PROPERTY INSIGHTS

2019 Property-Related Focus Areas – Residential Market Segment performances "converging"??

We ponder the next potential 2019 property theme…the Lower Income Area end's "outperformance" fading away.

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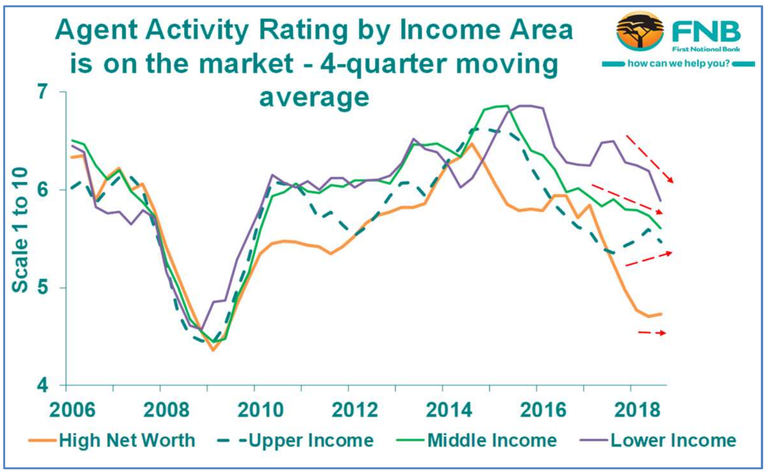
JOHN LOOS:
PROPERTY SECTOR STRATEGIST
087-328 0151
john.loos@fnb.co.za

We continue on our look ahead to 2019 for likely "key themes" that may play out in the course of next year. Often in a property cycle we see the higher priced end of the Residential Market leading the downturn and the lower end "catching down" later. After a relatively good period in a property cycle, the high priced end can be the first segment to run into home affordability challenges, the lower priced areas having "more legs" as a portion of home demand shifts downward from higher priced end to middle or lower priced areas in search of greater affordability. But ultimately economic stagnation will normally affect all segments. Lower income households may be more sensitive to economic and interest rate cycles due to their more limited financial buffers built up to "weather the storm.

So, while higher priced areas have had affordability challenges emanating from both the economy as well as sharp increases in municipal rates and utilities tariffs, after 6-7 years of broad economic stagnation, and with interest rates again starting to rise as 2019 approaches, we expect that 2019 will be a year in which the market performance gap between the Lower and Middle Income Area Segments on the one hand, and the High Net Worth and Upper Income Area Segments on the other hand (the latter 2 segments having "outperformed in recent years) may diminish and possibly even disappear.

The FNB Estate Agent Survey sees estate agent respondents "self-defining" the areas in which they operate into 4 categories, namely High Net Worth Areas (average price = R6.8m), Upper Income Areas (average price = R3.36m), Middle Income Areas (average price = R1.63m) and Lower Income Areas (average price = R1.05,m).

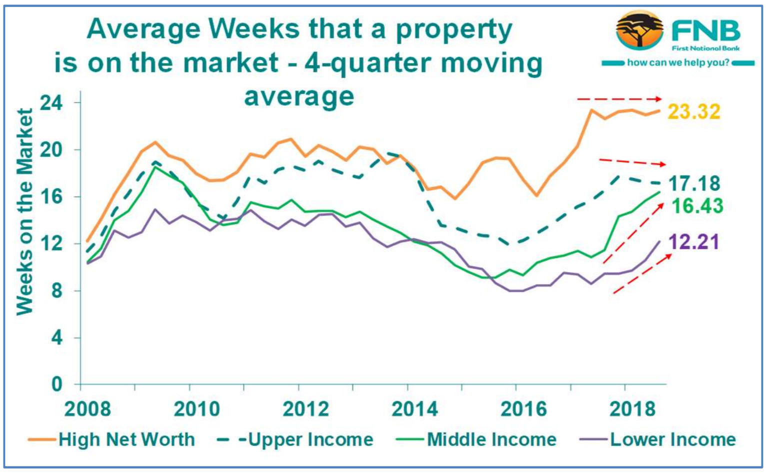
On a 4-quarter moving average basis (we use a moving average to smooth because sample size gets a bit small on a segment basis, for the 4 quarters up to an including the 3rd quarter of 2018, agents in the High Net Worth Areas



returned by far the lowest Market Activity Rating, i.e. 4.73 (on a scale of 1 to 10). The 2nd lowest rating was that of Upper Income Areas with 5.47, then came Middle Income Areas with a higher 5.61 and Lower Income Areas with the highest rating of 5.89.

However, the High Net Worth and Upper Income Areas appeared to be stabilizing in recent times, after prior declines, while the Middle and Lower Income Area Activity Ratings have seen more noticeable recent declines. Quarter-on-quarter, the 4-quarter moving average Market Activity Rating for High Net Worth Areas actually rose by 0.6% in the 3rd quarter of 2018, the Upper Income Area Rating declined by -2.2%, the Middle Income Area Activity Rating declined by -2.3%, and the Lower Income Area Rating by a more significant -5%.

MARKET BALANCE STILL WEAKEST AT THE HIGH END BUT WEAKENING MORE NOTICEABLY AT THE MIDDLE TO LOWER END OF LATE



We also examining the balance between supply and demand in the Residential Market, as implied by trends in average time of homes on the market prior to sale.

