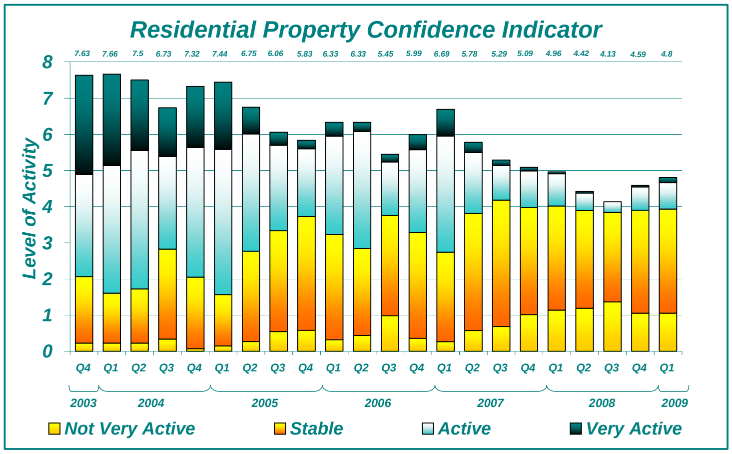
It is therefore expected that emigration selling of residential property will taper off steadily, to become a far less significant driver of supply of stock onto the market during the course of 2009.

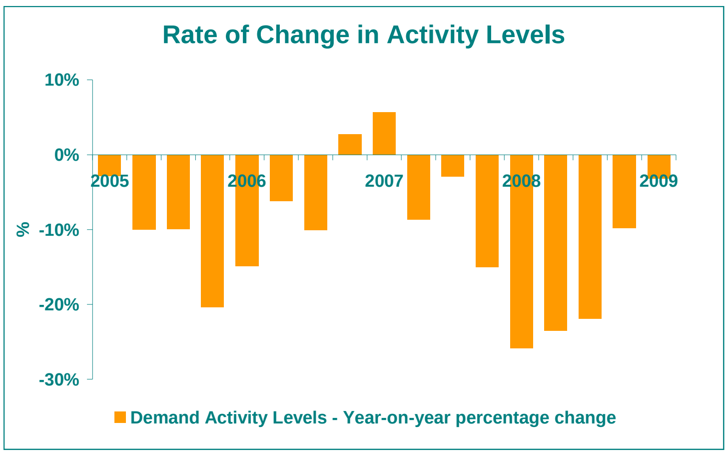


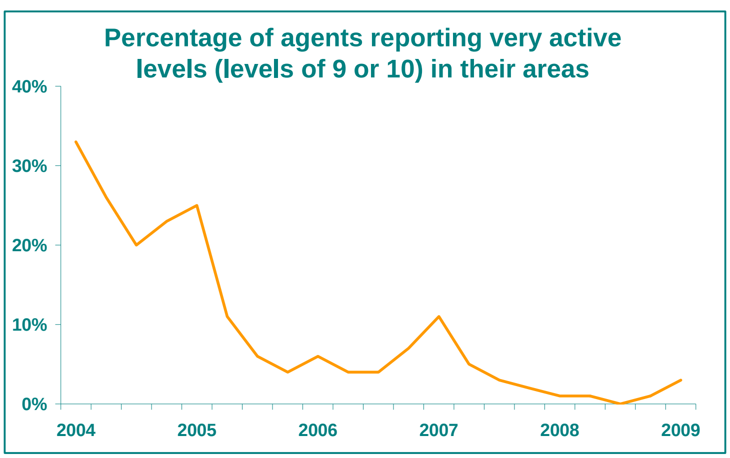


SECTION 2: DETAILED VIEW OF BAROMETER FINDINGS

DEMAND ACTIVITY RISES FURTHER, WITH INTEREST RATES POSSIBLY ALREADY HAVING SOME MILD IMPACT







According to the FNB Residential Property Barometer survey, the positive impact from interest rates on residential property may have begun prior to interest rate cutting, although the impact appears mild. In this survey of a sample of estate agents, where it is asked of them to rate demand activity as they experience it on a scale from 1 to 10, Quarter 1 of 2008 saw the second consecutive quarter of increase in activity levels. The lowest activity level on record was recorded in quarter 3 of last year, a level of 4.1, which rose to 4.6 in the following quarter and then further to 4.8 in the current quarter.

