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DEVELOPMENTS IN THE ECONOMY AND THEIR IMPACT ON HOUSING DEVELOPMENT

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ENVIRONMENTAL SCANNING: DEVELOPMENTS IN THE GLOBAL AND LOCAL ECONOMY AND THEIR IMPACT ON HOUSING DEVEKLOPMENT

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1. INTRODUCTION

The human settlements environmental scanning report is a quarterly publication focusing on developments in the global and local economy, building sector as well as residential property market and their potential impact on housing development. This report is compiled by Governance Frameworks, Research Directorate of the Department of Human Settlements using various sources that comprise Statistics South Africa, Bureau for Economic Research, building material retailers, document analysis, surveys and interviews with key players in the construction industry. The publication is intended for practitioners and stakeholders in the human settlements sector. It provides an analysis of trends relating to developments in the global and local economy, the state of the building industry, the residential property market and how these affect the mandate of the Department of Human Settlements.

The impact of global economic developments in South Africa is analysed using variables such as GDP growth, inflation, interest rates, access to credit, credit defaults and rate of unemployment. Analysis of developments in the building industry includes comparative analysis of the cost of building materials, building plans passed, etc. An analysis of developments in the residential property market is also discussed focusing mainly on the affordable market.

Furthermore business and consumer confidence indices are utilised to determine future developments in the economy and construction industry. Implications are drawn on how these could weaken or strengthen the implementation of policies and programmes of the Department of Human Settlements.

2. GLOBAL ECONOMIC DEVELOPMENTS

According to du Toit, global real economic growth moderated from 3.8% in the second half of 2013 to 2.8% in the first quarter of 2014. The slower growth in world economic activity in the early stages of the year was the result of factors such as severe winter conditions and a high level of inventories in the United States (US), slowing domestic demand in China and sharply lower activity in Russia, due to geopolitical tensions. However, US growth rebounded strongly to 4% in the second quarter after a contraction of 2.1% in the world largest economy in the first quarter. The second-quarter growth was above expectations of 3.2% and was largely driven by strong growth in personal goods consumption, domestic private sector investment and exports. Economic growth in the euro area remained low, with the European Central Bank recently easing monetary policy further in an attempt to revive activity and prevent a situation of deflation. On balance, these developments contributed to lower levels of activity in emerging economies, with a slowdown in domestic demand and lower growth in investment also evident in these countries (ABSA, 2014).

The first quarter of 2014 saw the South African economy contracting at a seasonally adjusted annual rate of 0.6% from a growth rate of 3.8% in the fourth quarter of 2013. The depressing first-quarter growth performance came on the back of contractions in output in mining, affected by strikes, and manufacturing. The mining sector was mainly plagued by protracted industrial action in the platinum sector, which contributed to real output dropping by a massive 24.7% in the first quarter compared with the preceding quarter. Output in the manufacturing sector was down by a real 4.4% compared with the final quarter of 2013, resulting from contractions in output in the manufacturing subsectors of petroleum, chemical, rubber and plastic products; motor vehicles, parts and accessories; basic iron and steel; glass and non-metallic mineral products; and furniture (ABSA, 2014).

After bottoming at 5.3% year-on-year (y/y) in November 2013, headline consumer price inflation trended upwards in the first six months of 2014, averaging 6.2% y/y over this period. The major factors causing upward pressure on inflation are food prices, transport costs, property-running costs, a relatively weak rand exchange rate and wage hikes of above inflation. While growth in wages remained above inflation, growth in labour productivity was, however, only about 1.3% per annum in 2011-2013, contributing to nominal unit labour costs rising by an average of 6% per annum, whereas consumer price inflation averaged around 5.5% per annum over this period (ABSA, 2014).

The Rand remains weak at R10.29/US$ and it remains under pressure given the large current account deficit and further QE tapering. The current slowdown in the domestic economy, coupled with some improvement in exports should help to reduce the current account deficit over the coming months, and ease the pressure on the Rand. The Rand/Dollar exchange rate forecast for end 2014 is currently at R10.75, weakening to R11.20 at end 2015, (Stanlib, 2014).

3. SOUTH AFRICAN ECONOMIC OUTLOOK

3.1 Economic Performance

According to Statistics South Africa, domestic seasonally adjusted real gross domestic product (GDP) at market prices for the first quarter of 2014 increased by an annualised rate of 0.6 % in the second quarter of 2014. The main contributors to this increase in economic activity were general government services and the transport, storage and communication industry, each contributed 0.4% point based on increases of 2.9% and 4% respectively. This was followed by finance, real estate and business services which contributed 0.3% based on an increase of 1.5% (STATSSA, 2014).

