

Research into Housing Supply and Functioning Markets



PRESENTATION TO FINMARK FORUM

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Settlement Dynamics
Contributors to housing, planning and development

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Presentation overview

1. Introduction
2. Scoping supply and demand
3. Functioning of the affordable housing market
4. Some conclusions

1. Introduction:

Purpose and objectives of the study

Financial Sector Charter commits the banking sector to provide some **R42 billion of which the vast majority will be applied to mortgage loans for housing units, with a maximum value of R180 000 per unit to households in the affordable housing sector** (households with a monthly income of less than R7500)*

The purpose of the study is to **understand the current dynamics and factors influencing the supply and demand for new and existing housing in the 'affordable housing market'** (with a mortgageable value of less than R180 000; targeting people with an income of between R2500 and R7500 per month)*

*CPIX adjusted

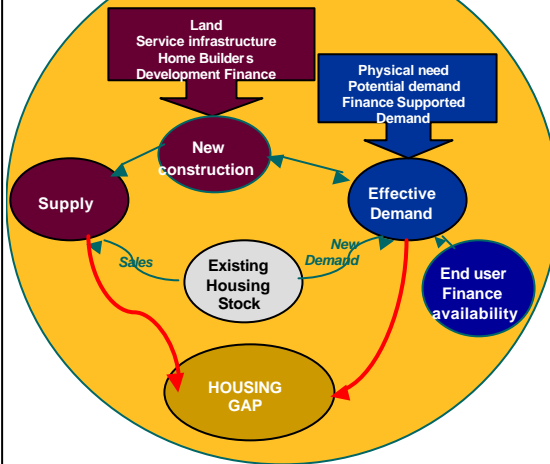
1. Introduction:

Key considerations

- **Affordable housing market** (assumed income of R2500 to R7500) is located in a general housing market. The performance of the affordable market sector is influenced by what is happening and not happening in the lower and upper segments of the general housing market.
- **There is no generally agreed econometric model** for the affordable market sector and currently **available housing data is poor**
- The supply of new affordable housing units is **fundamentally influenced by the significant process of transformation** in a legislative, jurisdictional and organisational sense that has occurred in Local Govt.
- **Macro economic conditions are currently generally positive** with inflation and interest rates being low and high levels of investment interest in the housing market
- The **gap between fully subsidised houses and current mortgage financed new housing supply** is significant and appears to be growing (currently about R35 000 – R160 000)
- The secondary housing market serving the target market (R2500-R7500) is **influenced by existing stock located in the previous 'Black, Coloured and Indian' Township areas**. This stock is still subject to a range of economic, social, administrative and physical factors which inhibit the operation of an effective property market. This impacts negatively on new housing supply.

2. Scoping Supply and Demand: Conceptual framework

Housing Model



Definitions: Need and Demand

Physical need – Determined by the number of households in the income bracket (pop projections, changes in household size, overcrowding and substandard accommodation). It is a stock variable i.e. total need at a point in time. It is an ideal which cannot be realistically addressed in a single time period.

Potential demand - It is a flow variable per year, taking account of a realistic rate at which physical need backlogs are addressed. The rate varies – Baseline Case is set that there would be a reduction in the shortfall in housing needed of 60% by the end of 2010, if the demand generated was fully financed and met by supply.

Finance supported demand – Applies lending criteria used by Banks - reflects households who qualify for mortgage finance, from the Potential Demand, on a year by year basis. (Factors applied are income, interest rate, repayment to income ratios and subsidy)

Effective demand - Determines the extent to which the supply of housing per annum meets Finance Supported Demand. Supply constrained is when supply falls short of demand. Demand constrained is when supply exceeds demand.