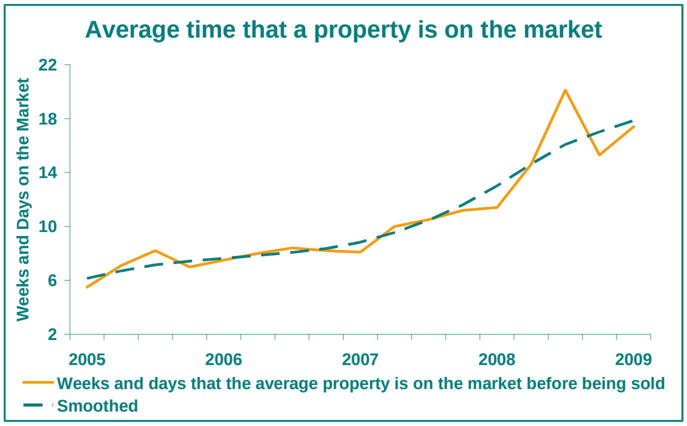
It is possible that seasonal factors did play a role in this 2-quarter rise, but even when we cut out seasonal factors by calculating year-on-year percentage change in activity levels, we see that by the first quarter the previously rapid rate of year-on-year decline had become almost non-existent, representing at least a stabilisation in demand. So, while this improvement in activity levels is by no means wonderful, it would suggest that we have perhaps had a bottoming out in demand for now, and surveyed estate agents mention interest rates as a very important factor in driving their near-future expectations.

How do interest rates impact on demand before they get cut? It is through the additional comfort that a group of potential buyers takes from the end of interest rate hiking and increasing expectation that the next rate move will be down, as was the case in the latter part of last year. So confidence levels can rise prior to rate cuts, and this may have been the case for a group of people, inducing a slight improvement in residential demand.

Although still a very small group, the percentage of survey respondents reporting "very active" levels of demand activity rose slightly from 0% of total respondents in the 3rd quarter of 2008 to 3% in the 1st quarter of this year.

BUT THE BROADER SET OF BAROMETER "HEADLINE" INDICATORS DOES NOT YET PROVIDE A CONVINCING PICTURE

All 4 of the "Headline Indicators", namely Time on the Market, Percentage of sellers required to drop their asking price, First time buyers as a percentage of total buyers, and Buy-to-let buyers as a percentage of total, showed quarterly deteriorations in the first quarter.

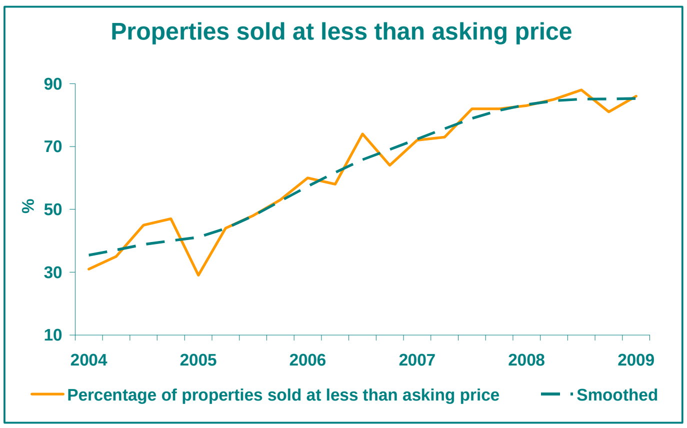


AVERAGE TIME ON THE MARKET RISES ONCE MORE

After a significant fall, during the 4th quarter of 2008, in the average time of a property on the market to 15 weeks and 3 days, the 1st quarter saw this average revert to its rising trend back up to 17 weeks and 4 days.

