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FNB/BER BUILDING CONFIDENCE INDEX

Issued by First National Bank

EMBARGO: Tuesday 17 June 2014
12:00

Growth in building activity slows in Q2

- The **FNB/BER building confidence index** fell 11 index points to 41, from 52 in 1Q2014.
- Confidence in all the sub-sectors making up the index was lower, with the confidence of manufacturers of building material registering the biggest fall.
- The building activity of non-residential contractors declined unexpectedly during the quarter while that of residential contractors continued to weaken.
- In sum, the growth in the building sector, which accelerated somewhat over the past few quarters, slowed in 2Q2014.

After breaching the key 50-index point mark in 1Q2014, the **FNB/BER building confidence index** fell by 11 points to 41 in 2Q2014.

The current level indicates that about 60% of respondents are dissatisfied with prevailing business conditions.

"*The 11 point drop in overall building confidence was largely due to a sharp fall in the confidence of <u>building material manufacturers</u>*" said John Loos, property economist at FNB. The decline in confidence was largely due to weaker domestic demand. Domestic sales and orders received were significantly lower than in 1Q2014. However, the export market remained buoyant, but this was not enough to boost confidence. According to Loos "*The slowdown in domestic demand could also partly be due to the prolonged labour unrest in the platinum sector and while exports, mainly to the rest of Africa, remained robust, volumes are small in comparison to the domestic market.*"

The weakness in the domestic building sector is further reflected in the activity of main contractors. Building activity for both residential and non-residential main contractors declined during the quarter. As a result, the confidence of main contractors edged lower to 45 index points in 2Q2014, from 49 in 1Q2014. "*While a further decline in residential building activity was expected, the slowdown in non-residential activity, which up until now helped lift the sector, was surprising. This will certainly weigh on the outlook going forward*" said Loos.

Despite the fall in activity, overall profitability improved. According to Loos "*This is possibly due to firms increasing their margins, especially in the residential sector. However, given the continued weakness in building demand this may not be sustainable.*"

After rising in 1Q2014, the confidence of architects and quantity surveyors declined to 47 and 45 index points respectively. Although the level of activity for architects was largely unchanged from 1Q2014, that of quantity surveyors worsened noticeably. This means that, in sum, the building pipeline deteriorated during the quarter. "*The slowdown in activity in the building pipeline suggests that the underperformance of the building sector seen this quarter may continue for the rest of the year*" said Loos.

One glimmer of hope remains retailers of building material. Although confidence edged lower in 2Q2014, at 55, the majority of respondents in this sector are still satisfied with prevailing business conditions. However, much of the optimism in the sector is as a result of a rise in order volumes (to be filled in subsequent quarters), while the growth in sales this quarter moderated. "*It is interesting to see the confidence of retailers remain relatively high. However, they represent only a small portion of the overall building sector*" said Loos.

Confidence of building sub-contractors fell to 43, from 47 index points in 1Q2014.

In conclusion: The results of the 2Q2014 survey suggest that just as the recovery in the building sector gained noticeably momentum, it was nipped in the bud. This is particularly true for non-residential contractors, where the growth in building activity moderated unexpectedly. In previous quarters, building activity in the non-residential sector was able to offset declining growth in the residential market. The fragility of the domestic market is further highlighted by the sharp decline in domestic sales for both retailers and manufacturers of building materials.

Although the results regarding the building pipeline are mixed, on balance it is negative. This dampens the outlook for the sector going forward. In addition, weaker economic growth will also weigh on the sector.

