PROPERTY INSIGHTS

FNB House Price Index

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Ongoing slow house price growth will keep Residential Building Sector under pressure

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September 2018 saw the FNB House Price Index growing by a slightly faster 4.4%, year-on-year, up from the previous month's revised 4.1%. However, this still translates into ongoing decline in prices in "real" terms (adjusted for CPI inflation), a trend that has been ongoing since early-2016.

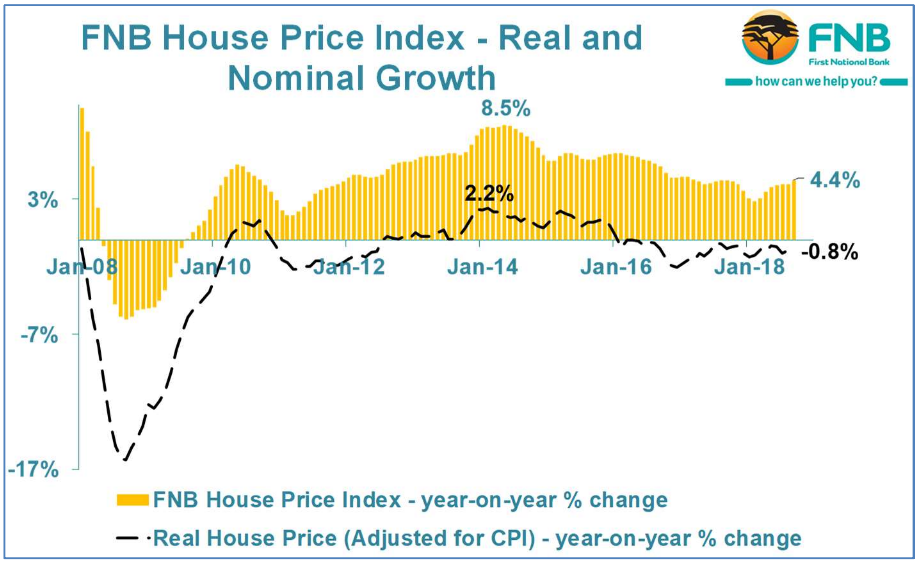
FNB HOUSE PRICE PERFORMANCE

LOW SINGLE DIGIT HOUSE PRICE GROWTH CONTINUES, WITH NO STRONG DIRECTION

On a year-on-year basis, the FNB House Price Index for September showed a slight strengthening in its growth rate, from a revised 4.1% in August to 4.4%.

The revised figures show a mild acceleration in recent months, but the theme remains a stagnant market with low single digit growth which translates into ongoing gradual real price decline, "real" referring to the rate of change after adjustment for CPI (Consumer Price Index) inflation.

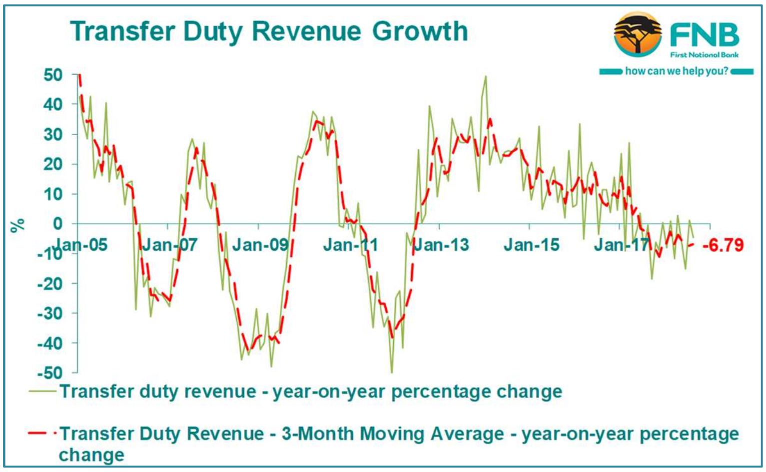
At 4.9% in August (CPI for September not yet available), the 4.1% house price inflation rate in that month translated into a -0.8% year-on-year real house price decline.



