

Economic Strategy

South Africa: Residential Property Viewpoint

Sustained recovery at risk

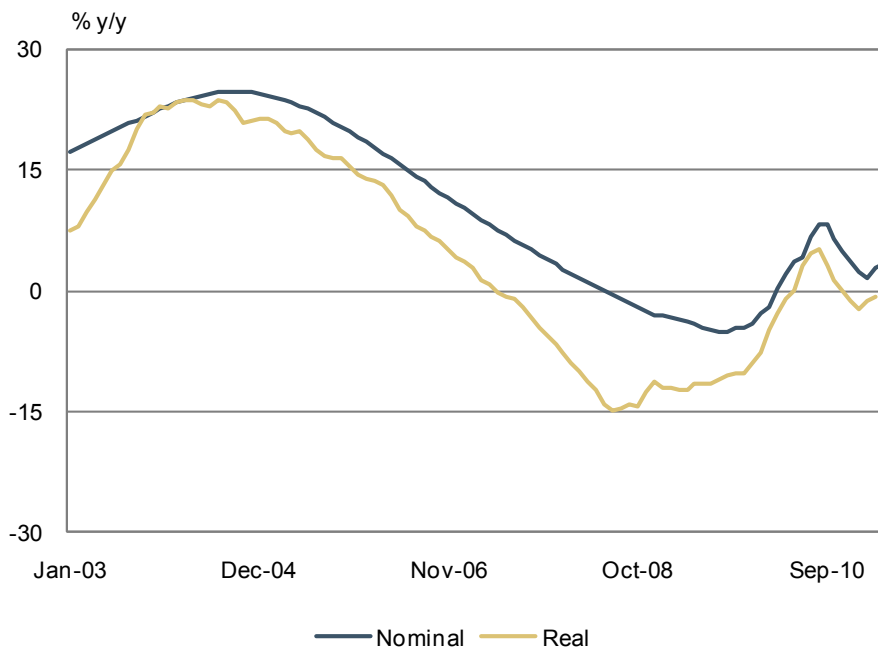
4 May 2011

- **Standard Bank's median house price recorded a growth rate of 3.4% y/y in April 2011, from 2.9% y/y in March 2011.**
- SA's economic recovery is on a delicate footing, with improvements in business confidence and the manufacturing sector being offset by stalling employment growth and declining consumer confidence.
- An erratic labour market and increasingly stringent environment faced by consumers will further dampen consumer confidence as well as depress prospects for a sustained recovery in the residential property market.

Research Analyst

Sibusiso Gumbi*
Sibusiso.Gumbi@standardbank.co.za
+27-11-3787228

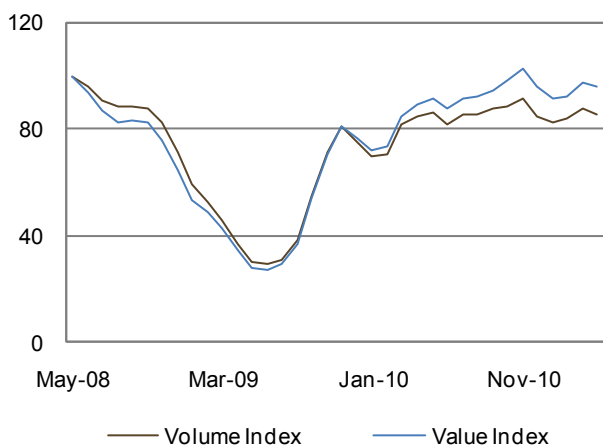
Standard Bank median house price growth



Source: Standard Bank Research

Standard Bank’s median house price (smoothed) saw a moderate uptick in April, recording a 3.4% y/y growth rate, from 2.9% y/y in March. However, m/m growth eased for the second consecutive month, to 0.3% (from 0.8% in March), suggesting that y/y growth may owe its improvements largely to a depressed base and not to improving market conditions. The median house price in real terms remains in negative territory. Both the volume and value of applications received exhibited moderate m/m declines in April (Figure 1).

Figure 1: Application index — smoothed (2008=100)



Source: Standard Bank Research

The SA economy continues to exhibit mixed signs of improvement. South African retail sales growth saw an easing to 5.6% y/y in February, from 6.3% y/y in January. Growth in wholesale trade followed suit, easing to 3.4% y/y in February, from 7.6% y/y in January. The moderation in sales growth may be attributed to the fading of favourable base effects.

