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Explanatory notes:
The Absa House Price Index is based on the total purchase price of houses in the 80m²-400m² size category, valued at R2,9 million or less in 2007 (including improvements), in respect of which loan applications were approved by Absa. Prices are smoothed in an attempt to exclude the distorting effect of seasonal factors and outliers in the data. As a result, the most recent index figures may differ materially from previously published figures.

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Pace of house price growth slowed further in May

Based on the latest Absa House Price Index, house price growth dropped further to a nominal 4,3% year-on-year (y/y) in the middle segment of the market (see explanatory notes) in May this year, down from a revised 5,5% in April. It was the lowest nominal year-on-year price growth recorded since October 1999, when it was also 4,3%, and brought the average price of a middle-segment house to about R960 700 in May.

In real terms, house prices in the middle segment of the market dropped by 5,0% y/y in April 2008, compared with a decline of 3,4% y/y recorded in March, based on headline CPI inflation. This was the biggest real year-on-year drop recorded in house prices since March 1997, when it was at a level of -5,2% y/y, based on nominal price growth of 3,9% y/y, and a headline CPI inflation rate of 9,6% at the time.

On a month-on-month basis, revised nominal house price growth was negative to the tune of 0,1% between March and May this year, which was the first nominal month-on-month price drop since January 1999. As a result, the average nominal house price has declined by about R4 000 over the past three months. In real terms, house prices dropped by a further 1,9% in April from March. The real price of a middle-segment house has dropped by a total of R37 200, or 5,7%, from an all-time high of around R651 600 (at constant 2000 prices) in August last year to about R614 400 in April this year.

CPIX inflation rose to 10,4% y/y in April, driven by the usual factors of high oil prices and food inflation, and exchange rate movements. Fuel prices were raised further to record highs this week, which should keep inflation under upward pressure in the near term. As a result, inflation expectations will remain high over the short term, which are expected to contribute to higher wage demands this year. Moreover, if the food and fuel price components are excluded, the CPIX inflation rate continued its upward trend to reach a level of 6,1% y/y in April - an indication of secondary inflationary effects present in the economy, which are of great concern to the Reserve Bank.

These developments, as well as recent comments by the governor of the Reserve Bank that drastic measures now need to be taken, and the fact that the Bank is now forecasting CPIX inflation to reach the 6% level only by 2010, are expected to see the Monetary Policy Committee hiking interest rates by a full 100 basis points next week (11-12 June), with the risk of further rate hikes later this year if the CPIX inflation rate remains stubbornly high.

In view of these developments and expectations, activity levels in the residential property market, and both nominal and real house price growth are forecast to slow down even further in the rest of 2008 and into 2009. In real terms, house prices are expected to decline this year compared with 2007, with a further real decline projected for next year.

