

PROPERTY BAROMETER – RESIDENTIAL BUY-TO-LET AND RENTAL MARKET

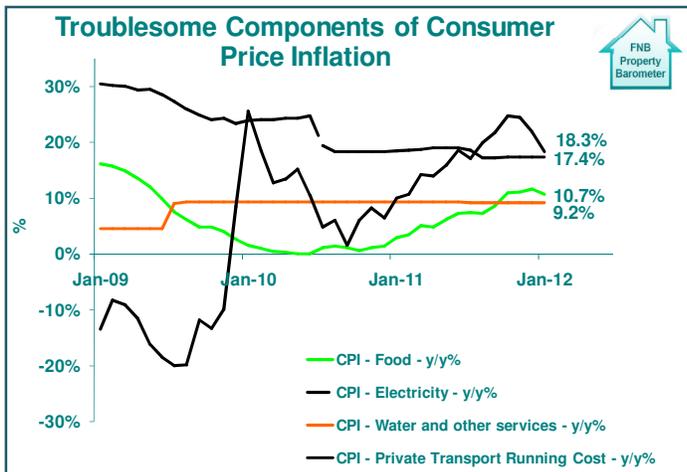
Buy-to-let buying remains in the doldrums and rental inflation directionless, and may remain so for some time. But a weak residential rental market may have been key in preventing interest rates from rising in 2011.

2 March 2012



Through 2011, the percentage of residential buyers that were buying properties to let was believed to have remained fairly weak, according to the FNB Estate Agent Survey. As at the 4th quarter survey, the sample of agents estimated that around 8% of total buyers were buy-to-let buyers, virtually unchanged from the previous 3 quarters and still a far cry from the near 25% recorded early in 2004.

However, one would think that this would imply some mild improvement in absolute terms, given that overall residential transaction volumes have gradually risen since 2009.

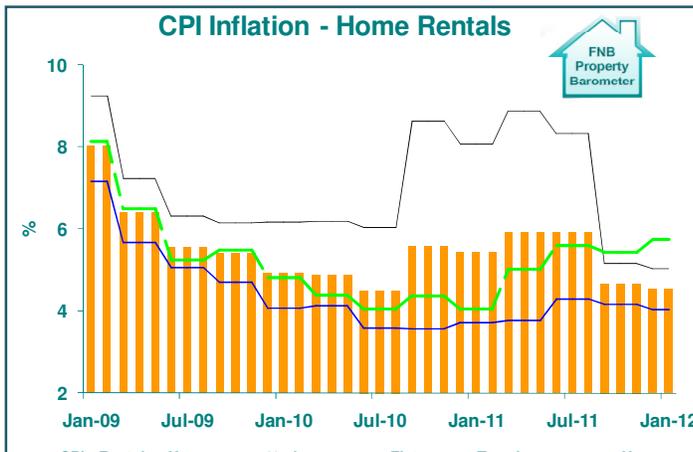


Nevertheless, the level appears to remain weak, as one would expect in the current situation of significant household sector financial pressure.

The sources of pressure have been a mediocre economic performance (despite some recent improvement), along with sharp increases in the costs of high frequency consumer purchases.

Although price inflation for petrol and food are starting to turn for the better, their inflation rates remain very high, and these highly essential items do exert a significant degree of financial pressure.

But more significant in limiting the appeal of owning a second home is arguably the ongoing increases in municipal rates, while utilities tariffs,



most notably in the area of electricity are skyrocketing. While utilities tariffs are generally passed on to the tenant in a rental property, the general levels of financial pressure in recent years must often have meant that the negative impact of utilities tariffs and other CPI inflation items, on tenants, limits the "pricing power" of landlords when it comes to hiking rentals.

And so, according to StatsSA CPI figures, weak residential rental inflation of 4.5% as at January 2012 was arguably the result of the other

