2 July 2012

PROPERTY BAROMETER
–FNB HOUSE PRICE INDEX – JUNE

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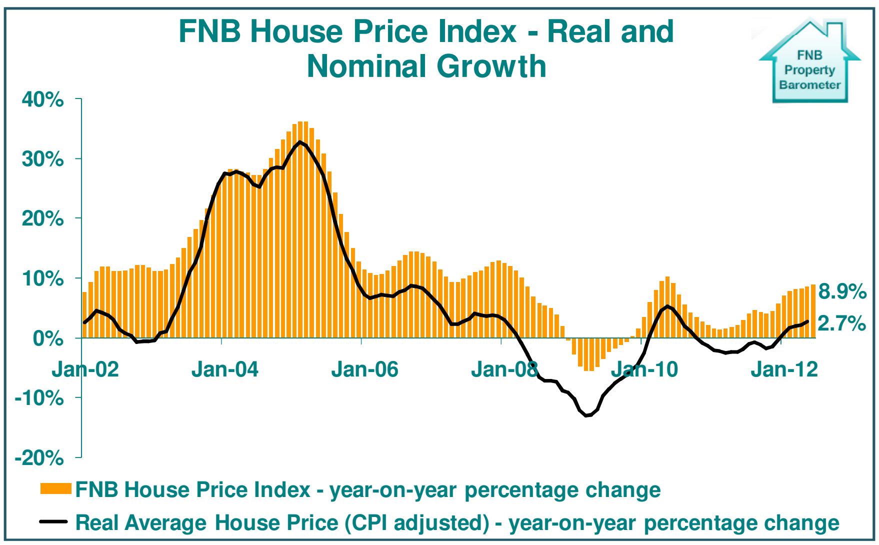
June FNB House Price Index shows further year-on-year rise, but peak is near as month-on-month growth slows for the 5th consecutive month.

YEAR-ON-YEAR HOUSE PRICE GROWTH ACCELERATED FURTHER IN JUNE, BUT MONTH-ON-MONTH WE ARE SEEING FURTHER LOSS IN GROWTH MOMENTUM

The FNB House Price Index showed a further acceleration in June, in year-on-year growth terms, from a revised 8.6% rate in May to 8.9% in June. This is the highest year-on-year growth since June 2010.

In real terms, too, as at May the index showed a mild increase to the tune of +2.7% year-on-year, with consumer price inflation in that month having come in at 5.7%.



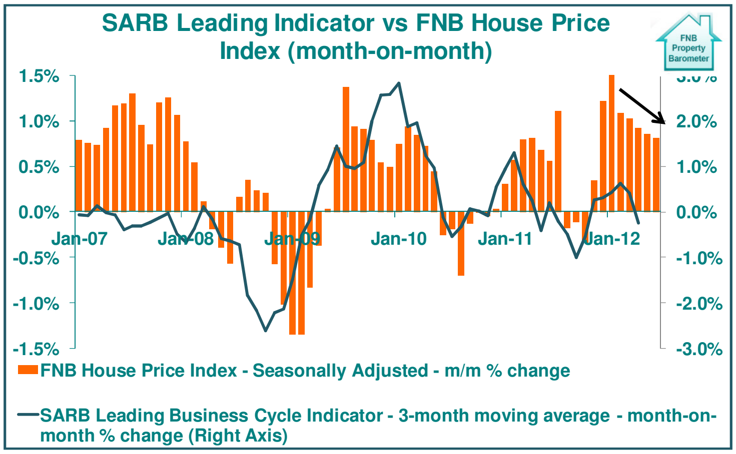
This means that since the real "boom-period" house price peak reached in February 2008, real house prices (house prices adjusted for CPI inflation over the period) were -12.6% lower at May 2012, although in nominal terms they were +15% higher than February 2008 as at June 2012.

However, compared to price levels at the inception of the FNB House Price Index back in July 2000, real prices were 70.2% higher as at May 2012, while nominal price were +236.6% higher as at June 2012.

The recent mild resurgence in house price growth comes largely as a result of a late-2011 strengthening in the domestic economy after 2 weak Winter quarters in 2011.

However, a better way of examining recent house price growth momentum is on a month-on-month basis, using seasonally-adjusted data.

Here, we have begun to see a gradual loss in house price growth momentum since a revised peak in January 2012. From a peak of 1.65% in January, month-on-month seasonally-adjusted house price growth has slowed to 0.82% by June.

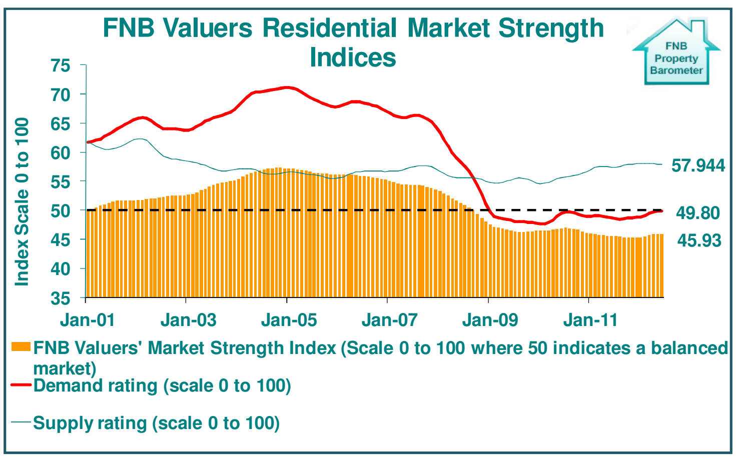


This slowing month-on-month growth trend suggests that a peak in the year-on-year house price growth rate should be reached soon. The recent month-on-month house price growth slowing also appears to be reflective of a housing market that is tracking short term fluctuations in the economy, and signs that economic growth in South Africa is slowing.

