

Are house prices really falling?

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The residential property market is currently under immense strain and sellers are struggling to get the prices they want. But whether SA house prices are currently in a plummeting phase, is a question to which there won't be an answer in the foreseeable future.

Standard Bank's economics department sent shock waves through the market last week with an announcement that during March house prices dropped for the first time in eight years. They were also 5,2% lower in the same month last year.

Just a few days later, Absa's house price index, which is widely accepted as credible and which has been in the market much longer than Standard Bank's index, indicated that house prices were 8,7% higher last month than in the previous year. Although this index still indicates the growth in prices, the trend is clearly downward.

An announcement such as the one made by Standard Bank can cause great harm to confidence in the market and should be judged with great caution.

The reason for the difference between the two house price indices and the tremendous confusion they create is the different ways in which the index is calculated.

Absa has been using the average house prices to calculate its index. Two years ago, when Standard Bank decided to also publish its own index, the decision was made to use the median price instead of the average price.

In layman's terms, the median price means the 'middle' price. For instance, the sixth price from the top is the median price if eleven houses are being sold in a month. Five are therefore cheaper and five more expensive.

Standard Bank defended its choice of the median price when it released its index, as a result of the fact that one or two exceptionally high prices have the ability to skew the average.

Absa's defence was that exceptionally high or low prices are excluded from its index by default in order to eliminate such distortion.

Only houses that are larger than 80sq m (currently selling for R400k) and houses cheaper than R2,3m are included in Absa's index.

However, the issue is that the median house price can also easily be distorted.

If, as agents allege, a greater number of cheaper houses and a smaller number of expensive houses are being sold, then the middle price will lie somewhere between the cheaper houses.

It is therefore possible that Standard Bank's price index is indicating a greater number of cheaper houses being sold, rather than house prices necessarily dropping across a broad spectrum.

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This suspicion is confirmed by Standard Bank's own analysis. The middle price of the bottom three quarters of the list was R295k last month, as opposed to R350k during the same month last year.

However, the middle price of the top quarter was R950k in March this year, as opposed to R900k last year.

According to this estimate the lower end market is starting to struggle, while the middle market, which Absa is largely measuring, is still heading upwards in accordance with Absa's price index – although not by much.

It will be interesting to see whether other price indicators are also saying that the lowest sector of the market, which includes the affordable market, is also experiencing increased price pressure.

It is true that people are buying cheaper houses because they are currently unable to afford more expensive ones - which will bolster the prices of cheaper houses - but the buyers in the lower segment of the market are usually also the hardest hit by rising interest rates and spiraling inflation.

So what do agents think of the confusion? Dr Andrew Golding, CEO of the Pam Golding Group, says the group's point of departure is still that if a house was sold for R1m last year, it will fetch a price of R1,1m or slightly less this year.

The perception of the falling prices was probably caused because the gap between the prices that sellers expect and that which the buyer is prepared to pay, is growing.

For instance, someone who bought a townhouse for R350k five or six years ago, is now placing the townhouse on the market for R1,3m and is then disappointed when it ultimately only fetches R1,1m.

The price it fetched might not have met the seller's expectations, but it's not clear whether it's an indication of falling prices. The sharp rises during the recent years have often created unrealistic expectations with sellers.

Golding says the current market conditions indicate that the residential property market has moved in the direction of a buyer's market. "Sellers are much more conservative with their offerings."

Buyers are also being forced in this direction due to the fact that they don't qualify for the same large mortgages as before because of the rising interest rates and the stipulations of the National Credit Act (NCA).

"In this scenario, sellers should adjust to realistic, market related prices in order to lure buyers, who now have a larger range of properties to choose from than before."

The number of properties being sold is currently 20% lower than a year or so ago.

Ronald Ennik, Pam Golding Group director and managing director for the Gauteng region, says

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sellers' perceptions of their properties' market value is still so unrealistic that he, in certain instances, advises his agents to convince their clients to lower the mandate price by as much as 20%.

He says the interest in property has indeed waned, but that the market is nowhere near the 1997 situation when show houses drew very few potential buyers.

"There are still very busy show house days in Gauteng, despite the downturn."

However, agents are performing five times more valuations than last year. This can indicate that after the strong growth in the value of properties over the last decade, some home owners want to convert this growth into money.

"However, the problem is to keep their expectations realistic." – David van Rooyen, SakeRapport

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I must compliment you on a very well-researched and informative article. However, exactly in this lies the answer to one or two of the questions raised in the article.

You raise the question that "people may get confused with the difference between the two indices". You must be correct, because I feel that Joe Public does not read this type of article as often as they should, and will therefore not really get confused. What they see in the news headlines are that "house prices are dropping" and that may motivate them to accept low offers from shrewd buyers or agents. Fortunately, the majority of people who do read it is involved in the industry and should be familiar with the indexes by now.

My agency specialises in the lower income areas, but is also represented well enough in the middle to upper market to be convinced that the number of units turned over in the sub-R500k market, has definitely increased relative to the rest. I personally feel that there are two main reasons for this, even though a lot of buyers in these price ranges are assumed to have risky credit records.

First, many buyers are reaping the benefits of affirmative action and BEE. Now, when purchasing a property, they often earn twice as much as they did a few years ago, hence the financial institutions are prepared to ignore bad records or defaults incurred when the applicant earned half his current income. Makes sense, doesn't it?

On the other hand, developments, especially of apartments below R500k, are commonly sold off plan within days (or even hours) from launch, to serious investors. I can assure you that many investors have doubled their portfolios in the past 12 to 18 months. Most agencies should have a database of such investors just waiting to get a first bite at new developments selling below R500k.

I predict that the relevant index will prove a year from now, that the average has decreased even further, as long as building costs can be contained reasonably with all the outside factors such as fuel costs, electricity and interest rates affecting it. -Marius Cronjé