Economic activity in the transport, storage and communication industry reflected positive growth of 4.0% due to increased activities in the land transport, air transport and transport support services and communication industry. Economic activity in the mining and quarrying industry reflected negative growth of 9.4% due to lower production in the mining of gold and the mining of other metal ores including platinum. Economic activity in the manufacturing industry reflected negative growth of 2.1% due to lower production in the following divisions: food, beverages and tobacco; petroleum, chemical products, rubber and plastic products; motor vehicles, parts and accessories and other transport; and glass and non-metallic mineral products (STATSSA, 2014).

3.2 Developments in energy prices

The energy prices and in particular petrol price in South Africa is linked to the price of crude oil in international markets and is quoted in US dollars (US$) per barrel. Crude oil prices combined with the Rand/Dollar exchange rate therefore have a major impact on petrol prices. In order for a refinery to make a profit, the price for the product manufactured from crude oil has to be higher than that of the crude oil price. Therefore, if crude oil prices increase, the petrol price has to increase so that crude oil refineries are able to cover their costs.

Crude oil spot price increased from an average $106/bbl in June to $115/bbl in July which led to the increase in petrol prices. This was driven partly by the relocation of crude oil to refining centres along the Gulf Coast through new pipelines, crude oil inventory levels at the Cushing, Oklahoma storage hub (US Energy Administration Information, 2014).

The Rand depreciated against the US Dollar from $10.40 to $10.68 during the July review period. This also contributed to the fuel price increases. With effect from 02 July, the petrol price increased by 14c/l from R13.81c/litre to R13.95c/l. During the September review, petrol price decreased by 67c/l and it was R14.62c/l (Department of Energy, 2014).

3.3 Inflation[1] movements and its impact

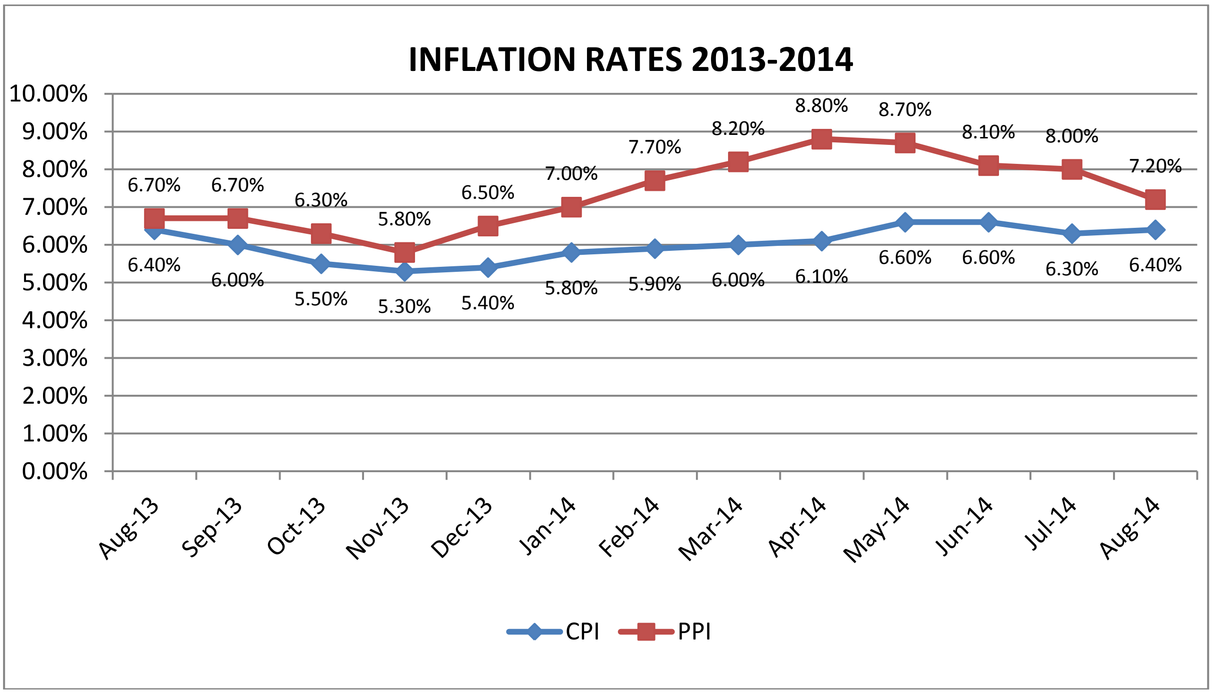
The Consumer Price Index (CPI) and Producer Price Index (PPI) are the two primary measures of inflation for South Africa. The CPI tracks the rate of change in the prices of goods and services purchased by consumers. Thus, the headline CPI is used as the inflation target measure which guides the South African Reserve Bank (SARB) on the setting of interest rates. The PPI tracks the rate of change in the prices charged by producers of goods.

Consumer inflation increased up to 6.4% in August compared with July's reading of 6.3%. The increase was mainly a result of upward pressure from food and motor vehicle prices. Annual food and beverage inflation, which registered 8.8% in June and July, climbed to 9.4% in August. Food inflation has been increasing since December 2013 when it registered at 3.5%. Meat and dairy products were the main drivers of food inflation in August. While petrol prices were unchanged in August, prices of new vehicles increased by 1.2% from the previous month. They now show an 8.1% annual inflation rate.

