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Property Insights

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SARB Leading Business Cycle Indicator – Further decline in June SARB Leading Business Cycle Indicator reading suggests likely further new mortgage lending weakness.

John Loos:
Property Strategist

FNB Commercial Property Finance

Tel: 087-312 1351

Email:
john.loos@fnb.co.za

The June SARB Leading Business Cycle Indicator continued to point to likely economic weakness in the near term, declining month-on-month by a further -0.5%, after a -1.6% decline in May.

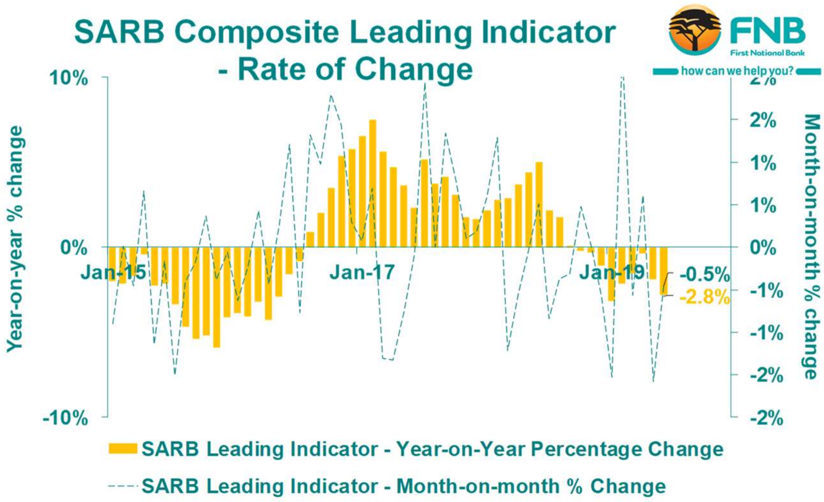
The month-on-month growth rates are volatile, however, and the year-on-year rates of change give a better idea of the broader trend. On a year-on-year basis, the Leading indicator declined by -2.8% in June, a greater magnitude of decline that the prior month's -1.9%, and the 9th consecutive month of year-on-year decline.

This once again moderates any expectations of a near term economic recovery, and suggests that both new mortgage lending growth as well as new property development may remain mediocre in the near term.

The Leading Indicator can be a useful near term indicator of economic growth direction, but also an indicator of near term new mortgage lending direction, new mortgage lending itself being a more leading component of the economic cycle.

From a mortgage lending point of view, therefore, the June Leading Indicator was a further disappointment, having declined significantly once again.

The list of negative contributors included certain global economic factors in the form of SA's export-related commodity prices, but more domestic factors, including job advertisements, new residential building plans passed, average hours per worker worked in Manufacturing, and the interest rate spread between Government 10-year and longer bond yields on the one hand and 3-month Treasury Bills on the other.

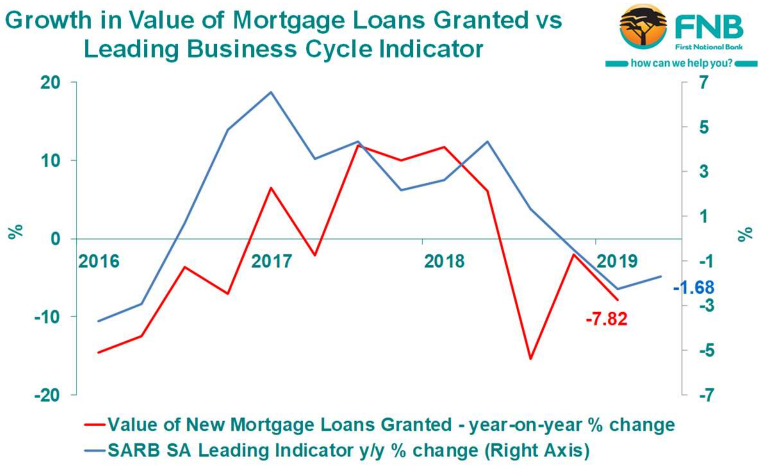


There were some positive contributors to the monthly indicator number, however, including Manufacturing Order Volumes, Real M1 Money Supply growth, the Leading Business Cycle Indicator for SA's Major Trading Partner Countries, and New Passenger Vehicle Sales.

So the indicators that serve as inputs in the Composite Leading Indicator were not all negative contributors, although the negatives outweighed the positives still.

Examining the Leading Indicator on a quarterly basis, the 2nd quarter's year-on-year rate of change was still negative to the tune of -1.68%, but mildly less so than the -2.3% rate of decline in the 1st quarter of 2019.

But it remains a reading that points to further likely near term weakness in growth in the value of new mortgage lending.



According to SARB data, growth in the value of new mortgage loans approved broadly tracked the Leading Indicator growth rate slower and into negative growth territory in the 2nd half of 2018, recording a year-on-year decline of -7.82% in the 1st quarter of 2019.