To the naked eye, this would appear in contradiction of the survey respondents' assertion that average demand activity levels are rising. However, it is possible that, following the start of interest rate cuts late last year, unrealistic expectations amongst sellers regarding asking prices and their ability to achieve these prices may have once again risen.

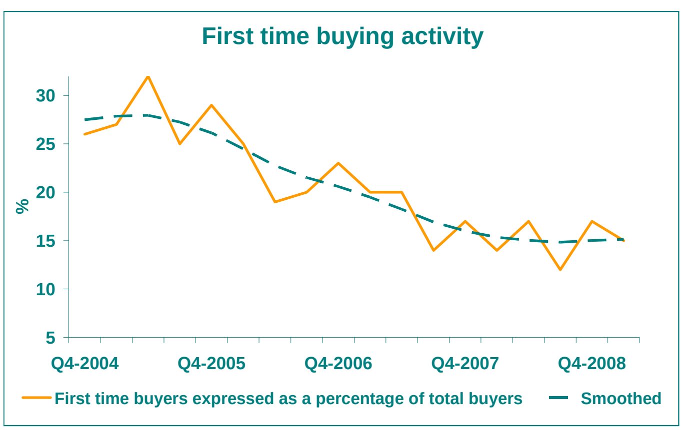
The smoothed trend line, representing average time on the market, still points higher.



A SLIGHT RISE IN PERCENTAGE OF SELLERS DROPPING THEIR PRICE

The overwhelming majority of sellers were still required to drop their asking price to make the sale in the 1st quarter, and a percentage of 86% (slightly up from 81% previous) is ongoing indication of the unrealistic expectations still prevalent in the selling market during these very weak economic times.

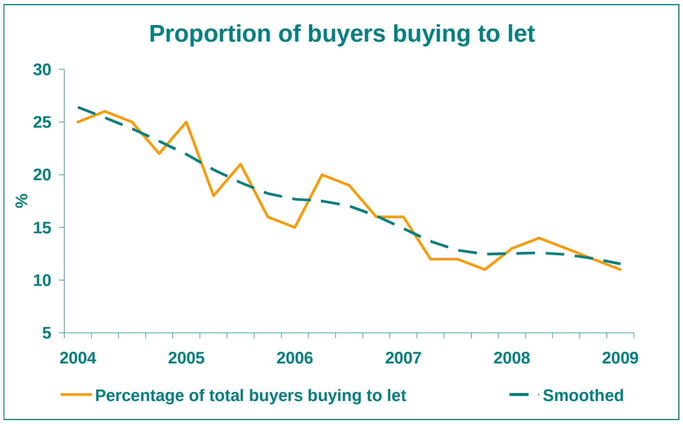
The smoothed trend line for percentage of sellers having to drop their asking price has flattened out after a multi-year rising trend.



FIRST TIME BUYERS DECLINE SLIGHTLY

The level of first time buyers expressed as a percentage of total buyers remains in the doldrums, having shown a small quarter-to-quarter decline from 17% in the 4th quarter to 15% in the current quarter.

First time buyers continue to exercise their greater degree of flexibility, as opposed to established families, either choosing to stay in the rental market for longer or remain in their family home. This group should begin to arrive in the market in greater numbers in better economic and interest rate times. However, against the positive news of interest rate cuts, this group may be more affected by banks' recent tightening up on loan to value ratios and thus increased deposit requirements, which may slow its recovery in demand. The first time buying smoothed trend line has flattened out in recent quarters after a multi-year decline.