[1] Inflation is the rate at which prices are increasing

The upward trend in inflation generally mean that household's disposable income is eroded at a faster pace thereby is reducing the standard of living at a faster rate. The same income level now can only afford fewer goods.

FIGURE 1: INFLATION RATES



Source: STATSSA, June 2014

The annual percentage change in the PPI for final manufactured goods was 7.2% in August 2014. From July 2014 to August 2014 the PPI for final manufactured goods remained unchanged. The main contributors to the annual rate of 7.2% were food products, beverages and tobacco products which contributed 2.9 % points. Coke, petroleum, chemical, rubber and plastic products contributed 1.1% points and metals, machinery, equipment and computing equipment contributed 1.2% points.

For housing specifically, if costs of production are increasing, it means that the value capital investments made for housing development will consistently decline. The result is that it will cost a little more to build the same size of a house. These developments together with price increase of essentials like food and clothing for instance does indicate that households will find it more challenging to provide shelter for themselves and therefore will require some form of assistance from government.

3.4 Interest Rates

At its Monetary Policy Committee (MPC) meeting in July, the South African Reserve Bank hiked interest rates by 25 basis points. During its September meeting, the MPC has left the repo rate unchanged at 5.75%. The prime interest rate asked by commercial banks also remained unchanged at 9.25% (SA Reserve Bank, 2014). This decision meant that the pressure on disposable income for individuals with mortgages and other forms of credit exposure also remained unchanged.

The Monetary Policy Committee (MPC) continues to face the difficult dilemma of dealing with upside risks to inflation and a deteriorating domestic economic growth outlook. Although the breach of the upper end of the inflation target band was in line with the Bank's forecast, the risks to the forecast remain on the upside. The policy dilemma is increased by the fact that inflation is seen to be driven primarily by supply side factors, while demand conditions in the economy remain subdued (SA Reserve Bank, 2014).

3.5 Unemployment

According to the labour force survey of Statistics SA, shows that there was a q/q increase in employment of 155 000 from 8 511 000 in March 2014 to 8 666 000 in June 2014. This was largely due to increases in the following industries: community services industry increased by 143 000 (5.8%); trade industry increased by 17 000 (1.0%); construction industry increased by 5 000 (1.2%) and finance industry increased by 2 000 in the (0.1%). There were decreases reported by manufacturing was down by 6 000 or -0.5%; transport was down by 4 000 or -1.1%; mining was down by 1 000 or -0.2%; and electricity was down by 1000 or -1.6%.

Employment increased by 229 000 (2.7%) year-on-year between June 2013 and June 2014. Most increases were reported by the community services (up by 220 000 or 9.2%); followed by trade (up by 26 000 or 1.5%); and finance (up by 15 000 or 0.8%).

Unemployment rate increased to 25.5% in the second quarter from 25.2% in the first quarter of the year, which implies that a total of 5,154 million people were unemployed in the second quarter, up from 5,067 million having been unemployed in the preceding quarter. According to Andrew Levy Employment Publications, a total number of 7,5 million man-days were lost due to industrial action in the first half of 2014 compared with 1,8 million lost in the same period last year and 5,2 million lost in the whole of 2013. These labour market trends are not conducive to higher levels of confidence, investment and employment in the medium to longer term.

The high levels of unemployment means people will still be dependent on State assistance programmes. For the Department of Human Settlements it means more people will require housing assistance and this will add to the already existing backlog.

3.6 Access to credit

At the end of the second quarter, there were 79.42 million accounts recorded at registered credit bureaus. This was an increase of 2.9% quarter-on-quarter and 11.6% year-on-year. Of the 79.42 million accounts, 58.15 million (73.2%) were classified as in good standing, a negative variance of 1.8% quarter-on-quarter and 0.3% year-on-year.

According to the National Credit Regulator (NCR), the overall value of credit granted increased from R117.21 billion to R118.66 billion for the quarter ended December 2013. This is an increase of 1.24% when compared to the previous quarter but it decreased by 1.06% a year ago. The number of applications for credit increased by 525,000 from 10.22 million in September 2013 to 10.75 million in December 2013. This represents an increase of 5.14% for the fourth quarter (NCR, 2013).

The rejection rate of applications was 57.37%. Mortgages accounted for R34.72 billion (29.26%); “Secured credit agreements” for R40.58 billion (34.20%); Credit facilities for R18.70 billion (15.76%); Unsecured credit for R21.61 billion (18.22%); Short-term credit for R1.38 billion (1.16%); and Developmental credit for R1.68 billion (1.41%) of the total credit granted.

The number of applications received and the number of applications rejected increased by 5.14% and 5.41% respectively for the quarter ended December 2013.

