January 2021

Property Barometer.

3.8%
y/y FNB HPI

9.4
weeks on market

49.25
FNB Valuers' Market Strength Index

Housing market showed resilience in 2020: What's in store for 2021?

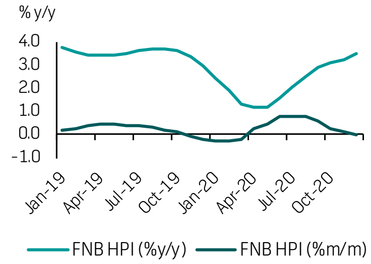
The pandemic had a profound impact on global output in 2020. Many economies experienced sharp recessions, unemployment spiked, and incomes stagnated. Yet, housing markets in major economies remained relatively unimpacted: we saw robust growth in buying activity and house prices continued climbing. This happened despite a rising number of infections and significantly weaker labour markets. Apart from pandemic-induced changes in housing needs (e.g., demand for bigger space to facilitate work-from-home), this disparity is explained by the sizeable stimulus packages (fiscal and monetary) deployed by different countries to fend off wider economic calamity. These included ultra-low interest rates, mortgage-repayment holidays and tax exemptions on property purchases. Naturally, these measures supported demand and, eventually, house prices.

South Africa's experience has not been dissimilar. Industry-wide data continues to show robust home-buying activity. In fact, 2020 is set to register the highest volume of mortgage approvals in over a decade. This is despite relative caution from lenders: approval rates were lower in 2020 compared to 2019.

Activity is propelled by lower interest rates, attractive market pricing, lower transfer duties and the changing housing needs due to the pandemic. The improved affordability made buying property more attractive than renting. In part, this explains the rising vacancy rates and subdued rental escalations, as landlords struggle to hold on to their good quality tenants. Another explanation is that job losses were more prevalent in low-paying occupations and for those employed on a non-permanent basis, who would generally not afford to buy property. Thus, the impact of the pandemic is more visible on the rental market than on home-buying market.

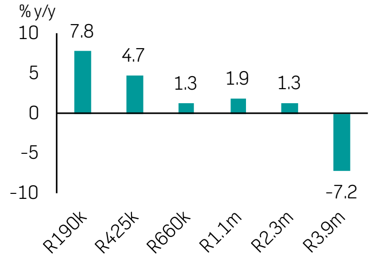
From a price growth perspective, the FNB HPI shows house prices remained resilient in the second half of 2020, rising by 3.8% y/y in December from 3.5% y/y in November. This is in contrast to initial expectations of more subdued price growth. However, the pace of this annual price growth is decelerating. Monthly price growth has consistently slowed over the past five months, registering just 0.01% in December, down from 0.11% in November (Figure 1). This takes average annual house price growth to 2.1% in 2020, down from 3.5% in the previous year. Much of the price growth is in the lower end of the market, in part, due to the tight supply of properties for sale (Figure 2). Freehold properties, which have become more popular as more people work from home, continue to outperform sectional title units. FNB data shows that average value of freehold properties grew by 3.5% y/y in 4Q20, versus 1.3% y/y for sectional title units (Figure 3).

Figure 1: FNB HPI – Annual price growth resilient; but momentum slowing



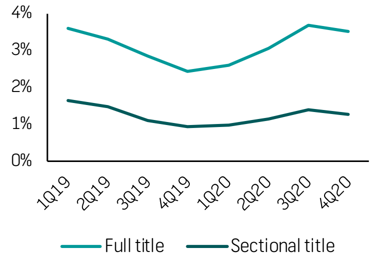
Source: FNB Economics

Figure 2: Price growth by price buckets (average purchase price)



Source: FNB Economics, Deeds Office

Figure 3: FNB HPI – Free-standing properties performing better



Source: FNB Economics

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Insights from the FNB Estate Agents Survey

Market Activity

Data up to 4Q20 shows that market activity continued to improve, albeit at a softer pace. Agents' rating of activity (0-10) edged up to 7.08 in 4Q20 from 6.86 and 3.36 in 3Q20 and 2Q20 respectively (Figure 4). In contrast to a surge in activity in 3Q20, which was driven mainly by middle-income segments (due to low interest rates and more favourable labour market outcomes for middle-income earners), the 4Q20 activity was spearheaded by the affordable market. This could be due to easing of lockdown restrictions, which allowed many low-income earners to go back to work and earn a living, but also some high-income households purchasing investment properties. All other price buckets saw a slight improvement in activity, except the R750k-R1.6m range which pulled back, following a robust increase in activity in 3Q20.

This corresponds with sentiment indicators: while the R750k-R1.6m range scored the highest in 3Q20, sentiment levels pulled back in 4Q20, reinforcing the view that perhaps activity is losing steam. Interestingly, however, satisfaction levels soared in the R1.6m-R2.6m range. We suspect this was supported by the work-from-home drive, which has seen some households looking for bigger spaces. Worth noting also is that sentiment continued to recover in the >R3.6m range, albeit from depressed levels (this corresponds to a slight uptick in activity). The high-net-worth segment has had to contend with negative wealth effects due to the impact of the pandemic on asset prices, corporate income, dividend income, interest income as well as bonuses.