2. Scoping Supply and Demand:

Results

Modelling Outputs : Baseline Scenario: Housing Need and Demand (R2500 to R7500 income)

	2003	2004	2005	2006	2007	2008	2009	2010
HOUSING DEMAND								
No of Households [2.5-7.5k]	2,403,374	2,465,873	2,525,050	2,580,605	2,632,210	2,682,216	2,710,009	2,737,109
Housing stock needed units	2,446,329	2,509,946	2,572,494	2,629,723	2,683,237	2,734,629	2,763,681	2,791,318
Existing units	1,884,270	1,933,271	1,950,274	1,968,977	1,989,551	2,012,183	2,037,077	2,064,461
Physical need	562,059	576,675	622,220	666,745	693,686	722,446	726,604	726,856
Potential demand (60% of Need)								
Units	112,412	115,335	124,444	132,149	138,737	144,489	145,321	145,371
Rm Real 2005	11,766	15,727	17,805	18,356	19,043	20,153	20,784	22,000
Finance-supported demand								
Units	52,148	57,661	73,585	77,744	67,790	70,301	71,409	71,725
Rm Real 2005	5,458	7,863	10,528	10,799	9,305	9,806	10,213	10,855
Effective demand								
Housing supply new units	4,678	11,057	17,339	19,073	20,980	23,079	25,386	27,925
Housing supply new Rm	490	1,507	2,481	2,649	2,880	3,219	3,631	4,226
Effective demand units	4,678	11,057	17,339	19,073	20,980	23,079	25,386	27,925
Effective demand Rm	490	1,507	2,481	2,649	2,880	3,219	3,631	4,226

2. Scoping Supply and Demand: Results cont. Scenario Sensitivities : 2008

Scenarios	Housing need	Pot demand [units]	Fin Supported demand	Effective demand	Secondary trans	Total mort gen	Comments
Baseline	723,000	145,000	70,000	23,000	58,000	81,000	-
Sizwe	723,000	145,000	79,000	23,000	58,000	81,000	Finance supported demand little changed
1: 20% Supply Growth (up from 10% pa)	710,000	142,000	71,000	30,000	58,000	88,000	Effective demand increased due to supply constraint being partially alleviated. Significant increase in no of mortgages [8% relative to Baseline]
2: New House Price (Down to R90k from R130k)	723,000	145,000	121,000	23,000	58,000	81,000	Finance Sup Demand increased [69%] due to increased no of hh able to afford bond repayments of new housing. Effic demand - constrained by supply
3: Overcrowding Threshold (up from 1,5 to 2,0)	702,000	140,000	70,000	23,000	58,000	81,000	Physical need, Potential Demand reduced, Fin Supported demand reduced marginally. Effic demand - constrained by supply

Scenarios	Housing need	Pot demand [units]	Fin Supported demand	Effective demand	Secondary trans	Total mort gen	Comments
Baseline	723,000	145,000	70,000	23,000	58,000	81,000	-
Sizwe	723,000	145,000	79,000	23,000	58,000	81,000	Finance supported demand little changed
4. Interest rate reduction (From 2% to 1% above prime)	723,000	145,000	86,000	23,000	58,000	81,000	Fin support demand increases significantly [19%]. Effic Demand - constrained by supply
5. High growth (up from 4% to 6%)	723,000	145,000	103,000	23,000	58,000	81,000	Fin supported demand increases significantly [44%]. Effic demand - constrained by supply
6. Low growth (Down from 4% to 2,5%)	723,000	145,000	58,000	23,000	58,000	81,000	Fin supported demand decreases significantly [19%]. Effic demand - constrained by supply
Key findings: <ul style="list-style-type: none"> • New housing supply represents the most significant constraint to Effective Demand • A decrease in the minimum house prices and interest rate reduction result in a significant increase in Finance Supported Demand • Shifts in growth in the economy have a major bearing on the housing market 							
<small>Research into Housing Supply and Functioning Markets: Findings & Preliminary Action Plan</small>							

2. Scoping Supply and Demand:

Implications

- **Physical need** in the target market (R2500 to R7500) that is the shortfall between housing stock needed and existing housing stock is currently (2005) **estimated to be 625 000 units** .
- It is estimated that approximately **125 to 150,000 units need to be delivered pa** if the Physical Need is decreased to 60% by 2010.
- Of this applying current lending terms 75,000 to 88,000 units could be **financed by the Financial Institutions**
- **However due to severe supply constraints Effective Demand for new units is only around 15 to 20,000 units pa.**
- **The analysis of the scenario sensitivities indicates the following:**
 - **New housing supply currently** represents the most significant constraint to increased Effective Demand
 - **Actual loan conditions [particularly a reduction in interest rate], a reduction in house price and the economic growth rate could also impact on the level of Effective Demand** but only once new housing supply constraints are substantially resolved.