Already we have seen real economic growth, on a quarter-on-quarter annualized basis slow from a mini-peak of 3.2% in the 4th quarter of 2011 to 2.7% in the 1st quarter of 2012.

And plotting the 3-month moving average of the Reserve Bank Leading Business Cycle Indicator's month-on-month growth against month-on-month growth in house prices, we see the Indicator also having begun to slow in March and April, declining by -0.2% as at April.

Recent FNB Valuers' Market Strength Index rise confirms recent relative market strength, but….



The FNB Valuers' Market Strength Index, a barometer of our valuers' perceptions of market strength, remained virtually unchanged at 45.93 in June, after some improvement in the 5 months up to and including May.

The Market Strength Index is more of a co-incident to lagging indicator, as opposed to being a leading indicator of price trends, but is useful as a confirmation of a price trend.

The 5 months of increase prior to June's stalling were thus supportive of the recent period of more solid price growth. The improvement in the Market Strength Index (which represents the difference between the valuers' demand strength rating and their supply strength rating) up until May was the net result of a decline in the Valuers' Supply Rating as well as a rise in the Demand Strength Rating.

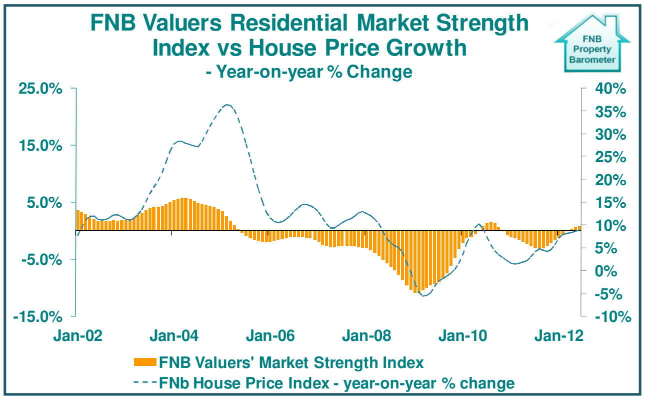
…… its pace of improvement has slowed.

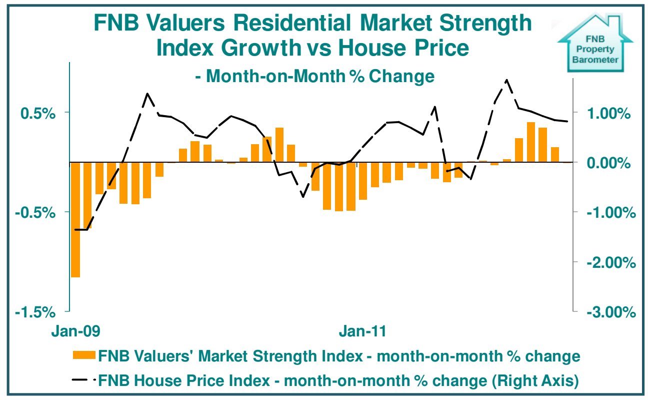
Examining the FNB Valuer's Market Strength Index rate of growth makes its trends a little more visible to the naked eye.

In year-on-year change terms, the Market Strength Index turned to positive growth by April, after seeing its rate of decline steadily diminishing from late in 2011. This trend is much in line with the improving trend in year-on-year house price growth.

In month-on-month growth terms, the Valuers' Market Strength Index has seen its growth rate fall from a mini-peak of 0.7% in March to 0% as at June, thus seemingly "supportive" of the slowing month-on-month growth trend in the FNB House Price Index.

In short, therefore, FNB's valuers have perceived the market to have strengthened during the summer of 2011/12, but they have also seen the pace of improvement in the market slowing in the recent months to June.





CONCLUSION

While house price growth on a year-on-year basis accelerated further to 8.9% in June, a loss of month-on-month price growth momentum over the past 5 months suggests that the year-on-year growth peak in the FNB House Price Index is not far off.

Various economic data released in recent months suggest that the housing market is set to head into a "softer patch" again. Economic growth slowed mildly in the 1st quarter of 2012, and various global and domestic data point towards further slowing in the current quarter.

In June, some of the national high frequency data releases also pointed to economic slowing. Real retail sales released for April showed further decline in year-on-year growth to 4.7% on a 3-month moving average basis, from a previous month's 5.9%. The Manufacturing Purchasing Managers' Index declined for the 3rd consecutive month in May. StatsSA manufacturing stats for April showed a mere 0.8% year-on-year growth on a 3-month moving average basis, further down from a 1.2% growth rate in the previous month. And Mining production declined year-on-year by a massive -10.6% in April on a 3 month moving average basis.

While economic slowing, globally and locally, looks as if it is becoming reality, resulting in declining inflationary pressure, and indeed the CPI inflation rate declined in May to 5.7% (from 6.1% previous), the Reserve Bank continues to keep interest rates unchanged since late-2010, thus not yet offering any new stimulus.

All considered, therefore, a weakening economic environment, coupled with no new interest rate stimulus (reduction) to date, suggests that the recent slowing trend in month-on-month house price growth will continue in the near term, and that this will soon translate into slowing year-on-year house price growth.

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:*

o *Less than 2 bedroom (Weight – 0.0718)*

o *2 Bedroom (Weight – 0.2106)*

o *3 Bedroom (Weight – 0.101)*

o *4 Bedrooms (weight – 0.0031)*

o *More than 4 Bedrooms (Weight – 0.0002)*

- *Full Title:*

o *Less than 2 Bedrooms (Weight – 0.053)*

o *2 Bedrooms(Weight – 0.1092)*

o *3 Bedroom(Weight – 0.3561)*

o *4 Bedroom (Weight – 0.0811)*

o *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.*

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.*