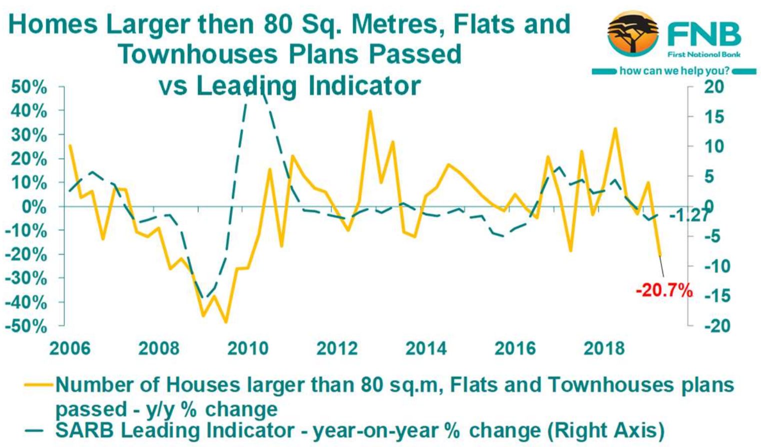
New commercial property mortgage loans approved were particularly hard hit, declining by .-29.6% in the 1st quarter, according to SARB data.

The 2nd quarter's further decline in the Leading Indicator suggests that a further weak quarter in new mortgage lending was experienced in the 2nd quarter of 2019, and this could spill over into the 2nd half of 2019.

One event that could change things slightly going forward is the commencement of SARB interest rate cutting last month, with new mortgage lending being interest rate sensitive. The one 25 basis point rate cut to date would probably not make a meaningful difference, but if followed up by more in the coming months one could conceivably see a return to some positive new mortgage lending growth later in the year.

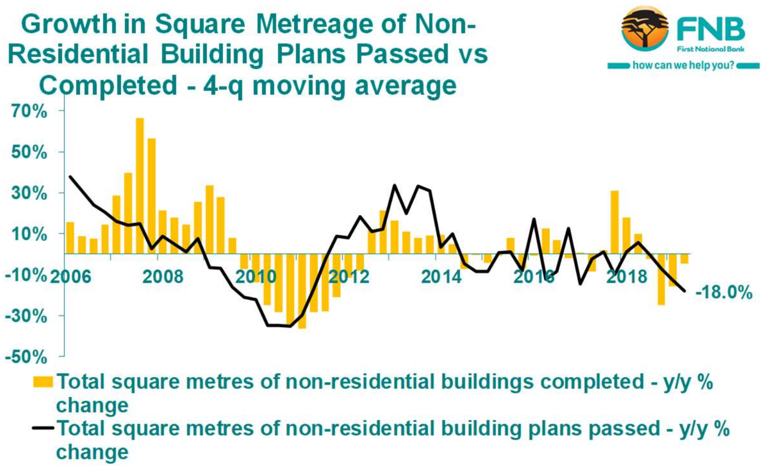
For the time being, though, the Leading Indicator doesn't point to any strong support for mortgage lending from the economy's performance just yet, with both global and local economic factors playing a negative role.

New Building Plans broadly track Leading Indicator weaker



One of the inputs into the Composite Leading Indicator is that of "Building Plans Passed for Residential Homes Larger than 80 square metres, Flats and Townhouses".

This data series is admittedly volatile, but showed sharp weakening in the 2nd quarter of 2019, declining year-on-year by 20.7%. This is its biggest quarterly year-on-year rate of decline since a stage of 2010.



While not an indicator used in the compilation of the Composite Leading Business Cycle Indicator, the rate of change in square meterage of Non-Residential Buildings is nevertheless highly sensitive to the cycle, and has also broadly tracked the Leading Business Cycle Indicator weaker of late.

Using a 4-quarter moving average for smoothing purposes, Square Metres of Non-Residential Building Plans Passed declined year-on-year by -18% for the 4-quarters to Q2 2019, a downward acceleration from the -12.8% decline of the prior quarter.

This reflects the Commercial Property Development Sector responding to the business cycle downward phase and the rising property vacancy rates that it has brought, notably in the Office and Retail Sectors.

In short, the SARB June Leading Business Cycle Indicator showed a greater magnitude of year-on-year decline than that of May, suggesting that economic weakness could spill over into the 2nd half of 2019. This is typically a "negative sign" for new mortgage lending and planned new property developments, these sectors usually "leading" sectors themselves and their growth direction thus often broadly tracking that of the Leading Indicator.

Indeed, this broad relationship appears to have held of late. We had seen new mortgage loans granted growth negative since late last year, although we don't yet have 2nd quarter 2019 new mortgage data. And both residential and non-residential building plans passed have recorded significant rates of decline in the 2nd quarter of 2019

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