3. Functioning of the affordable housing market:

Approach

Three aspects researched:

- **New Housing Supply** focusing on:
 - Township development
 - Housing delivery
- **Process of transferring state owned stock**
- **Secondary (resale) housing markets**

Particular emphasis on detailing and evaluating supply / transaction chains and identifying dysfunctional elements

Methodology applied:

- Literature reviewed
- Workshops held or personal interviews with stakeholders
- Analysis undertaken
- Findings documented

3. Functioning of the affordable housing market:

New Housing Supply: Township Development

Land

Based on a review of IDP's of 11 of the 20 selected Municipalities and a IDP Review Process (2005) the following was determined:

- Many Local Authorities **are struggling to develop adequate housing sector plans** – only 12-15% have plans that are satisfactory from a development perspective
- Housing delivery not often seen as a core competence by Local Government. Especially for **bonded houses**.
- **Focus is on providing for the poorest of the poor**
- **Details on land identified for affordable housing and the provision of bulk infrastructure is consistently lacking.** The wider focus on housing delivery discussed in the Breaking New Ground policy has not yet been acted upon.

3. Functioning of the affordable housing market:

New Housing Supply: Township Development

Three legislative procedures: Ordinance, LFTEA, DFA. Ordinance most common and detailed below

Land procurement	Evaluating restrictive conditions of title and development potential of land Securing development rights or acquiring land Concluding relevant development and services agreements with Municipality	3/ 6 months ★ Tec/ Stat Risk
Township Application Preliminary Plan	All planning information obtained and a layout plan prepared by a town planner. Environmental and social impact studies undertaken	3 months
Environmental Mgt Plan Approval	EIA exception application submitted to DACEL. Exception application publicly advertised and interest groups invited to comment. Comments received and either accommodated or appealed against. Once resolved DACEL issues an approval	6/12 months ★ Tec/ Stat Risk
Approved Township Application and Conditions of Establishment	Planning report submitted to Municipality Townplanning Dept. Advertisement posted so all interested parties submit comments and objections. Once period expired and comments resolved report submitted to Council. Council approves township establishment. Conditions of Establishment prepared.	7/ 18 months (sometimes concurrent with EIA) ★ Stat Risk
Approved Gen Plan Engineering Designs	Complete cadastral survey (pegging) and drawing up of a General Plan. Forwarded to the Surveyor General for approval and then to the Deeds Officer. Detailed engineering designs prepared.	3/7 months ★ Stat/Comm Risk
Township Register	All conditions of establishment undertaken and documentary evidence submitted to the Deeds Officer. Deeds Officer examines all documents and opens the Township Register. Transfer documents for the first registration of title can be submitted	2/6 months ★ Stat Risk
Installation and Handover of Services	Tenders are issued and the installation of services is undertaken.	6/7 months ★ Tec/comm

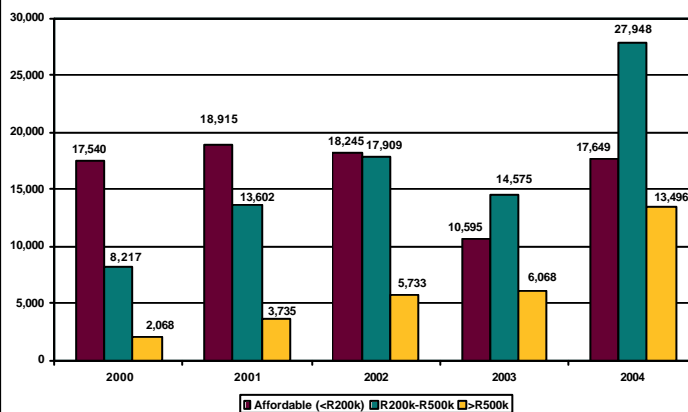
3. Functioning of the affordable housing market:

New Housing Supply: Housing delivery

- **Price of newly constructed housing increasing more rapidly than average income:**
 - Building and construction inflation increased prices by just over 50% between 2000 and 2005. This problem exacerbated by AML specifications which require high levels of services and single detached units (results in high land and housing costs)
- **The private housing delivery sector is migrating out of the affordable housing market in favour of higher priced units:**
 - Overall increase in the total number of housing units delivered between 2000 (28 000) and 2004 (59 000). However the proportion of total annual delivery comprising the **affordable housing market declined from 65% in 2000 to 29% in 2004.**
 - Total enrolments by home builders for the development of housing products below R200000 have remained static between 2000 and 2004 at about 17500 units. During this period the enrolments in the R200000 to R500000 price category increased fourfold.
- **The decline in delivery is more significant for housing units below R100 000:**
 - There was a 40% decline in housing products delivered in the R100 000 and below category with a shift towards providing housing units at the upper end of this category (7460 in 2000 to 4463 in 2004).

3. Functioning of the affordable housing market:

New Housing Supply cont: NHBRC Enrolments 2000 - 2004



- NHBRC data indicates that the private sector delivered a total of 196,296 houses from 2000 to 2004.*
- The affordable (<R200k) housing market's share over this period was 42.25% or 82,944 units.
- As an overall proportion of delivery, affordable housing has declined from 63% in 2000 to 30% in 2004, even though actual unit numbers have remained almost constant.
- The most dramatic growth in both numbers as well as overall delivery ratios has occurred in the R200k plus and especially the R500k plus segments.

* It should be noted that the inclusion of RDP units, while legally prescribed, is not consistent across the Provinces. However it is likely that a portion of the R50k and below units (only 637 delivered in 2004) are RDP units.

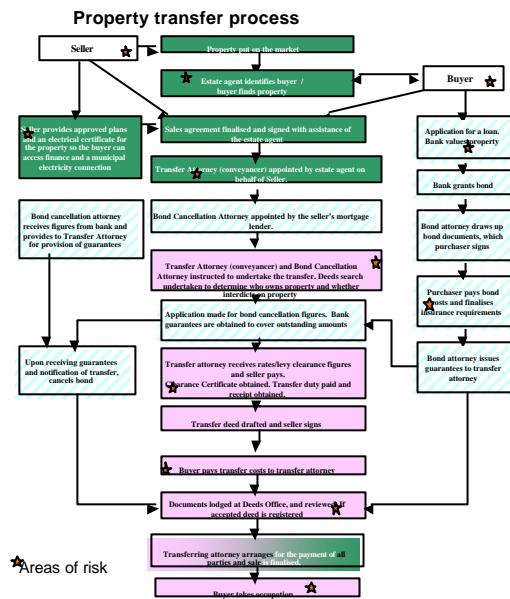
3. Functioning of the affordable housing market: <i>New Housing Supply cont. : Process – Hsg dev and indiv transfer</i>		
House design and bld plan approval	Plans and base specifications prepared and costed Provided to Municipality for approval and Lender for project funding commitments	1/3 months Com Risk ★
Sales Agreements Concluded	Development marketed. Offers to purchase processed and pre-screening undertaken. Bond application submitted to Lender	1/3 months Tec/Com Risk ★
Title and Bond Registration and Bond Drawdowns	Bond registration lodged and build order issued. Deeds Office register the bond. A clearance certificate requested from Municipality who undertakes valuation.	1/10 months Stat/Com Risk ★
House Construction and Handover	House constructed and handed over to new owner	2/3 months Tec/Com Risk ★

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3. Functioning of the affordable housing market: <i>New Housing Supply Constraints</i>	
<ul style="list-style-type: none"> ● Lack of access to well located and reasonably priced land: <ul style="list-style-type: none"> – Private sector land expensive – Public sector land not being assembled ● Serious delays in the land proclamation and servicing process: <ul style="list-style-type: none"> – Extended time duration and delays in land proclamation due to lack of Municipal capacity – Transparent and consultative process e.g. environmental provisions – Lack of existing bulk service capacity / uncertain delivery ● Decline in delivery of housing products and number of home builders operating in the affordable housing sector: <ul style="list-style-type: none"> – Operating risk increasing – Home builders margins reduced – Price increases reducing product affordability – Distortion due to the housing subsidy ● Delays in the registration of title and mortgages: <ul style="list-style-type: none"> – Inadequate capacity in Deeds Offices – Clearance certificates 	