TABLE 1: NUMBER OF APPLICATIONS RECEIVED AND REJECTED

Agreements	**2012 4th Q 000**	**2013 1st Q 000**	**2013 2nd Q 000**	**2013 3rd Q 000**	**2013 4th Q 000**
Number of application received	11,813	10,117	10,350	10,222	10,748
Number of applications rejected	6,301	5,631	5,811	5,850	6,166
% of applications rejected	**53.34%**	**55.65%**	**56.14%**	**57.23%**	**57.37%**

Source: National Credit Regulator, 2013

Mortgages' percentage share of total credit granted decreased to **29.26%** for the quarter ended December 2013 from 29.45% in the previous quarter. Unsecured credit as a percentage of total credit granted continued to grow from **17.83%** for the quarter ended September 2013 to **18.22%** for the quarter ended December 2013.

TABLE 2: CREDIT GRANTED BY CREDIT TYPE

Agreements	**2012 4th Q R000**	**2013 1st Q R000**	**2013 2nd Q R000**	**2013 3rd Q R000**	**2013 4th Q R000**	**2013 4th Q % distribution**
Mortgages	28,603,463	25,039,734	30,099,218	34,521,936	34,717,349	29.26%
Secured credit	39,478,512	35,185,813	37,539,671	39,911,580	40,579,597	34.20%
Credit facilities	19,182,321	16,725,388	16,627,607	17,719,904	18,698,299	15.76%
Unsecured credit	29,072,652	22,592,797	22,064,444	20,897,196	21,614,882	18.22%
Short term credit	1,707,277	1,590,561	1,450,531	1,394,880	1,378,018	1.16%
Developmental credit	1,896,498	1,151,721	1,834,435	2,768,119	1,675,816	1.41%
Total	**119,940,724**	**102,286,014**	**109,615,905**	**117,213,616**	**118,663,962**	**100.00%**

Source: National Credit Regulator, 2013

The value of the gross debtors book for the period ended December 2013grew by R26.68 billion (1.79%) and by R76.90 billion (5.33%) on a year on year basis. The unsecured credit book grew by R3.34 billion (2.00%) on quarter on quarter and by R11.50 billion (7.22%) year on year. The mortgages book grew by R8.17 billion (1.01%) and secured credit book grew by R11.74 billion (3.77%) for the December 2013 quarter. Gauteng province accounted for R56.10 billion (47.27%) of the total R118.66 billion of credit granted. Western Cape and KwaZulu Natal accounted for R16.28 billion (13.72%) and R14.24 billion (12.00%) respectively. The remaining provinces constituted R32.05 billion (NCR, 2013).

There was an overall quarter on quarter increase of 0.57% in the rand value of mortgage agreements granted for the quarter ended December 2013. The majority (71.39%) of mortgage agreements granted during the December 2013 quarter were in excess of R700K. The number of mortgage agreements concluded increased by 0.04% for the quarter ended December 2013. The majority (72.78%) of mortgages were granted in favour of larger sized credit agreements. On a year on year basis, mortgage agreements increased by 13.18%.

TABLE 3: MORTGAGES GRANTED BY SIZE OF AGREEMENTS

Agreements	**2013 3rdQ (R000)**	**2013 4th Q (R000)**	**2013 4th Q % distribution**	**% change (4thQ/3rdQ)**	**% Change (Y/Y)**
R0-R50K	33.008	38,750	0.11%	17.40%	-29.00%
R51K-R100K	174.358	165,330	0.48%	-5.18%	-11.67%
R101K-R150K	241.926	226,155	0.65%	-6.52%	-3.58%
R151K-R350K	1,972.058	1,905,584	5.49%	8.17%	-4.51%
R351K-R700K	7,450.421	7,598,281	21.89%	16.87%	7.47%
≥R700K	24,650.164	24,783,248	71.39%	14.93%	27.91%
Total	**34,521.936**	**34,717,349**	**100.00%**	**14.69%**	**20.02%**

Source: National Credit Regulator, 2013

Individuals with a gross monthly income of "Up to R10K" received 63.33% of the total number of short-term credit agreements granted for the quarter ended December 2013 as indicated in Table 4. Individuals with a gross monthly income of "Up to R10K" received

50.85% of the rand value of short-term credit granted for the quarter ended December 2013. This may suggest the individuals at lower income levels depend more on short-term loans.

TABLE 4: SHORT-TERM CREDIT GRANTED – GROSS MONTHLY INCOME OF INDIVIDUALS (NUMBER OF AGREEMENTS)

Level of income	**2013 1st Q**	**2013 2nd Q**	**2013 3rd Q**	**2013 4th Q**
≤R10K (R000)	620,696	589,912	562,322	553,823
% share of credit granted	62.35%	62.44%	62.59%	63.33%
R10.1K-R15K (R000)	172,994	162,221	149,922	142,294
% share of credit granted	17.38%	17.17%	16.69%	16.27%
>R15K (R000)	201,882	192,693	186,189	178,388
% share of credit granted	20.28%	20.39%	20.72%	20.40%
Total value of mortgages (R000)	**995,572**	**944,826**	**898,433**	**874,505**

Source: National Credit Regulator, 2013

The number of agreements that were concluded with individuals in the greater than R15K income category constituted more than 85% as indicated in Table 5. This income category also accounted for 95.88% of the rand value of the mortgages granted during the quarter ended December 2013 (NCR, 2013).