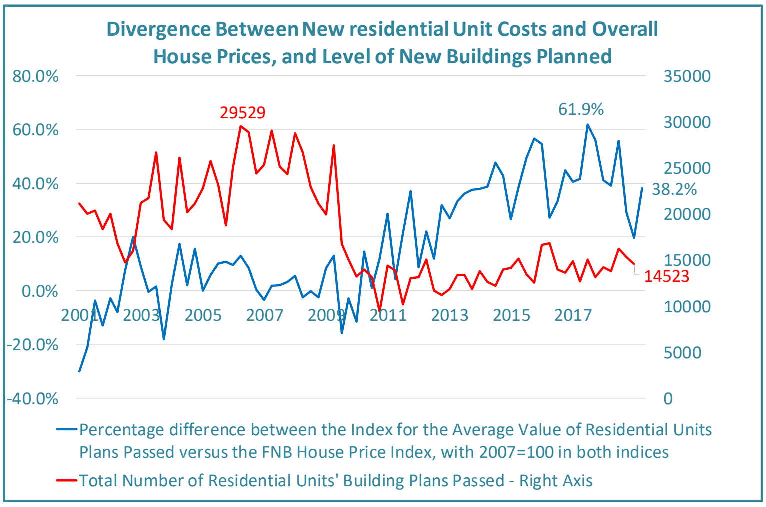
Therefore, the most recent house price data, despite some mild upward move in nominal growth, remains in real price "correction" mode, as it has since early-2016, which is reflective of a weak economy causing a gradual residential market shift away demand-supply equilibrium.

This move away from equilibrium has been seen in a gradual lengthening of the average time of homes on the market prior to sale in recent years, as per the FNB Estate Agent Survey.

The 2018 year to date average house price growth is 3.7% year-on-year, which continues to point to the likelihood that 2018 will be a slower price growth year than 2017's 4.3%, the 4th consecutive year of slowing nominal price growth, and the 3rd consecutive year of real price decline.



The consequences of a weak Housing as well as Commercial Property Market have been felt by the fiscus, with property transfer duty revenues having been largely in negative growth territory in recent times. For the 3 months to August, transfer duty revenues declined year-on-year by -6.79%., this 3-month moving average having been in decline since mid-2017.



The slow price growth in the overall home market (dominated by the existing home market) also continues to make it challenging for the New Residential Development Sector to bring competitively priced stock to the market.

Since 2007, the end of last decade's residential building boom, the average value of residential units' plans passed has inflated by 112% up to the 2nd quarter of 2018, and those units recorded as completed have inflated by 183% over the same period. By comparison, the FNB House Price Index, which is overwhelmingly dominated by the existing home market, has only inflated by 53.5% since 2007.

This slow existing home price growth relative to new home cost growth has kept new building volumes relatively low over the past decade, with the 2nd quarter level of units plans passed at 14,523, around half the number being built at stages of 2006/7.

The ongoing low single digit house price growth is likely to keep the New Residential Development Sector under pressure in the near term, doing little to allow new development costs to narrow the gap with existing home prices.

ADDENDUM - NOTES:

Note on The FNB House Price Index:

The FNB Repeat Sales House Price Index has been one of our repertoire of national house price indices for some years, and is based on the well-known Case-Shiller methodology which is used to compile the Standard & Poor's Case-Shiller Home Price Indices in the United States.

This "repeat sales approach" is based on measuring the rate of change in the prices of individual houses between 2 points in time, based on when the individual homes are transacted. This means that each house price in any month's sample is compared with its own previous transaction value. The various price inflation rates of individual homes are then utilized to compile the average price inflation rate of the index over time.

The index is compiled from FNB's own valuations database, thus based on the residential properties financed by FNB over the past 18 years.

We apply certain "filters" and cut-offs to eliminate "outliers" in the data. They main ones are as follows:

- The maximum price cut-off is R15m, and the lower price cut-off is R20,000.
- The top 5% of repeat sales price growth rates, and the bottom 5% of growth rates are excluded from the data set.
- Repeat transactions that took place longer than 10 years after the previous transaction on the same home are excluded, as are repeat transactions that took place less than 6 months after the previous transaction on the same home.
- 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.