However, manufacturing production unexpectedly accelerated in February, rising by 6.0% y/y, from 1.6% y/y in January. The Kagiso/BER Purchasing Managers Index (PMI) stabilized at a fairly high level of 56.4 points during April, marginally lower than the 13-month peak of 57.2 index points achieved in March.

The SACCI business confidence index rebounded in March, rising to 88.3 pts, from a four-month low of 86.4 pts in February. This represents its highest reading since September 2008. The index assigns the rebound in *building construction* as a chief contributor to improving business confidence.

The value of buildings reported as completed to larger municipalities (at current prices) decreased by 0.2% y/y over the first two months of 2011. Larger decreases in the value of residential and non-residential buildings completed (-3.3% y/y and -16.9% y/y respectively) were offset by buoyant growth in *additions and alterations* (20.7% y/y) recorded over the corresponding period (Figure 2).

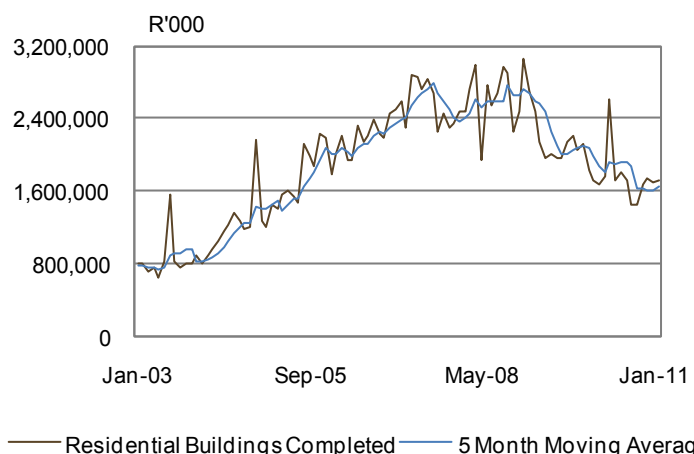
Key to the outcome of an improved housing market is the extent to which improvements in the economy translate to growth in employment and wages. The *employment* sub-index of the PMI did see an improvement to 49.0 points in April; however, it remained below the key 50 level, indicating that the sector had continued to shed jobs in April.

This unfavourable statistic is mirrored by data from Statistics South Africa’s Quarterly Labour Force Survey. The data shows that South Africa’s unemployment rate rose in Q1:11 to 25.0%, from 24.0% in Q4:10. The rise was a consequence of the economy shedding 14,000 jobs in Q1:11, compared to an increase of 156,000 jobs in Q4:10. Sectors such as *mining, manufacturing, and finance and other business services* contributed positively to job creation. These gains, however, were offset by job losses in the *transport, trade, construction, and agriculture* sectors. Worryingly, the four aforementioned sectors account for approximately 40% of the total employed population.

SA’s erratic labour market may restrict momentum in household expenditure (which grew by 4.4% in 2010 from a contraction of 2.0% in 2009). Households have already seen growth in disposable income moderate slightly in Q4:10, with real disposable income growth easing to 5.3% q/q (saar), from 5.5% q/q (saar). This was indicative of a moderation in growth in employee compensation, which slowed to 9.1% y/y in Q4:10, from 11.5% y/y in Q3:10.

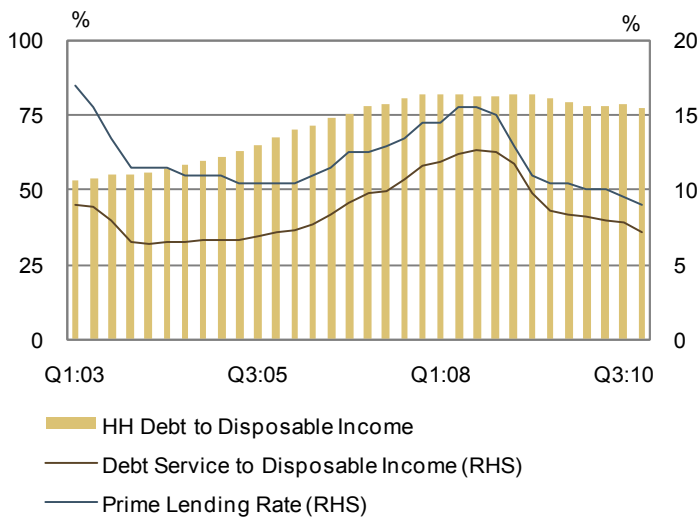
Consumer prices increased at a faster-than-expected rate in March. The CPI accelerated to 4.1% y/y (a nine-month high), from 3.7% y/y in February. Chief contributors to the increase included *administered prices* (which grew by 10.9% y/y in March), *housing and utilities* (6.6% y/y), *food and non-alcoholic beverages* (5.0% y/y) and *transport* (3.3% y/y). Standard Bank, while acknowledging the increasing risks to the upside, remains of the view that interest rates will remain the same for the duration of 2011, with a rate hike expected in Q1:12. The combination of steady low interest rates and improving household disposable income

