

Residential Property Indices

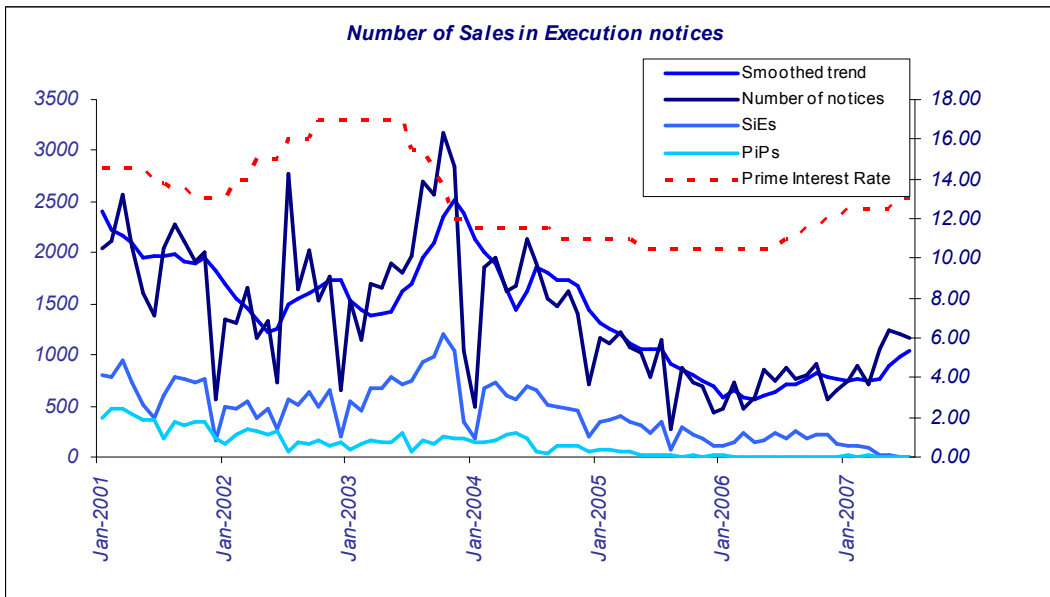
Press Release

PRESS RELEASE

SALES IN EXECUTION SET TO RISE AS INTEREST RATES BEGIN TO CLIMB

The recent trend of interest rate rises is beginning to have impact on the risk associated with lending into the residential property market. The number of notices of Sales in Execution (SiE) has begun to rise noticeably for the first time in over two years. SiE's arise where mortgage holders cannot afford their bond repayments, resulting in the bank foreclosing on the loan and selling the property on auction. On the other hand if the bank buys the property in house this is referred to as a Property in Possession (PiP), although these have become a lot less favoured by banks in recent times.

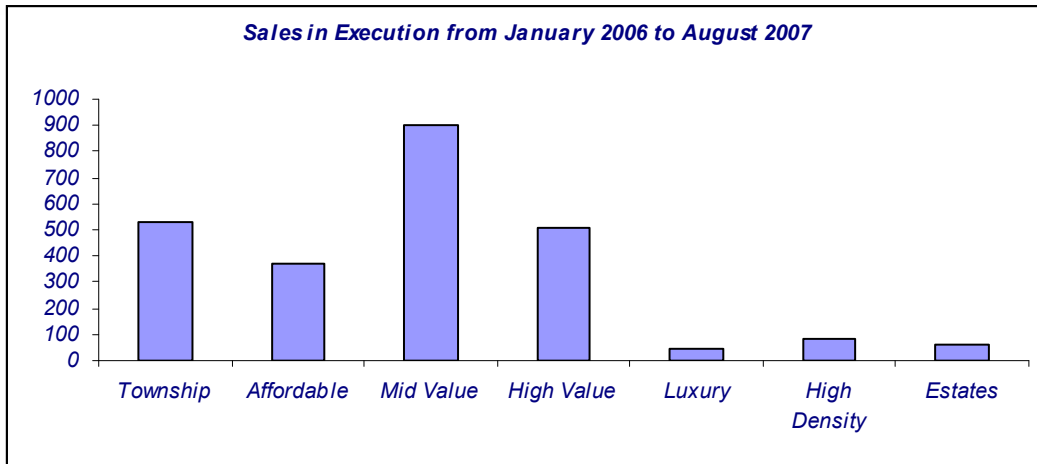
Although actual SiE's and PiP's currently remain at record lows with virtually none occurring over the last few months, notices of SiE's which are published in the Government Gazette have risen above 1,000 per month since June 2007, after remaining well below 1,000 for the preceding 2 years. This is still well below the peaks in 2001 and 2004 which were closer to 2,500 but does not auger well for the near future.