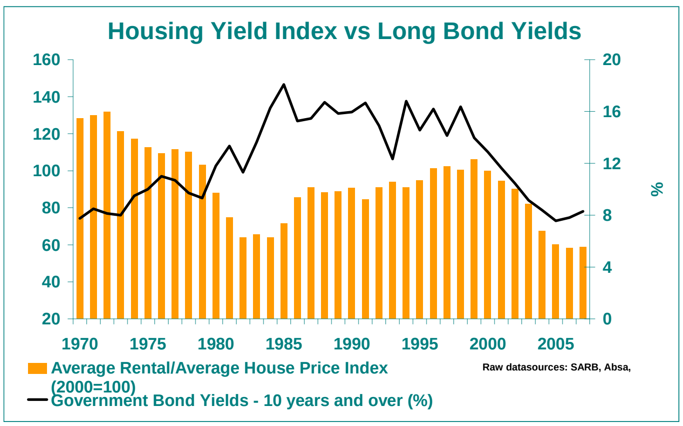


BUY-TO-LET BUYING REMAINS SLOW

From quarter-to-quarter, buy-to-let buying expressed as a percentage of total buying continued its mild decline, with buy-to-let buyers expressed as a percentage of total buying declining from 12% in the 4th quarter of 2008 to 11% in the 1st quarter of 2009.

The smoothed trend line for buy-to-let buying is still on a mildly declining path.

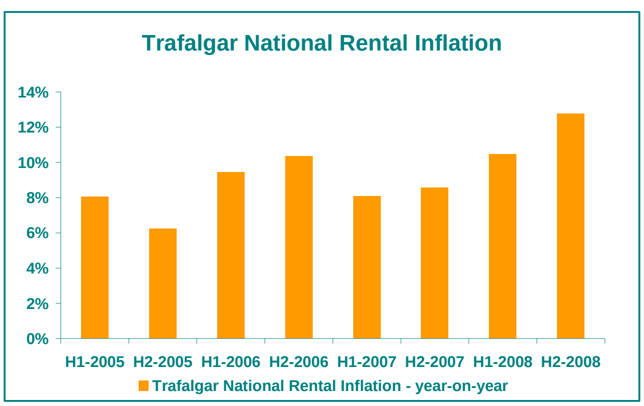
For many investors as yet unsure about the timing of a residential market recovery, buy-to-let buying remains un-attractive. Although rental data in SA remains piecemeal, indications are that rental inflation continues. Trafalgar reports national rental inflation of 12.8% year-on-year as at the end of 2008. StatsSA, which surveys actual rental paid (determined by the combination of market rentals and escalations of existing contracts), estimates 8% year-on-year actual rental inflation as at January.

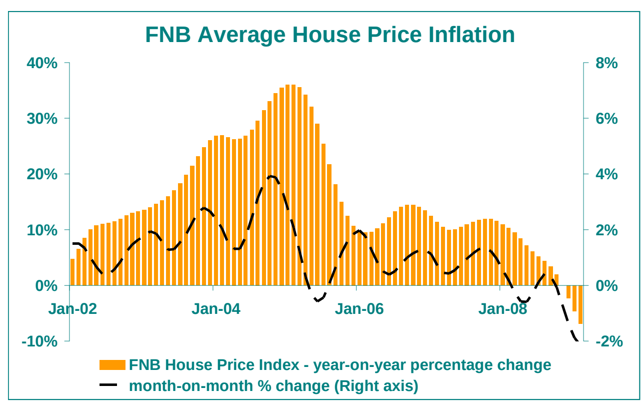


Against ongoing rental inflation, we have house prices firmly in deflationary territory, which should be translating into a steady widening of yields, which ultimately would contribute to making buy-to-let buying more attractive. The graph to the left shows that the declining yield trend of the boom years probably started to flatten out around 2007.

Widening of yields, though, would be insufficient for many prospective buy-to-let investors though, with many also concerned with capital growth, something non-existent at present.

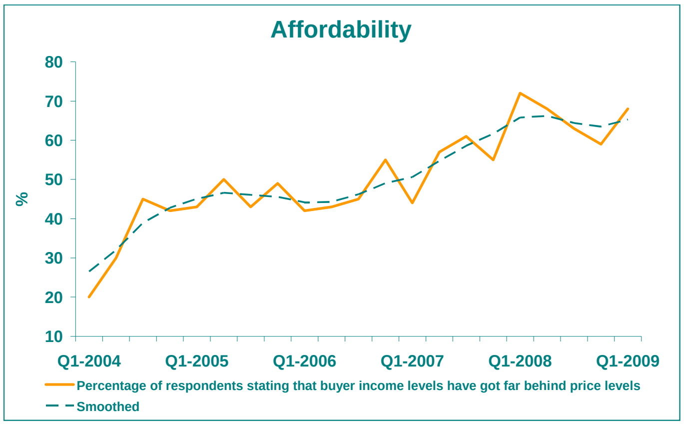
Although yields are believed to be rising at present, they are still believed to be on the low side in the case of residential property, while many potential buy-to-let buyers would probably only appear once interest rates are firmly on a downward path and capital growth prospects improve. Therefore, we anticipate little in the way of buy-to-let improvement as a percentage of total buying in the near term, and any possible recovery in demand at present is expected to be more primary residential demand driven.