Figure 2: Value of residential buildings reported as completed s.a.



Sources: Statistics South Africa; Standard Bank Research

Figure 3: Household debt profile



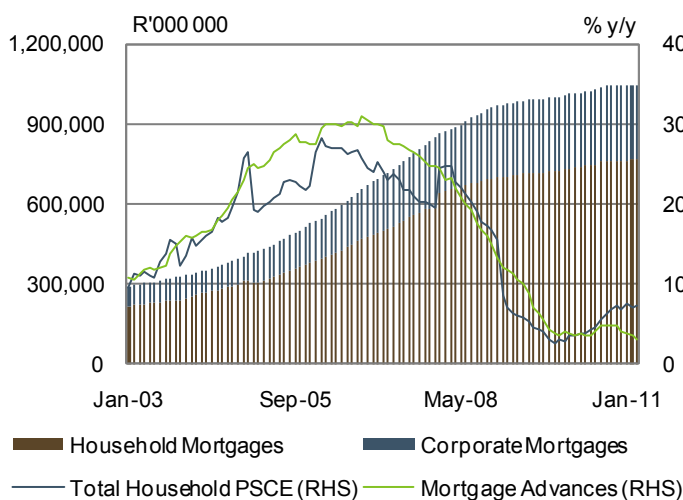
Sources: SARB; Standard Bank Research

may contribute to declines in the ratio of debt-servicing cost to disposable income (7.2% in Q4:10) as well as the ratio of household debt to disposable income (77.6% in Q4:10) (Figure 3).

Private sector credit extension growth unexpectedly slowed in March to 5.1% y/y, from 5.4% y/y in February (although credit extended to households did pick up, recording a 7.4% y/y growth rate in March, from 7.0% y/y in February). The moderation in total PSCE was driven largely by a further easing in mortgage advances (2.9% y/y in March, from 3.4% y/y in February) as poor appetite for credit by the private sector and high debt levels serve to depress prospects for a sustained improvement in credit extension (Figure 4).

Ever-increasing pessimism on the part of consumers regarding the long-term outlook for the economy may be contributing to the reluctance in purchasing big-ticket items such as houses (Figure 5). Consumer confidence as reflected by the

Figure 4: Private sector credit profile



Sources: SARB; Standard Bank Research

BER Consumer Confidence index, fell to 9 points in Q1:11 from 14 points in Q4:10. Notably, fewer consumers were confident about their financial position in a year's time and were less optimistic regarding the timing of durable goods purchases.

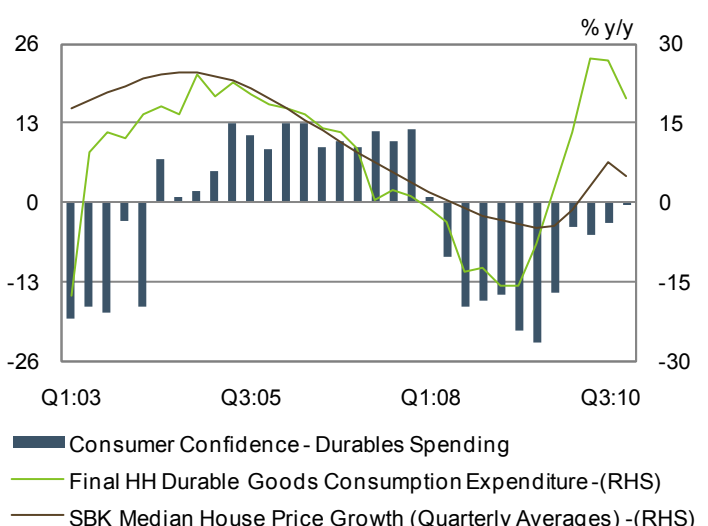
Current accommodative conditions (from a monetary policy standpoint) have not provided a catalyst for a pronounced growth in house prices. It appears consumer sentiment, and not interest rates exclusively, may prove vital in sparking demand.