Commensurately, time on market shortened to 9 weeks and 4 days, from 10 weeks and 6 days in 3Q20. This is on the back of increased activity in the affordable market, as well as a slight improvement in the top end.

Price realisation

The improved affordability (lower acquisition and repayment costs) and increased demand has, inadvertently, offered sellers a bit more room to negotiate: the proportion of properties sold at less than the asking price narrowed to 72% in 4Q20, from 80% in 1Q20. Similarly, discount on asking prices narrowed marginally to 10%, from 11% in 3Q20 and 13% in 1Q20. As a result, price reductions have not been as large as initially feared, underpinning the resistance in house prices.

Expectations of future activity

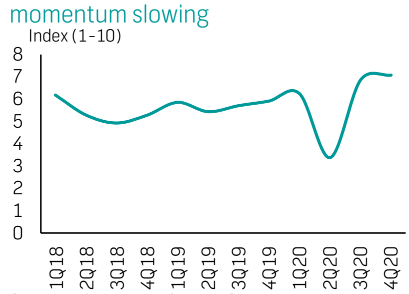
Agents' expectations of near-term activity tapered towards the end of the year. The proportion of agents that expected activity to increase from current levels declined from 50% in 3Q20 to 37% in 4Q20, while the proportion of agents who expect activity to decline increased to 17% from 10% in the same period. Importantly, however, 60% of agents in the "affordable" market still expect activity to increase (62% in 3Q20), compared to 29% (47% in 3Q20) in the conventional market. Thus, much of the "pessimism" is coming from higher-priced segments. Chief among the reasons given is buyer despondency: buyers are afraid to commit due to job insecurity and uncertainty about salary increases.

Reasons for selling

Downscaling due to financial pressure is fast becoming the most prominent reason for disposing of property in SA, tied with downscaling due to lifestyle changes at 22% (two-quarter moving average). Historically, downscaling due to lifestyle changes accounts for the largest proportion of disposals, and usually oscillates at around 22% of the market. At these levels, volume sales attributed to financial pressure are the highest since 2011. These are evident across all price buckets, but more so in the affordable segments. For the <R750k band, these are estimated to have risen to around 30% of disposals. This is on the back of relatively severe labour market pressures for lower-income earners. Part of the disposals, however, may be due to high-income households disposing of investment properties to alleviate financial pressures. There are also rising incidents of corporates disposing of property to alleviate cash flow and balance sheet pressures.

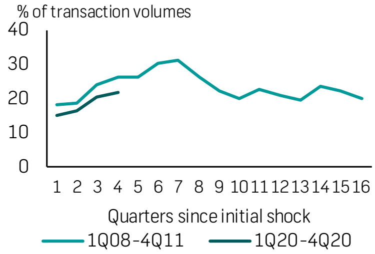
Interestingly, the trend looks similar to the 2008 crisis, although at a noticeably lower level. If the trend continues to track 2008, we should expect more properties on market due to downscaling, and a peak between 2Q21 and 3Q21 (Figure 5). While financial pressure is evident, the R1.6m-R2.6m price bucket is experiencing increased incidents of upgrading. We suspect that this is driven by the changing housing needs due to the pandemic and remote working, and the less severe job losses among high-income earners.

Figure 4: Market acitivity still strong, but momentum slowing



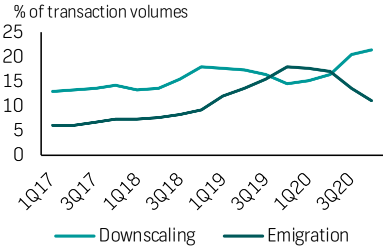
Source: FNB Estate Agents Survey

Figure 5: Trend in sales due to financial pressure similar to GFC



Source: FNB Estate Agents Survey

Figure 6: Property sales due to financial pressure on the rise (2qma)



Source: FNB Estate Agents Survey

Emigration sales continued to pull back from the recent peak of approximately 18% in 4Q19, to 11% of the market in 4Q20 (two-quarter moving average). Disaggregating by price bucket, these sales have started rising in the higher-priced segments, particularly the R2.6m-R3.6m band. However, we suspect that part of these relate to delayed decisions due to travel restrictions during the year. Should the trend continue, this could push the higher-end market deeper into excess supply and cause further price reductions.

Outlook

In our view, property market outcomes in 2021 will be highly dependent on how the labour market evolves. Data from Stats SA shows that the economy shed approximately 1m formal jobs between 4Q19 and 3Q20; including the Agricultural sector, this figure is closer to 1.1m. This is in comparison with our forecast of 1.2m job losses due to the pandemic. Even with these massive numbers, the impact on the home-buying market has not been as bad as initially feared. As elucidated above, the this might be due to the composition of those job loses, or the profile of workers who lost their jobs.