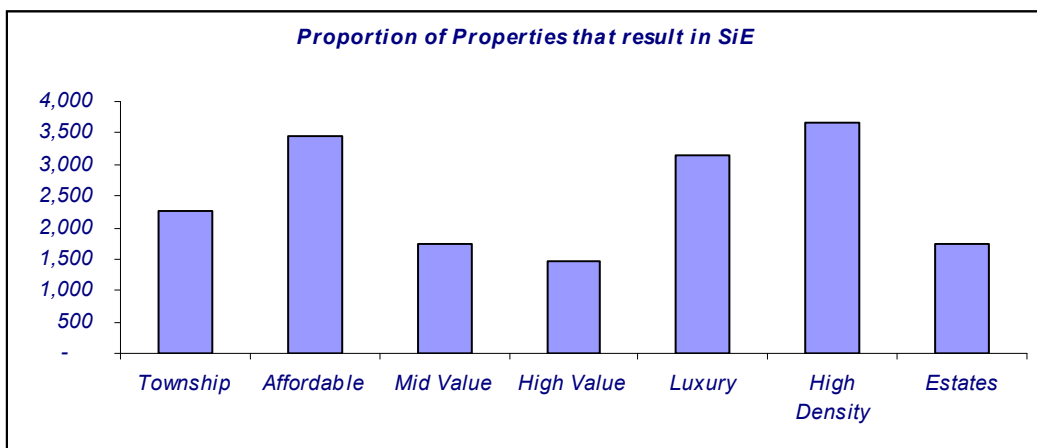
Historically, about 30% of SiE notices normally result in actual SiE's or PiP's. In other cases the mortgage holder manages to sell the property independently or manages to make other arrangements to finance his mortgage payments. Given this, we could expect to see SiE's rise to around 300 per month over the next year. Based on this conservative estimate, this would amount to R215m worth of properties being repossessed each month with the bank and owner likely to recover on average only 62% of the market value of these properties on auction.

However, the incidence of SiE's across different market segments, as one would expect, differs widely. If we analyse all SiE's since the beginning of 2006, we find the lower value market segments having many more SiE's than high value segments. Interestingly, at the lowest end of the scale however, the number of SiE's tails off slightly due to the lower proportion of bonded properties in that segment e.g. only 10% of township properties are bonded.

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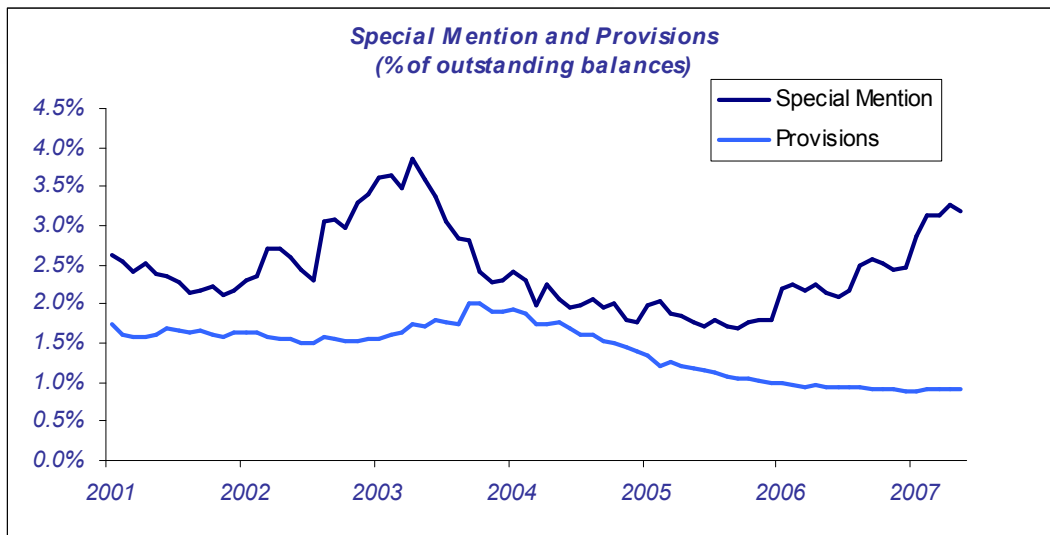


Therefore when we examine SiE's as a proportion of the number of properties in each segment, we see a more insightful trend. We find that properties in high density (inner city) and luxury areas have low incidence of SiE i.e. less than 1 house in 3,000 resulted in a SiE. Due to the low mortgage penetration in the lower value areas (townships and affordable areas) the incidence of SiE in these segments is also low i.e. 1 in 2,200 and 1 in 3,500 respectively. However it is in the mid-market where mortgage holders are most feeling the effect of interest rate rises, and where banks have penetrated more deeply, that the incidence of SiE's is highest. Mid value areas and high value areas have both seen as many as 1 on 1,500 properties sold in execution since the beginning of 2006. As a result of this the banks' provisions for credit losses are likely to begin to increase.



In their regulatory returns to the SARB, one can see that while actual reported provisions are currently still very low (<1% of total balances), "special mention" accounts which the banks have identified as at risk, have risen from 2.2% in January 2006 to 3.2% in August 2007. This is at levels last seen in early 2003 during which provisions rose from 1.5% to 2.0% over the remainder of that year.

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It is noticeable that the upward trend in special mentions was not precipitated by interest rate hikes, but actually started back in 2005. This is due to a steadily rising household debt-to-disposable income ratio since 2003, which has been driving the household debt-service ratio (the cost of repayment of the total household debt burden expressed as a percentage of disposable income).

The debt-service ratio peaked at only 8.8% at the height of the previous interest rate hiking cycle in 2002, and was contained by very low household debt levels (after cutbacks in the debt-to-disposable income ratio following the 1998 rate shock). This time around the debt-service ratio had already reached 9.8% by the second quarter of 2007. This ratio should have risen further given further rate hikes and still-strong household credit growth since.

Given higher indebtedness levels and debt-service ratio compared to 2002, we would be fortunate to get away with special mentions and provisions remaining lower than the 2003 peak during the current cycle. To get things in perspective, though, 2002 was an abnormally good credit cycle due to low debt levels, and it is unlikely that we are headed for anything near to the pain suffered at the peak of the cycle around 1998.

Definitions: Area values are defined as Luxury if the average house value in an area was above R1.5m as at December 2006, High if the average house value was between R700,000 and R1.5m, Mid value if the average house value was between R250,000 and R700,000 and Affordable if less than R250,000. Former townships (according to the Apartheid classification) are analysed separately to these segments.

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