THE FOCUS IS ON THE BASICS AS THE HOUSEHOLD SECTOR TRIES TO IMPROVE ITS FINANCIAL SITUATION

Although agents report some mild rise in residential demand activity, we're by no means out of the woods yet, with affordability issues still widespread in this weak economic growth environment. And in many of the "supplementary indicators" that make up the Barometer, we find widespread evidence of attempts to get the household finances back in order in response to a tough economic period. The demand focus is increasingly on the primary residence, renovations and maintenance are increasingly focused on the essentials only, widespread selling in order to downscale continues to be reported, while selling in order to upgrade is the exception.



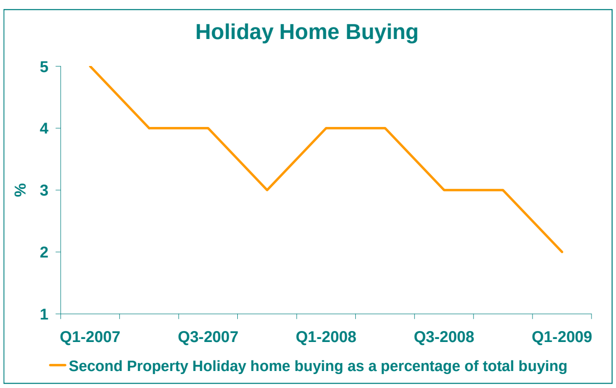
Affordability is still believed to be a key issue in this market, with 68% of agents surveyed believing that household income levels have got far behind property price levels. 19% say income levels are "a bit behind" price levels, while only 13% claim that household income levels have kept up with property values.

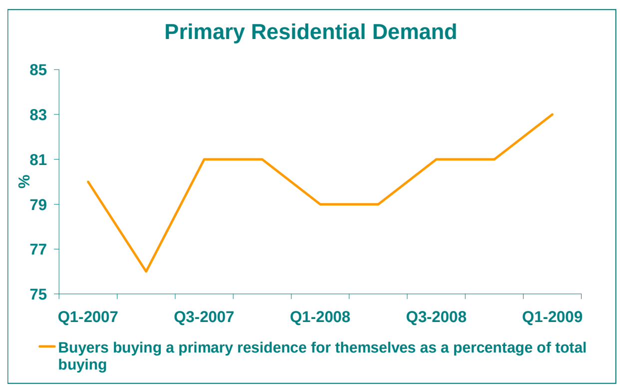
The smoothed trend line points towards a flattening out in the trend, from a previous steady rise, but the widespread belief that affordability is an issue has not yet dissipated.

PRIMARY RESIDENTIAL DEMAND RULES AS HOLIDAY BUYING DECLINES IN IMPORTANCE

Not only has the non-essential buy-to-let buying category been declining in significance. Holiday home buying, too, continues to decline as a percentage of total buying, reaching 2% of total buying by the 1st quarter of this year. By contrast, primary residential demand rose further in the 1st quarter, reaching an estimated 83% of total buying, up from 79% three quarters ago.

Of coastal holiday home buyers, 78% are said to be from "out of town", mainly from Gauteng, only 8% are from the same coastal region, 10% are believed to be foreigners and a mere 2% are estimated to be expats living abroad.