TABLE 5: MORTGAGES GRANTED BY GROSS MONTHLY INCOME OF INDIVIDUALS (RAND VALUE)

Level of income	**2013 1st Q**	**2013 2nd Q**	**2013 3rd Q**	**2013 4th Q**
≤R10K (R000)	210.541	236.620	260.179	242.376
% share of credit granted	*0.85%*	*0.80%*	*0.765%*	*0.71%*
R10.1K-R15K (R000)	981.329	1,146.680	1,233.152	1,171.389
% share of credit granted	*3.95%*	*3.86%*	*3.61%*	*3.41%*
>R15K (R000)	23,654.688	28,313.860	32,658.951	32,935.414
% share of credit granted	*95.20%*	*95.34%*	*95.63%*	*95.88%*
Total value of mortgages (R000)	**24,846.558**	**29,697.161**	**34,152.282**	**34,349.179**

Source: National Credit Regulator, 2013

The above data indicates that it has become increasingly difficult for low-income earners to access credit particularly mortgage loans. This trend suggests a need to encourage banks to focus on the lower market. But the argument might be that individuals at the lower market are not affording due to over-indebtedness and lower salaries or are not qualifying for mortgages.

Inflation rates and availability of stock also affect access to mortgages finance. If the entry stock is priced at an average of R350 000, monthly repayment will be R3 500 at 10% interest. This amount will be difficult for the household earning around R7 000.00 to make repayments. The cost of home ownership is not only the bond repayment, but it includes the property rates, electricity and water charges. At the end the household will be required to pay over R4000.00.

The policy implication is that the success of FLISP will remain limited if the implementation continues to rely on mortgages. There is a need for provinces to provide serviced stands for the gap market as this will allow individuals to request finance in smaller amounts depending on individual affordability.

3.7 Credit Defaults

According to du Toit (2014), the consumer sector continued to experience financial pressure in 2014. The ratio of household debt to disposable income ratio was virtually stable at 74.5% in the first quarter of 2014 from 74.6% in the fourth quarter of last year. This was the net result of nominal household disposable income growing by 1.6% quarter-on-quarter (q/q), while household debt increased at a rate of 1.4% q/q in the first quarter of 2014. The debt ratio is calculated as the total amount of outstanding household debt expressed as a percentage of the total annual disposable income of households, i.e. after deductions for tax, social contributions and transfers. The number of consumers in good standing came to 12.11 million (55.8%) in the first quarter. A total number of 77.18 million consumer credit accounts were active in the first quarter of the year, of which 57.91 million (75%) were in good standing and 19.27 million (25%) were impaired (ABSA, 2014).

This situation regarding consumers' credit-risk profiles severely restricts the access to credit and adversely affects household consumption expenditure against the background of the continued low level of household savings.

4. CURRENT DEVELOPMENTS IN THE BUILDING INDUSTRY

According to ABSA's Housing Review, the residential building activity with regard to the planning phase of new housing, as reflected by the number of building plans approved by local government institutions for houses, flats and townhouses, showed relatively strong growth of 16.6% y/y to a level of 25 266 units in the first five months of 2014 from 21 671 units in the corresponding period last year. However, the construction phase of new housing, i.e. the number of housing units reported as completed, contracted by 14.1% to a total of 15 329 units in the period from January to May this year compared with 17 854 new housing units built in the same period last year. In both the planning and construction phases more than 73% of the level of building activity this year occurred in the segments of smaller-sized houses and higher-density flats and townhouses. This has become a structural feature of the supply of new housing in the country over the past twenty years, driven by factors such as urbanisation, land scarcity, building costs, housing affordability, property running costs.

4.1 Building plans completed

The number of building completed reflects the level of building activities that occurred during the specified period. According to Statistics South Africa (2014d), the value of buildings reported as completed decreased by 7.7% (-R2 287.8 million) during January to July of 2014 compared with January to July of 2013. Additions and alterations were the largest contributor with -29.7% (Statssa, 2014).

4.2 Building Plans Passed

The building plans passed provide an indication of the level of building activities that is expected to take place in the near future. According to the Statistics South Africa, the value in the building plans passed at current prices increased by 7.6% (R3 775.6 million) during January to July of 2014 compared with January to July of 2013. The increase was mainly driven by an increase in residential buildings with 13.1%. Non-residential buildings and additions and alterations recorded 6.6% and -0.2% respectively (Statssa, 2014).