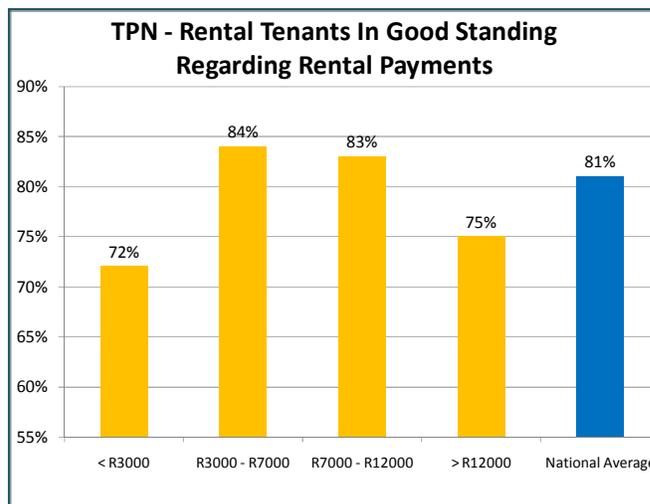
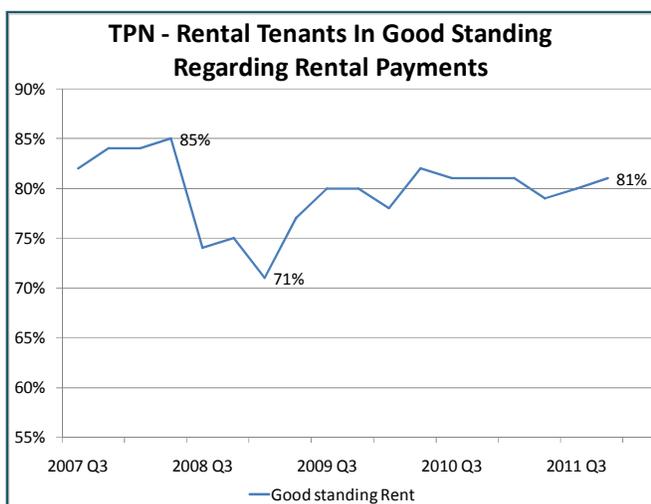
“crowding out” forces observed elsewhere in the consumer price index. In 2010, rental inflation had started to rise, and we had anticipated a strengthening in the rental market. This petered out late in 2011 after never really having seriously got going, and we believe will remain benign in the near term, curbed by the myriad of other consumer cost increases, along with the likelihood that personal tax relief this year will be insufficient to cover “bracket creep”.

In addition, first time buying picked up noticeably in 2011, suggesting that an increased number of young rental tenants moved out of the rental market and into home ownership, dampening rental demand

And so, the 2010/11 rental market period of slightly greater strength appears to have been short-lived, and it would appear that we have to wait a little longer as home buyer confidence (for primary residence purposes) appears to have mildly picked up.

Nevertheless, there are some signs that certain rental market fundamentals are improving. For one, low buy-to-let buying implies slow rental property supply growth, gradually laying the foundation for a future shortage which would lead to stronger rental inflation. On top of this, according to TPN (Tenant Profile Network), the percentage of tenants that are in good standing with regard to rental payments is on the increase. In the 4th quarter of 2011 this percentage reached 81%, the 2nd successive quarter of increase. It isn't back to the high of 85% reached in early-2008 just before the recession, but it is significantly better than the 71% low reached at the end of 2008 as recession hit.

Broken up into rental segments, it would appear that the middle segments are financially the healthiest. Below R3,000/month rentals one sees a lowly 72% of tenants being in good standing, whereas the Above-R12,000/month Segment fares little better at 75%. In contrast, the R3,000-R7,000/month (84%) and the R7,000-R12,000/month (83%) Segments achieve considerably higher percentages of tenants in good standing.



CONCLUSION

Buy-to-let buying remains weak, as does the rental market and thus rental inflation. Weak buy-to-let buying, however, does lay the foundation for the ultimate recovery of the rental market by constraining supply. However, it would now appear that significant strengthening in the rental market may be some way off, with credit-dependent 1st time buyers flocking into the home buying market in greater numbers as opposed to renting.

A weak rental market, however, may currently be a saving grace of the overall residential market. This is because of rental's (along with owner occupied rentals) large weighting in the consumer price index. Should the rental market have strengthened more significantly in 2011, at a time when other components of the CPI were rising sharply, overall consumer price inflation may have risen far higher above the 6% upper target limit, and that may just have been the catalyst for the Reserve Bank to start hiking interest rates.

For now, though, interest rate hikes appear to have been significantly delayed, and residential buying demand continues to grow gradually. How long before the rental market picks up? Our expectations for the start of interest rate hikes are around 2014, and we believe that this event would be the catalyst for a stronger rental market as many aspirant 1st time buyers delay their home buying, and rent for longer.

In the mean time, we expect to see further improvement in the payment performance of tenants, and ongoing buy-to-let weakness, which will pave the way for the ultimate rental market recovery.

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