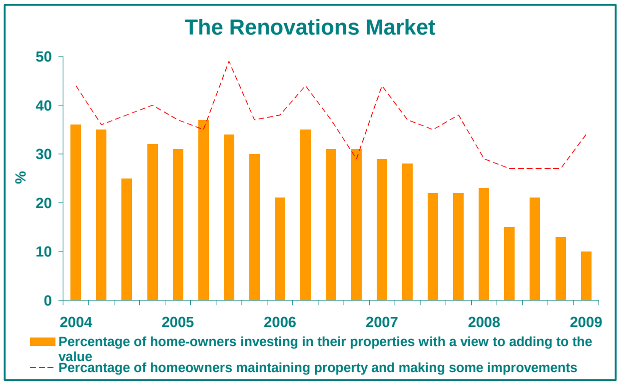
INVESTMENT IN PROPERTY BY OWNERS IS INCREASINGLY FOCUSED ON ESSENTIALS

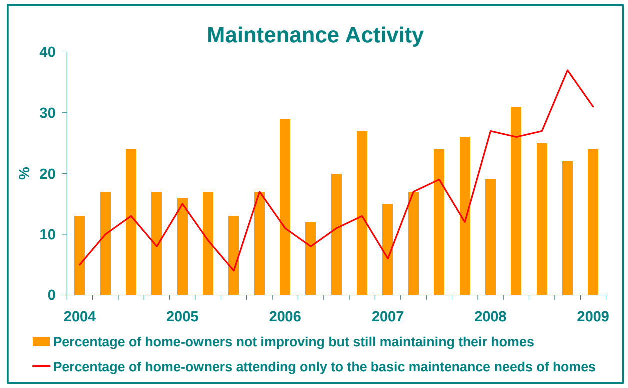
The percentage of homeowners believed to be undertaking investments in the property aimed at increasing the value of the property declined further in the 1st quarter to 10% from 12% previous. This is down from 23% in the same quarter a year ago.

In the next level down, where owners maintain and make limited improvements, 34% of the total is believed to reside here in the current quarter, which is a little up on the 27% of the previous quarter. Bear in mind some volatility in the numbers, and 34% of the total is still significantly down from near 50% at a stage in 2005.

Broadly-speaking, both of the above categories of maintenance/investment appear to be on a broadly declining trend. Not so in the case of the more basic maintenance categories.

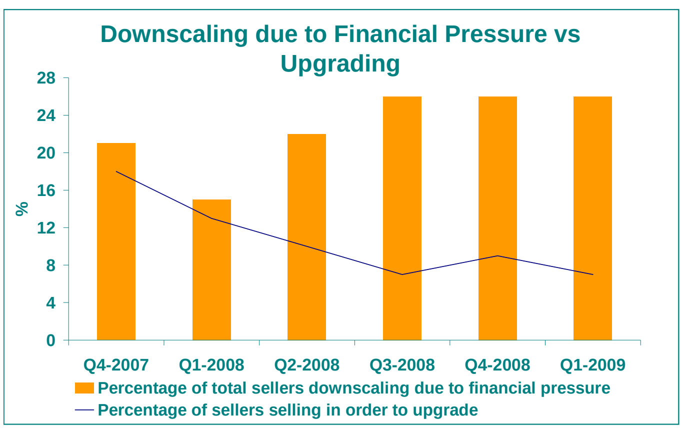
The percentage of owners not improving but still maintaining their homes was 24% in the 1st quarter, which is well-up from levels around 2005/06 that sometimes went as low as 12 -13%, while the percentage doing only basic maintenance on their homes was 31%, a far cry from a percentage as low as 4% at a stage of 2005.





SELLING IN ORDER TO DOWNSCALE DUE TO FINANCIAL PRESSURE CONTINUES UNABATED

With emigration selling having declined as a percentage of total selling over the past 2 quarters, downscaling due to financial pressure is now by far the single-most important reason for selling according to the survey respondents. The percentage of total sellers believed to be doing so in order to downscale due to financial pressure remained at 26% for the third consecutive quarter after having risen significantly in the first half of last year.