Again, we use a 4-quarter moving average estimate for smoothing purposes.

Typically, the higher end areas see properties being on the market for longer than the lower priced areas, which can be regarded as a "structural feature of the market.

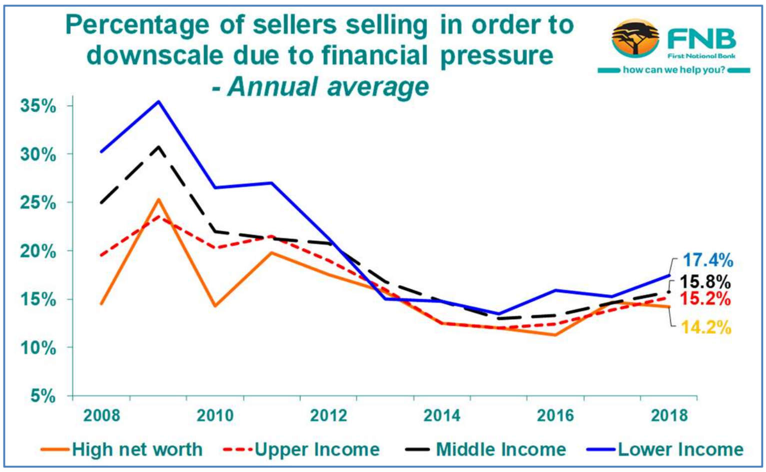
However, from around 2013 to 2016 we saw a noticeable widening in the gap between the High Net Worth and Upper Income Areas' estimated times on the market on the one hand and those of the Middle and Lower Income Area Segments on the other, the latter having significantly lower average times on the market.

But more recently, as the Higher End shows signs of "stabilizing" and the Lower End weakens, we have once again seen a narrowing in the gap between average times on the market by income area segment. The 4-quarter average estimated time on market for the High Net Worth Areas was the longest at 23.32 weeks as at the 3rd quarter of 2018. However, this average had moved almost sideways since an average of 23.4 weeks as at the 2nd quarter of 2017. The Upper Income Area average time on market was 17.18 weeks as at the 3rd quarter of 2018, which is a mild decline (strengthening) from the 17.5 weeks as at the 1st quarter of 2018.

By comparison, the Middle Income Area estimate was 16.43 weeks as at the 3rd quarter of 2018, up (weakened) from 10.8 weeks as at the 2nd quarter of 2017, while the Lower Income Area estimate was 12.21 weeks, the lowest but also significantly weaker than the 8.6 weeks as at the 2nd quarter of 2017.

So, while one could still argue that the Middle-to-Lower Income Area end is still a stronger part of the market than the Hight Net Worth-Upper Income Area end, the key indicators suggest a narrowing in the performance gap as the Middle-to—Lower Income Area end weakens more recently.

FINANCIAL PRESSURE APPEARS TO BUILD SLIGHTLY MORE AT THE LOWER END



We have said that the Lower Income Segment may begin to see its households become more financially pressured than the Higher Income Area Segments, the latter often having more financial buffers to help it through a weak economic period.

We examine a key question in this regard in the FNB Estate Agent Survey, i.e. the estimated percentage of total sellers that are selling their homes in order to downscale due to financial pressure. We have recently been seeing hints that financial pressure in Lower Income Areas may be "picking up" a little more significantly than at the higher end. For 2018 to date, the percentage of home sellers believed to be downscaling due to financial pressure has averaged 17.4% for the Lower Income Area Segment, up from 15.2%

average for 2017. In Middle Income Areas, the increase has been mildly less significant from 14.6% in 2017 to 15.8% in 2018 to date, while the Upper Income Area Segment also saw a more moderate increase from 13.8% to 15.2% over the same period. The High Net Worth Area Segment actually saw a decline in the estimate in 2018, from 14.7% in 2017 to 14.2% in 2018 to date.

The rotation in relative performances is a gradual one, but at the housing cycle high point in 2013, the year before the start of interest rate hiking in 2014, and before the economic growth performance had stagnated too far, Lower Income Areas had the lowest estimated downscaling due to financial pressure of the 4 area segments.

Going back further to the intense economic and interest rate pressures of 2008/9, the Lower Income Area financial pressure-related downscaling percentage peaked at 35.4% in 2009, Middle Income Areas at 30.8%, Upper Income Areas at 23.5% and High Net Worth Areas at 25.3%. It was from that severe pressure period that we learnt that Lower Income Areas could experience significantly higher financial pressure/stress than higher end areas in weak economic periods.

The more recent economic downturn has been a "slow puncture", and not nearly as severe to date as the short sharp recession of 2008/9 with its more significant rate hiking peak.

CONCLUSION

In short, in the initial stages of the housing market slowdown, starting around 2014, it was the higher income end of the housing market that appeared to lead the way "down". More recently, however, it appears that the High Net Worth and Upper Income Area Segments have been showing signs of "relative stabilisation", albeit at already-weak levels, while the Middle and Lower Income Area Segments have been weakening more noticeably from their relatively stronger levels. This can be a sign that financial constraints and pressures amongst households at the Lower End are becoming more significant, and this can become a "relative drag" on these segments' performance.

Therefore, a key theme in 2019 may be a "convergence" in performance of the various income/price segments of the housing market, the Lower-to-Middle End's relative "outperformance" fizzling out.