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3. Functioning of the affordable housing market: Secondary housing markets : Transactional Analysis



3. Functioning of the affordable housing market: Secondary housing markets cont.

Conclusions

- Residential secondary market transactions involve key **technical, statutory and commercial risks**. In the affordable market **increased risks/difficulty occur alongside comparatively low returns**.
- The most common impact of risks is **delays and uncertainty** - research in South Africa found that:
 - 90% of transfers took longer than the benchmark figures
 - The higher the price of property the shorter the duration of transfer.
- Not possible to price for risk in affordable market. Therefore Sellers, Estate Agents and others **either avoid market altogether or absorb the increased costs**.
- **Higher levels of passivity in the affordable residential secondary market** – evidenced by the low levels of churn.

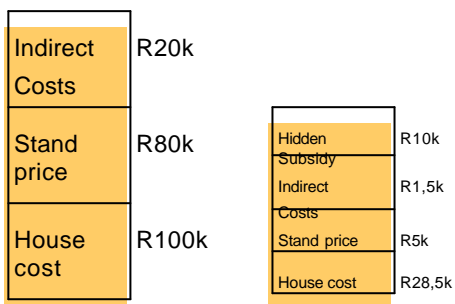
4. Conclusions

- There is **extensive potential demand in the affordable housing market estimated to be 125,000 units in 2005 increasing to 150,000 units in 2010**. In terms of **current lending practices the Financial Institutions should be able to provide mortgage finance to some 75,000 to 88,000 additional households pa**. The proposed Sizwe product makes **only limited change to Finance Supported Demand**
- **New housing supply currently represents the most significant constraint to increased effective demand**. Factors that could **impact positively on effective demand** are a reduction in interest rates, reduction in house price and the economic growth rate.
- **Housing Market processes are complex and high risk resulting in time delays, increased costs, uncertainty and limited supply:**
 - Land proclamation and servicing
 - Housing development and individual transfer
 - Property transfer in the secondary market
- **The Financial Institutions ability to meet the Financial Sector Target is limited by:**
 - Lack of **well located affordable land** with access to bulk infrastructure
 - **Lack of suppliers** wanting to participate in the market:
 - **Township Developers** to service land and **homebuilders** to build houses in the primary market
 - Estate agents, conveyancers and advertising in the secondary market
 - **Dysfunctionality in the affordable secondary residential property market is significant**
 - **Absence of a loan product that responds to income and product price realities** in the affordable housing market

4. Conclusions cont.

Product Price and Cost Realities

Affordable Housing	Fully Subsidised RDP House
R200 000 selling price	RDP House
42m ²	30m ²
Mortgage ± R208 000	Free



Implications

Affordable housing price/land structure

- **Stand price highly inflated** by land costs, shortage and municipal contributions

- **House cost under pressure** from building cost inflation

- **Overhead and profit margin insufficient** to justify risk and effort

Ongoing selling price increases

Further erode value for money compared to RDP house

Distort housing demand and willingness to invest savings

4. Conclusions cont.

Actions in respect of promoting increased mortgage lending in the affordable housing sector must focus on three priorities:

- 1. Improving housing supply at more competitive (value related) prices:**
 - Reduce risk, delays and scarcity impact of serviced stands
 - Increase cost efficiency of home building
 - Increase profitability to home builders
- 2. Improve efficiency and churn in secondary (resale) housing market:**
 - Improve transactional service provider support
 - Improve title accessibility
 - Promote awareness of property markets
- 3. Improve effective demand by expanding finance supported demand:**
 - Adjusted loan product
 - Reduced house loan value (savings, incremental, shared ownership or reduced specifications)

Generally these actions require substantial restructuring of the supply chain and regulatory framework for the affordable housing sector