PROPERTY BAROMETER

The May SARB Leading Business Cycle Indicator points to further possible weakness for the residential mortgage market

27 July 2011

With oil prices still troublesomely high, the global impact of QE2 (the second round of US quantitative easing) wearing off, and a lack of further interest rate cutting locally, yesterday's news that the May SARB Leading Business Cycle Indicator had weakened further came as little surprise. On a month-on-month basis, the indicator showed negative growth for the 3rd consecutive month to the tune of -1.6%

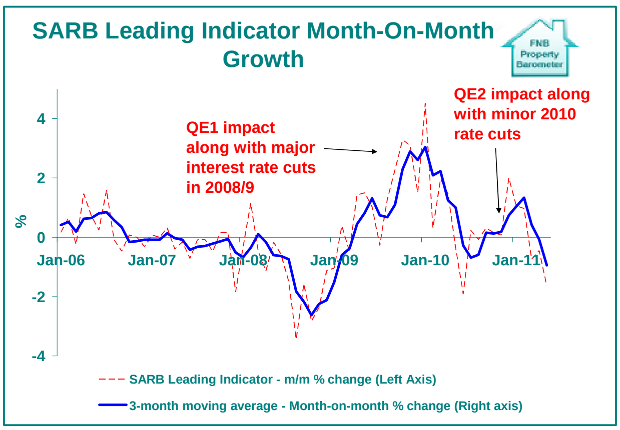
On a year-on-year basis, the indicator also entered slightly negative growth to the tune of -0.08%. The significance of this for the residential property market is that the growth rate in the value of new residential mortgage loans granted tracks the Leading Indicator trend quite closely, with residential mortgage grants growth trends also typically "leading" the business cycle.

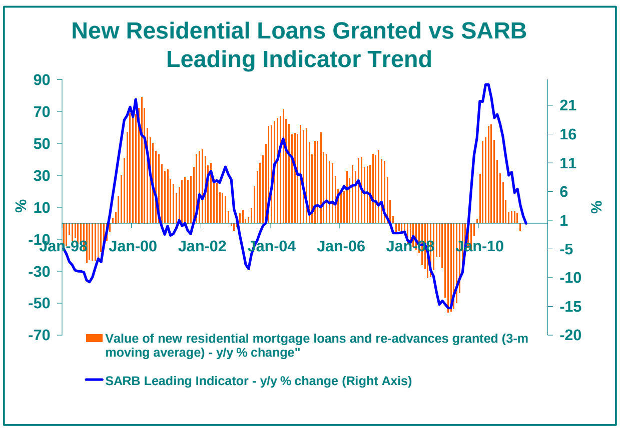
The extent of the correlation between the two is witnessed in the bottom right hand graph, where the year-on-year growth in value of new residential loans and re-advances granted has also been steadily slowing since around mid-2010, dropping into negative growth territory by March 2011 (-4.8% using a 3-month moving average).

The explanation behind the simultaneous decline in growth rates of the 2 indicators is that a deteriorating economy implies pressure on household sector income growth. This, along with a lack of further interest rate cuts implies nothing significant to further improve households' ability to pass the affordability criteria required to obtain a home loan.

While it is difficult to use the SARB Indicator as an indicator with which to predict the movement of another leading indicator, the economic environment that has led to its weakening does not look good. In the USA, the August 2nd deadline to raise the legal government debt ceiling to avoid defaulting sees that country at risk of having a downgrade in its credit rating. Even should it manage to raise the ceiling in time, there appears a general recognition by its policy makers that fiscal deficit reduction in order to reduce its borrowing requirement is needed, and this is a negative for the world's largest economy. On top of this, the US remains the main oil guzzler, and oil prices remain stickily high. No surprise that key global leading indicators have seen growth rates tapering. Domestically the SARB has had interest rates on hold since November, and the stimulus is wearing off, while the household sector is busy rebuilding its balance sheets..

Further slowing in growth in the May Leading Indicator, and even beyond, should therefore come as no surprise given the state of some of the world's biggest economies, along with a lack of monetary stimulus at home. For the residential mortgage sector, it probably means more weakness to come in the near term.





JOHN LOOS:
FNB HOME LOANS STRATEGIST
011-6490125
John.loos@fnb.co.za

EWALD KELLERMAN:
PROPERTY MARKET ANALYST
011-6320021
ekellerman@fnb.co.za