A second reason for selling which also points to the "back to basics" approach of the household sector is the percentage of total sellers selling in order to upgrade. This has declined to 7% by the first quarter of 2009, comparing poorly to the 18% estimated in the final quarter of 2007 when we started this line of questioning.

So, whereas downscaling due to financial pressure was similar in scale to upgrading, the market is very much a "net downscaler" these days (ignoring the other non-cyclical reasons for selling such as crime or life-stage etc).

Downscaling due to financial pressure is believed to get worse as a percentage of total as one moves from high income areas to lower income areas, with lower income areas (self-defined by estate agents) showing 33% of total sales estimated to be downscaling due to financial pressure.

Reasons for selling (As % of Total Sales)	Total	High Net Worth	Upper income	Middle income	Lower income
Downscaling due to financial pressure	**26%**	**23%**	**22%**	**29%**	**33%**
Downscaling with life stage	19%	17%	22%	18%	17%
Emigrating	**11%**	**14%**	**11%**	**8%**	**10%**
Relocating within SA	6%	7%	6%	5%	5%
Upgrading	**7%**	**8%**	**8%**	**6%**	**7%**
Moving for safety and security reasons	10%	12%	8%	12%	10%
Change in family structure	14%	13%	17%	14%	12%
Moving to be closer to work or amenities	7%	6%	6%	8%	6%

It would also appear that downscaling is slightly worse in the major coastal regions, notably KZN and the Western Cape, compared to Gauteng. This may be reflective of greater house price inflation, and thus affordability deterioration, in these 2 coastal regions during the boom years.

Reasons for selling (As % of Total Sales)	Jhb	Pta	KZN	W. Cape	E. Cape
Downscaling due to financial pressure	**23**	**26**	**29**	**31**	**26**
Downscaling with life stage	17	11	16	33	17
Emigrating	**9**	**15**	**16**	**7**	**8**
Relocating within SA	5	6	6	5	6
Upgrading	**8**	**5**	**8**	**8**	**3**
Moving for safety and security reasons	12	17	6	5	12
Change in family structure	16	13	18	8	14
Moving to be closer to work or amenities	9	6	1	4	14

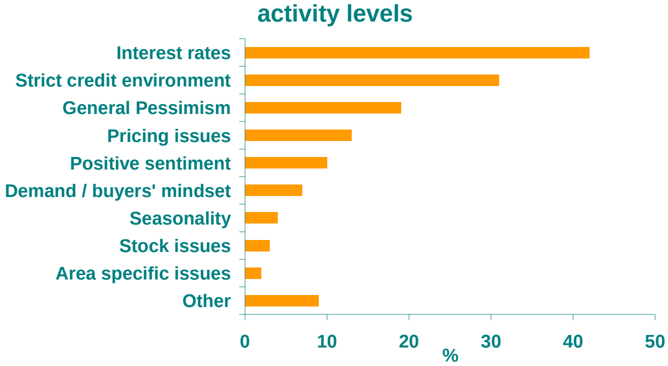
SECTION 3: BAROMETER OUTLOOK

41% of agents expect activity levels to increase further in the second quarter, compared to only 25% in the first quarter a year ago. The start of interest rate cuts, and expected further cuts, is the key driving force behind this more positive expectation at the start of 2009. 42% of agents surveyed indicated interest rates as an important factor in driving their future expectations, 33% citing rates as a positive factor, 6% said they were "wary" about future rate moves, while 3% cited rates as a negative factor because they were too high at current levels.

31% of agents cited strict credit criteria as a factor driving their near term expectations, and this was generally seen as a negative factor, especially the higher deposit requirements implicit in recent stricter loan-to-value ratio upper limits.

19% saw the "air of general pessimism" as a significant negative factor, with concerns regarding global and local economic recessions, and resultant retrenchments.

Factors that influence perceptions of future activity levels



13% saw pricing as a significant issue, with some still suggesting that prices were too high.

10% experienced a positive sentiment, and saw this as a key factor in determining their near term expectations, but it would seem that those who experienced a general negative sentiment outweigh those who experience positive sentiment.

Note: Bear in mind that agents can name more than 1 factor as important in driving their future expectations, so the factors highlighted in the bar graph exceed 100%.