The outlook for the economy may be best categorised as uncertain. The SARB's composite leading business cycle indicator gives a favourable outlook of the economy over the next 6 months, rising to 136.1 points in February, from a revised 134.7 points in January. This increase was driven by nine of the eleven sub-components of the index. In contrast, the *expected business conditions* sub-index of the PMI remained flat in April, amounting to the same 58.1 points (a nine month low) it recorded in March, with only 6 out of 10 (approximately) purchasing managers foreseeing an improvement in business conditions in the manufacturing sector over the next six months.

Notably, the residential building plans component of SARB's composite leading business cycle indicator contributed negatively to the indicator. The value of building plans passed for residential buildings (at current prices) fell by 3.5% for the first two months of 2011, compared to the corresponding period in 2010 (Figure 6).

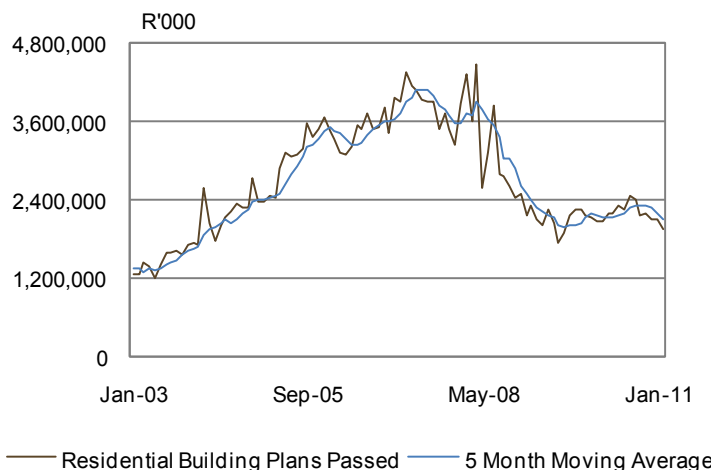
Standard Bank expects growth in aggregate household expenditure to maintain its momentum in 2011 (growth of 4.6% y/y is projected for 2011). However, the looming interest rate hiking cycle and its corresponding increase to the cost of debt could hinder this momentum, as the extent to which the deleveraging of debt has occurred has been minimal. One

Figure 5: Consumer confidence — durable goods spending



Sources: SARB; BER; Standard Bank Research

Figure 6: Value of recorded building plans passed, s.a.



Sources: Statistic South Africa; Standard Bank Research

should note that while indebtedness fell in relative terms (with a 1.1 pps decline in the ratio of household debt to disposable income in Q4:10), it ticked up slightly in absolute terms.

In addition, consumers are expected to face increasing price pressures. Inland prices for 95 octane unleaded petrol rose by 29 cents/litre on 4 May 2011, bringing prices above R10/litre for the first time since August 2008. Petrol is now R1.53/litre more expensive than a year ago, and nearly 71% more expensive than in January 2009.

SARB officials have stated, however, that they regard inflation as “contained”. This underscores Standard Bank’s view that the central bank will not hike lending rates as quickly as the market anticipates (in Q4:11). Standard Bank maintains the view that interest rates will be kept on hold throughout 2011. Economic growth prospects remain fragile (Standard Bank anticipates GDP growth of 3.8% y/y in 2011), and inflation is forecast to remain within the target band for the duration of 2011. Standard Bank expects the first interest rate hike to occur in Q1:12.

Standard Bank is of the view that growth in the residential property market in 2011 will track inflation, with zero or negligible growth expected in real terms. A shaky labour market and increasingly stricter conditions for consumers will dampen consumer confidence and depress prospects for a sustained recovery in SA’s residential property market.

Table 1: Standard Bank median house price growth

	Month-on-month change (%)	Year-on-year change (%)
2010		
January	0.4	-1.2
February	2.3	1.1
March	-1.4	2.2
April	4.5	3.1
May	1.4	2.5
June	2.3	3.6
July	0.8	7.3
August	0.6	8.1
September	-2.5	8.3
October	-0.7	6.5
November	-0.3	4.8
December	-0.1	3.6
2011		
January	-2.0	2.3
February	1.5	1.5
March	0.8	2.9
April	0.3	3.4

Source: Standard Bank Research

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