Table 2: Comparative Analysis of Building Plans Passed and Completed by Province

Province	**% Change in Buildings Completed Between January to March 2013 and January to March 2014**	**% Change in Building Plans Passed Between January to March 2013 and January to March 2014**
Eastern Cape	-1.2	-5.9
Free State	-55.6	37.8
Gauteng	14.1	-3.0
KwaZulu-Natal	-9.8	30.8
Limpopo	41.7	-12.0
Mpumalanga	66.6	-8.0
Northern Cape	101.7	27.7
North West	45.2	-16.2
Western Cape	-46.1	21.8
Total	**-7.7**	**7.6**

Source: Stats SA, 2014

Out of the nine provinces, four reported a year on year (y/y) decreases in the value of buildings completed in the third quarter of 2014. The major decrease was reported by the Free State Province followed by Western Cape, KwaZulu-Natal and Eastern Cape. Northern Cape was very active in terms of buildings completed and the province still shows some signs of future activities as the building plans approved are also high. In terms of building plans passed, four provinces reported y/y increases in the value of building plans passed. Free State Northern Cape recorded the highest followed by KZN, Northern Cape and Western Cape.

Residential building activity continues to be influenced by conditions and trends in the economy, household finances, consumer and building confidence, as well as factors related to the demand for and supply of new housing. These will remain the main driving factors of residential building activity.

4.3 Building Costs

According to ABSA (2014b), the average building cost of a new house increased by 5.9% y/y in the first quarter of 2014. Factors impacting building costs and ultimately the price of new housing include building material; transport; equipment and labor costs. The cost of developing land for residential purposes also contributes extensively to the escalation of building costs.

Global economic growth rates seem to be recovering gradually. BER business survey data reflect an improved business confidence levels. BER building survey respondents have become optimistic about business conditions for the first time in six and a half years.

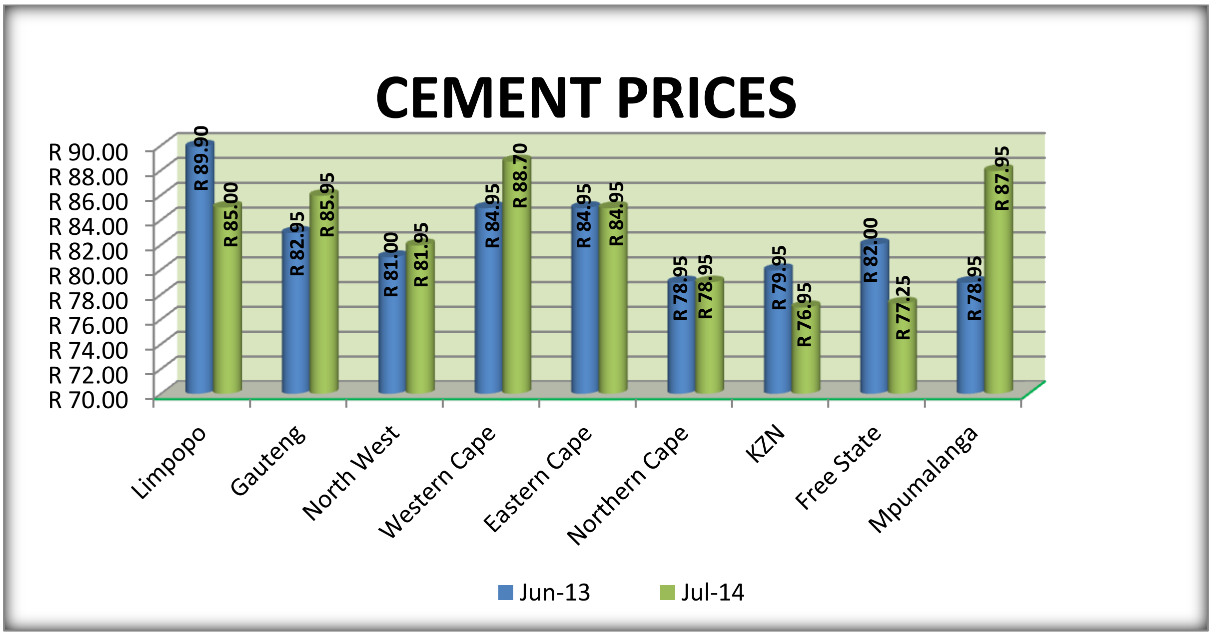
According to the Medium-Term Forecasting Associates, the Haylett Index (Work Group 180, lump-sum domestic buildings), which is a reflection of builders' input costs, rose by 6.4% on average in 2013. A rise of 6.7% was recorded in the year to August 2014 and it is expected to rise to an average of 6.9% in 2014. Haylett Index (Work Group 181, commercial and industrial buildings), rose by 6.2% on average during 2013. A rise of 6.5% was recorded in the year to August 2014 and an average rise of 6.9% is expected in 2014.