What insights does FNB derive from the barometer? While demand is said to be recovering, much of the rest of the Barometer survey results still point to large-scale financial pressure amongst homeowners. Selling to downscale is high and not appearing to subside just yet, selling in order to upgrade is low, renovations and maintenance to homes are said to be increasingly limited to the essentials, non-essential holiday home and buy-to-let buying remains on the back foot, and first time buying too is a far cry from yesteryear.

As such, the survey may be just starting to support the FNB view of demand being able to respond in a mildly positive way to actual and prospective interest rate cuts, despite a bleak economic environment. However, it also supports our view that the significant oversupply on the market is not set to disappear immediately. It could therefore be a considerable time before oversupplies are mopped up and the market is back in balance, and this results in the expectation of continued house price deflation for most of 2009.

Box 2: A note on some of the factors that a bank has to take into account in the current environment when setting credit policy

The Property Barometer survey shows agents often citing banks' stringent lending policies as negatively impacting on the housing market's performance. But banks have their own risk considerations to make which often differ from those of a long term property investor, and these deserve mention.

3 important factors must be considered in the lending approach:

1. A substantial portion of all loan defaults occurs in the early stages of the loan, within 1-1.5 the years after the commencement of the term of the mortgage loan.

2. When a loan defaults shortly after commencement, its loan-to-value ratio is normally still relatively high. This is a significantly worse situation for the bank to be in, compared with a loan defaulting some years further down the line. This is because further down the line a more significant portion of capital has been repaid and there has normally been some capital growth in the house, thereby reducing the loan-to-value ratio significantly.

3. At present, banks are staring at widespread near term house price decline.

From the abovementioned 3 points, it becomes obvious that, unlike many property investors who are in the game with a long term horizon (and are often happy to hold their stock and wait it out), banks have to focus very strongly on the near term, and strategies that mitigate risk in the near term. This is because the loss in the case of default is likely to be more severe on a loan that defaults shortly after commencement as opposed to one that defaults further down the track where the loan-to-value has normally declined significantly, while the risk of default also declines as the loan ages and the repayment-to-income ratio declines.

The FNB Property Barometer does point to some recovery in demand, and indeed we anticipate more mild recovery in the near term as interest rates get cut. But the Barometer also tells us that there remains widespread selling in order to downscale due to financial pressure, suggesting that financial stress will take some time to go away and that an oversupply that has developed on the market will also not disappear overnight. It could thus be some time before demand gets back into balance with supply in order to precipitate the end of house rice deflation. Banks, therefore, need to consider the risk that loan-to-value ratios can actually rise in the near term due to house price deflation, implying significant losses on loans that default early in their term. Hence, the recent reduction in loan-to-value ratio limits on loans granted.

In addition, despite interest rate cuts, there is currently the spectre of recession and job loss, as a result of the global economic crisis which is impacting negatively on SA's export sector. Widespread job loss contributes to the risk of default on home loans, and can partly offset the relief that households get from interest rate cuts. What comes out strongly in the Barometer survey is that the overwhelming majority of agents still believe that incomes have got far behind house prices, and indeed in such troubled economic times it is realistic to believe that affordability is still an issue for a still financially stressed financial sector. Sound lending principles dictate that banks consider affordability, and although lower interest rates should improve this situation in the coming months, it would appear that we're not our of the woods yet.

Finally, while stringent lending criteria of banks as a group can admittedly contribute to constraints on the performance of the property market, it is important to realise that South African banks operate in a competitive situation and don't co-ordinate efforts. In addition, in an open economy such as SA's, there are many external (global) influences on the economy, and thus on the housing market, over which a banking sector has no influence (Think of exports, which are over a third of size the economy, and have a huge influence on employment and thus housing demand). Therefore, any single bank is largely a price taker, as opposed to a price setter in the housing market. This implies that lending strategies would essentially remain largely reactive to market conditions or expected market conditions, as opposed to attempting the near-impossible and the dangerous, i.e. trying to drive market performance.