By Stuart Murray
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Steady but slow

House prices are rising again as consumer confidence builds up. The big issue in the market is fast becoming that of running a home as opposed to buying one.

THE LATEST RESIDENTIAL PROPERTY indices show a mild acceleration in house price inflation, further emphasising the steady upturn since last year. The FNB House Price Index, for one, shows an increase in year-on-year inflation in February of 5,8% compared to a 3,6% rise in the previous month. On a cumulative basis this implies an 11,1% rise since June 2009, the low point in the slump.

Most analysts consider the recovery due to the lagged effect of five basis points reduction in interest rates during 2008/09 (such cuts always take time to filter through into the market). This positive effect will most likely continue until later this year - unless the SA Reserve Bank reduces its repo rate still further. Economists, however, consider further cuts unlikely given the Banks' determination to bring inflation down below its top-end target range of 6%.

However, there is a more confident air about the housing market, with increased activity, more sales, and better selling values. There appears to be a segment of buyers who have decided that the market bottom has been reached and that now is the time to buy. Agents nevertheless report that many sellers are still asking for unrealistic prices.

Another important market indicator is the length of time a property up for sale remains on the market. This has fallen quite dramatically. During the second quarter of 2009, this waiting period peaked at around 21 weeks. By the end of the fourth quarter it had fallen to 13 weeks. Signs are that it will show a further drop by the end of the first quarter of this year.

The FNB's market strength index asks professional valuers for their experience of the current state of demand and supply for similar properties in a specific area. The latest index suggests that there are still more areas with an oversupply of property than areas with an undersupply.

Another indicator is that of mortgage advances, which continues to show improved growth, although slightly down in January compared with the previous month, according to Absa's data. FNB, on the other hand, reported a slight upturn in January compared with December, but the bank does not perceive this to be indicative of a rising trend. In terms of prices, Standard Bank reports very little average growth at all, stating that its median price measure indicates that house price growth is improving very slowly "but is likely to turn positive by the second quarter of 2010." Conversely, mortgage originator, ooba, says its barometer shows that there has been positive growth for the last eight consecutive months. FNB reports growth for the last four consecutive months.

So what does one make of these differing indices? The reason for the diversity is that each lender calculates its data based on its own mortgage book and share of the overall market. Let's say the bank with the biggest market share has 30% - that's as far as its database can stretch. Furthermore, some (Standard's median index is an example) calculate price inflation differently. Property market analyst, Lightstone, is another, making use of repeat sales only.

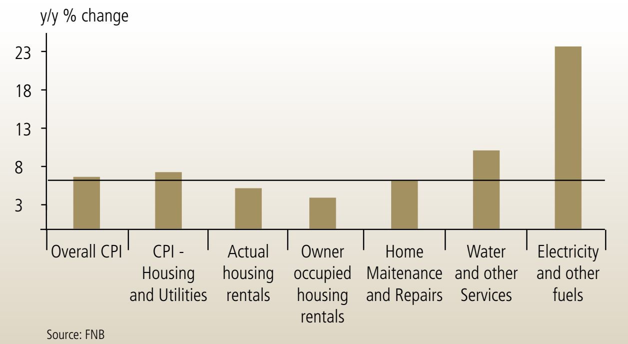
From a straightforward market analysis point of view - if such a thing is possible - the residential market looks, at most, steady rather than exciting. Average growth for this year is expected to come in at around 8% to 10% - restrained by households' still high debt-to-disposable income-ratio.

As to the outlook for the rest of the year, Standard says that due to the nature of the current economic recovery the property market "could possibly be one of the last sectors to improve." FNB is more prosaic. The bank's home loans strategist, John Loos, comments that the market is now "out of the death zone" but adds that the risks remain significant given the high levels of household debt. However, government's anticipation of 3% economic growth, if reached, should help the market.

The dark cloud on the horizon is the strain which households are facing in the steeply rising costs of running a home. Escom, of course, is the bad apple, having been given permission by the National Electricity Regulator (Nersa) to increase its tariffs by 24,8% this year, 25,8% next year and 25,9% in 2012. But it doesn't end there. Water and sewage infrastructure is also under pressure, as are the municipalities which supply consumers with such services and who will most definitely be increasing rates in order to finance budget deficits.

Up until now, the "affordability factor" affecting the housing market has been the ability of consumers to qualify for mortgage bonds by meeting the strict lending criteria of banks. Deposits have been high and interest rates on new bonds considerably higher than during the halcyon days of the property boom.

Housing Related Consumer Price Inflation



Source: FNB

Now, "affordability" has more meaning in terms of running a home than buying a home.

Recent Consumer Price Inflation shows the housing and utilities component of the CPI to be the most troublesome and will be the main cause for concern for the foreseeable future. This sub-index makes up 22,56% of the total CPI - the largest weighting of any of the sub-components. Even before the huge tariff increases just announced, Escom has been a key driver of the housing CPI inflation problem, with the "electricity and other fuels" sub-index inflating by a massive year-on-year rate of 23,9% (see bar graph). Also worrying is the "water and other services" index , which also includes municipal assessment rates, showing a year-on-year inflation of 9,4%.

Over the next few years the housing CPI looks unlikely to change. And encouraged by Escom's success in passing on costs, financially-strapped municipalities are likely to try their luck, creating future acceleration in the inflation rate for "water and other services".

All this has serious implications for the overall CPI and adds to the Reserve Bank's burden as it tries to keep inflation below its 3%-6% target range.

And thus the affordability issue now extends far beyond simply the cost of servicing a mortgage bond.

The tariff increases are expected to lead towards a shift in the residential market - smaller-sized units gradually replacing large ones as households increasingly struggle to meet rising costs; smaller stands; lower standards; fewer servants' quarters and swimming pools.

Whether a mass swing to solar energy will be the panacea we seek is yet to be seen. Installation is expensive and Escom "rebates" remain inadequate. Furthermore, the solar trend appears to be firmly based on replacing electrical geysers. But there's more to home-running costs than hot water.