Tender price increases, as measured by the BER Building Cost Index, dropped by -0.2% in 2010 as intensive competition in tendering forced building contractors to trim their profit margins. However, tender prices rose by 3.4% in 2011 and by 6.9% in 2012. In 2013 preliminary data record an average rise of 6.6% per annum.

These building costs developments suggest that input costs continues to increase going forward and therefore they should be adequately accommodated in the subsidy quantum.

4.4 Cement Prices

Cement is one of the major products utilised in the building industry particularly in government-subsidised housing. Therefore, increases in the cement price impact significantly in the delivery of government subsidised housing and the total building costs. A telephonic interview with Cash Build Hardware was conducted to establish the cement prices in all Provinces. According to the data obtained from them, it was evident that the cement prices vary. These varying prices might be due the transport costs associated with delivering products different provinces within the country.



Source: Department of Human Settlements, 2014

In trying to track the trend on cement price movements, data collected in June 2013 and July 2014 was analysed and it was evident that within the twelve months period some provinces experienced a hike in prices whereas some remained unchanged. Limpopo, KZN and Free State provinces showed a different trend. In June 2013 prices were very high but surprisingly went down to the lowest recording R76.95 in July 2014. Eastern Cape Province prices remained unchanged at R78.95. Mpumalanga province experienced a R10.00 hike in price from R78.95 recorded in June 2013.Gauteng, North West and Western Cape Province experienced a mild increase in price during this period. The price increases ranged from R1.00 to R3, 70 (Human Settlements, 2014).

In terms of the most expensive prices, Limpopo is ahead with R89.90, Western Cape at R88.70 and Mpumalanga at R87.95. Cement seems to be more affordable in KZN province with R79.95 in June 2013 and R76.95 in July 2014 (Human Settlements, 2014). These figures are indicating that the transport costs from the harbour to the inland could be a major factor that affects prices for goods in the inland provinces.

5. OVERVIEW OF THE RESIDENTIAL PROPERTY MARKET

Trends in house prices is a reflection of the property market conditions and related factors which are affected by a combination of macroeconomic developments, the state on household finances and the level of consumer confidence.

According to ABSA, nominal and real y/y house price growth in the middle segment of the market was stable in the second quarter compared with the first quarter. In the category of affordable housing nominal price growth accelerated in the second quarter, whereas price growth in the luxury segment tapered off further after a recent peak in the fourth quarter of 2013. Real house price growth was influenced by persistent upward pressure on consumer price inflation in the second quarter of the year. House price trends continued to be driven by property market conditions and related factors, which were affected by a combination of macroeconomic developments, the state of household finances and the level of consumer confidence (ABSA, 2014).

5.1 Residential Property Prices

The affordable segment (houses with the size of 40m^2 to 79m^2 and priced up to R545, 000 in 2014), accelerated to 6.6%, with an average price of about R368 300 in the second quarter of 2014, after rising by 3.6% in the first quarter. Real price inflation of 0.1% y/y was recorded in the second quarter after real price deflation for five consecutive quarters up to the first quarter of this year. (du Toit, 2014).

The average nominal price of a home in the middle segment of the market (homes of 80m² to 400m² and priced at R4million or less in 2014) increased by 8.8% y/y to around R1 257 900 in the second quarter of 2014 (8.7% y/y in the first quarter). Real price inflation in this category of housing came to 2.1% y/y in the second quarter of the year, down from 2.7% y/y in the first quarter (du Toit, 2014).

The second quarter of 2014 saw the average price of luxury housing (homes priced at between R4 million and R14,6million in 2014) rising by a nominal 2.6% y/y to a level of about R5,2 million, after prices had risen by 7% y/y in the first quarter. In real terms, the average price in this category of housing was down by 3.7% y/y in the second quarter of the year after rising by 1.1% y/y in the first quarter. (du Toit, 2014).

5.2 Land Values

The value of land for new housing in the middle and luxury segments of the market for which Absa received applications and approved mortgage finance, increased by a nominal 3.1% y/y to an average of about R587 400 in the second quarter of 2014, after having risen by 2.8% y/y in the preceding quarter. In real terms residential land values were down by 3.2% y/y in the second quarter of the year, after declining by a real 2.9% y/y in the first quarter.

The average price of land for new middle-segment and luxury housing, which amounted to 26.4% of the total value of a new residential property in these categories in the second quarter of 2014, will continue to reflect the all-important factor of location, as well as the availability of suitable land for development, the availability of municipal services such as electricity, water, sewerage and refuse removal, the availability and condition of transport infrastructure and the proximity to places of work, schools, shopping centres and medical facilities (du Toit, 2014).

6. CHALLENGES

6.1 Poor prospects of economic performance

Economic performance during the first quarters of 2014 saw a rebound from 2.9% in 2013 to 3.5% in 2014. Across the advanced economies, the 2014 growth outlook has started to show the signs of improvement with 2.2% growth in 2014, compared to 1.3% in 2013.