Naturally, employment is a lagging indicator. Survey data (from sentiment indicators) shows that corporates still expect more employment losses. For instance, latest PMI data shows that the index tracking employment expectations continues to contract, albeit at a slower pace. Crudely, this means we should expect more job losses in the manufacturing sector. While the headline number might not change massively from current levels, the composition of job losses might change drastically, and extend to higher-skilled workers. If we are correct, then we should expect more significant downward pressure on household incomes, and by extension, market activity and eventually house prices. Lower interest rates will assist, but this will hardly be enough to offset the demand-dampening effect of these job losses (law of diminishing returns).

On the supply side, we are already seeing rising incidents of property disposals due to financial pressure. Sales in execution are on the rise. Admittedly, these have not been as bad as in 2008. Among other factors, this is due to support from lenders (payment holidays) and the aggressive interest rate cuts that ameliorated financial pressures. These measures are coming to an end, and the effect is waning.

Furthermore, shrinking demand and rising vacancy rates in the rental market present a threat to housing stock for sale: more landlords may elect to sell their properties (supply impulse). Anecdotal evidence suggests that even corporates (mainly SMMEs) are disposing of their assets, to alleviate cash flow and balance sheet pressures. Involuntary sales are also prevalent, as can be seen by the high number of company liquidations in recent months.

A combination of these could culminate in a supply glut at a time when demand has dried up (due to income pressures and the diminished effect of low interest rates). This could dislocate market equilibrium and push the market deeper into excess supply. As mentioned above, property disposals due to financial pressure is now becoming the dominant reason for property disposal in SA; this is across the spectrum but more so in the lower end. This suggests that price pressures experienced in the top end could now filter down to the more affordable segments. As such, we expect house prices to decline by around 6% this year.

This assumes no further support to property owners by lenders (e.g., payment holidays or similar initiatives). It also does not take into account the impact of government's economic reconstruction plan. Should we see some movement on these, we could revise our expectations higher.

Table 1: Reasons for selling property by price – 4Q20

	4Q20	<R750k	R750k-R1.6m	R1.6m-R2.6m	R2.6m-R3.6m	>R3.6m
Downscaling due to financial pressure	20	27	20	19	16	16
Upgrading	14	18	16	13	12	9
Downscaling with life-stage	21	18	20	23	24	24
Security concerns	6	4	8	7	3	4
Emigrating	12	4	7	13	21	24
Relocating	11	16	11	9	11	9
Change in family structure	9	3	12	11	9	10
Moving to be closer to work or amenities	6	10	6	5	3	4

Source: Estate Agents Survey

Monthly FNB House Price Index (% y/y)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2001		-1.7	-0.7	-0.4	-0.5	0.7	3.0	5.9	8.6	10.6	11.6	11.8
2002	11.6	12.0	12.8	13.8	14.2	14.0	13.6	13.1	13.2	13.5	13.8	13.8
2003	14.0	14.5	15.3	16.2	17.1	18.2	19.3	20.3	21.4	22.9	24.7	27.0
2004	29.4	31.3	32.4	33.2	33.7	33.9	34.5	35.1	35.3	35.2	35.3	35.4
2005	34.8	33.8	32.9	31.8	30.7	29.7	28.8	27.9	26.9	25.7	23.9	21.7
2006	19.9	18.5	17.6	17.3	17.3	17.2	16.9	16.5	15.8	15.1	14.4	14.0
2007	14.0	14.3	14.9	15.7	16.3	16.6	16.3	15.5	14.5	13.2	12.0	11.0
2008	9.7	8.0	5.5	2.5	-0.4	-2.9	-4.7	-5.6	-5.8	-5.6	-5.1	-5.1
2009	-5.0	-5.0	-4.5	-3.8	-2.8	-1.8	-0.7	0.0	0.5	0.9	1.2	2.0
2010	3.0	3.9	4.6	5.2	5.6	5.5	5.0	4.7	4.5	4.1	3.7	3.1
2011	2.4	2.1	2.0	2.2	2.5	2.8	3.3	3.6	3.8	3.9	4.1	4.4
2012	4.7	4.8	4.8	4.7	4.6	4.7	4.9	5.2	5.6	5.7	5.8	5.8
2013	5.9	6.0	6.1	6.1	6.1	6.3	6.5	6.4	6.3	6.5	7.0	7.7
2014	8.2	8.3	8.2	8.3	8.4	8.3	8.0	7.8	7.6	7.2	6.8	6.2
2015	5.8	5.9	6.3	6.5	6.6	6.4	6.3	6.2	6.1	6.2	6.3	6.3
2016	6.3	6.2	6.1	6.0	5.9	5.8	5.7	5.6	5.4	5.1	4.8	4.8
2017	4.7	4.6	4.5	4.3	4.2	4.1	4.1	4.2	4.2	4.2	4.0	3.8
2018	3.5	3.3	3.4	3.5	3.7	3.8	3.9	4.0	4.1	4.2	4.1	4.0
2019	3.8	3.6	3.4	3.4	3.4	3.5	3.6	3.7	3.8	3.7	3.5	3.1
2020	2.5	1.9	1.3	1.2	1.2	1.6	2.0	2.5	2.9	3.1	3.3	3.5

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 fromthe 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 previoustransaction 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.