6.2 High rate of unemployment

Second quarter experienced a decline in employment due to job losses in the informal sector. In turn unemployment increased to 25.2% in the first quarter of 2014. These are indications that more South Africans will still rely on government for assistance including housing.

6.3 Vulnerability of the low income earners

High level of indebtedness and high level of impaired credit record presents evidence of vulnerability of low income earners to access mortgage loans which is the main form of funding housing development for ownership currently. This suggests that incremental housing should be the preferred approach for housing development for low income earners. Information from Credit Regulator provides evidence that low income earners are continually opting for short term loans to fund their housing development as opposed to mortgage loans.

6.4 Increasing input cost

Cost escalations for new house construction continue to outstrip the cost of buying an existing house. Increasing land cost is also expected to continue to contribute significantly to the costs of housing development. This means that more funding will be required to ensure that the level of housing development is not affected.

6.5 Subdued property market

The property market is expected to continue to reflect conditions of poor economic performance, struggling consumer sector due to declining values of disposable income (owing to inflation and increasing costs of living) and limited access to funding due to indebtedness, impaired credit record and risk aversion by financial institutions. This is more prevalent in the affordable segment of the market which registered real price deflation of 2.6% y/y in the first quarter.

7. FUTURE ECONOMIC PROSPECTS AND IMPACT ON THE RESIDENTIAL PROPERTY MARKET

Confidence indices are the key leading indicators which points the direction for the future economic performance. Business confidence and building confidence indices provides indication of future investments by businesses while consumer confidence is critical to point the direction of spending by the general public.

The **Business Confidence Index**[2] (BCI) which measures the confidence levels of prevailing business conditions in the manufacturing, building, retail trade, wholesale trade and new vehicle trade sectors increased by 5 points to 46 points third quarter of 2014.

According to RBM/BER the rise in the BCI reflects an improvement in sentiment in all the sectors making up the headline index, except for the new vehicle trade. Confidence among wholesalers increased by 15 index points. The retailers, building contractors and manufacturers, the business mood improved by 11, 8 and 3 points respectively. By contrast, sentiment among new vehicle dealers deteriorated by 15 points.

After increasing from 39 to 49 in the second quarter, retailers' confidence rose further to 60 index points. The confidence of wholesalers jumped from 44 to 59 index points and building contractors increased from 45 to 53. Manufacturing confidence increased marginally from 25 to 28 index points, as sales and production recovered only partially from the poor performance in the strike-affected second quarter. While both export and domestic sales volumes improved, levels are still much lower than they were at the beginning of the year.

According to RBM/BER, the **Consumer Confidence Index**[3] **(CCI)** The FNB/BER consumer confidence index (CCI) rebounded from -6 to 4 index points during the second quarter of

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[2] Business Confidence Index (BCI) is determined from a survey of five major sectors of the economy namely manufacturing, building, retail trade, wholesale trade and new vehicle trade. BCI measures whether investors in these sectors rate prevailing business conditions as satisfactory or not.

2014. The latest reading is the highest since third quarter 2011, but still marginally below the long-term average reading of the CCI (+5 since 1994). Consumers' rating of their own financial prospects improved significantly during the second quarter of 2014, with high income consumers in particular expecting their household finances to look up over the next 12 months. Consumers' rating of the outlook for the national economy and the appropriateness of the present time to buy durable goods also improved notably, but these two indices still remain well below their historical averages (RBM/BER, 2014).

The **Building Confidence Index**[4] increased up to 45 points in the third quarter of 2014 after the fall of 41 points which was registered in the second quarter. The survey results suggest that residential building activity improved satisfactorily, supporting the rest of the building sector. In contrast, nonresidential building activity was unchanged. Retailers of building materials increased by 18 to a six year high of 74 index points. Main contractors increased by 8 to 53 index points. This was primarily due to a marked increase in residential contractor confidence on the back of a sharp rise in residential building activity. Sub-contractors, manufacturers of building materials and architects gained confidence, recording an increase of 4, 4 and1 respectively. Despite the activity level in residential sector, confidence for quantity surveyors declined by 8 and recorded 37 index points.

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[3] **Consumer Confidence Index** is a FNB/BER survey of consumers based on three questions, namely the expected performance of the economy, the expected financial situation of households and the rating of the appropriateness of the present time to buy durable goods (such as furniture, appliances, electronic equipment, and motor vehicles) (BER, 2011c).

[4] **Building confidence Index** measures the level of performance as well as possibility for future investments in all sectors of the building industry. The index measures the business confidence of all the major role players and suppliers involved in the building industry, such as architects, quantity surveyors, contractors, sub-contractors, wholesale and retail merchants, and manufacturers of building materials (BER, 2011f). The index can vary between zero (indicating an extreme lack of confidence) and 100 (indicating extreme confidence).

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