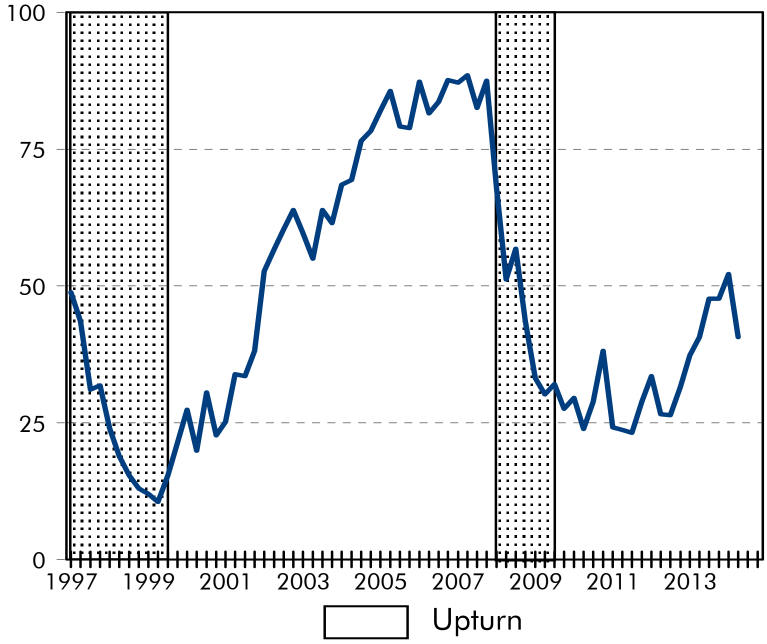
<u>About the survey:</u>

The FNB/BER building confidence index can vary between zero (indicating an extreme lack of confidence) and 100 (indicating extreme confidence). It reveals the percentage of respondents that are satisfied with prevailing business conditions in six sectors, namely architects, quantity surveyors, main contractors, sub-contractors (plumbers, electricians, carpenters and shop fitters), manufacturers of building materials (cement, bricks and glass) and retailers of building material and hardware.

In contrast to the RMB/BER BCI, which includes only main contractors, the FNB/BER building confidence index covers the whole pipeline, from planning (represented by the architects and quantity surveyors), renovations, additions, owner builders, the informal sector (represented by building material and hardware retailers) and production (manufacturers of building materials) to the actual erection of buildings by main contractors and sub-contractors.

The fieldwork of the second quarter survey was conducted between 5 May and 2 June 2014.

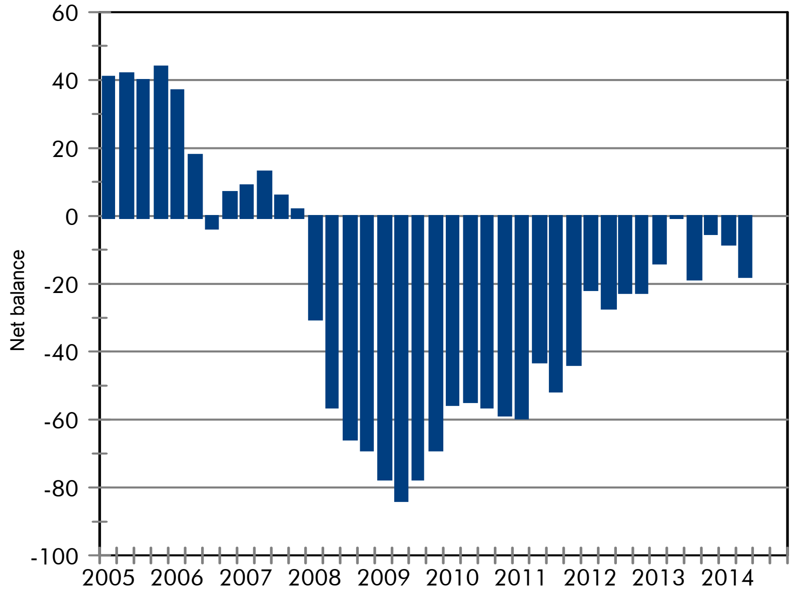
FNB Composite Building Confidence Index



Source: BER, Stellenbosch University.

Main Contractors:

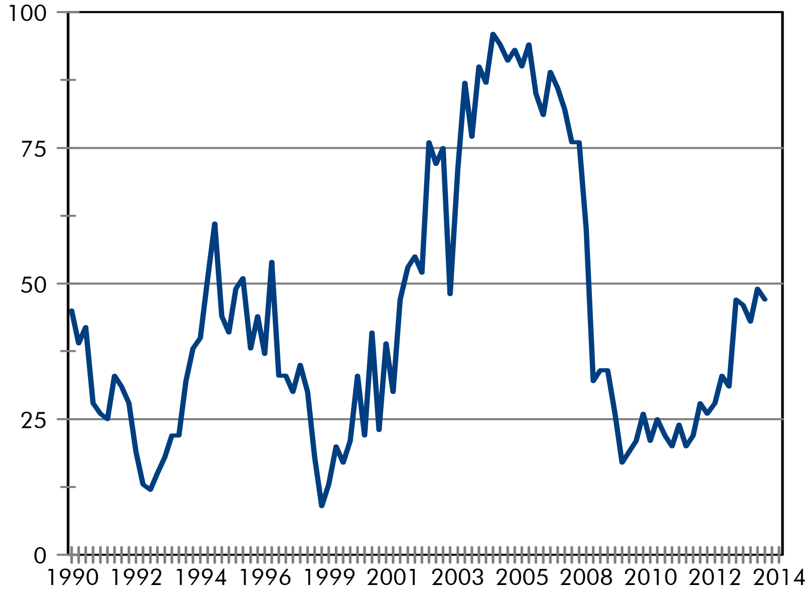
Growth in building activity (Net balance)



Source: BER, Stellenbosch University.

Residential contractors:

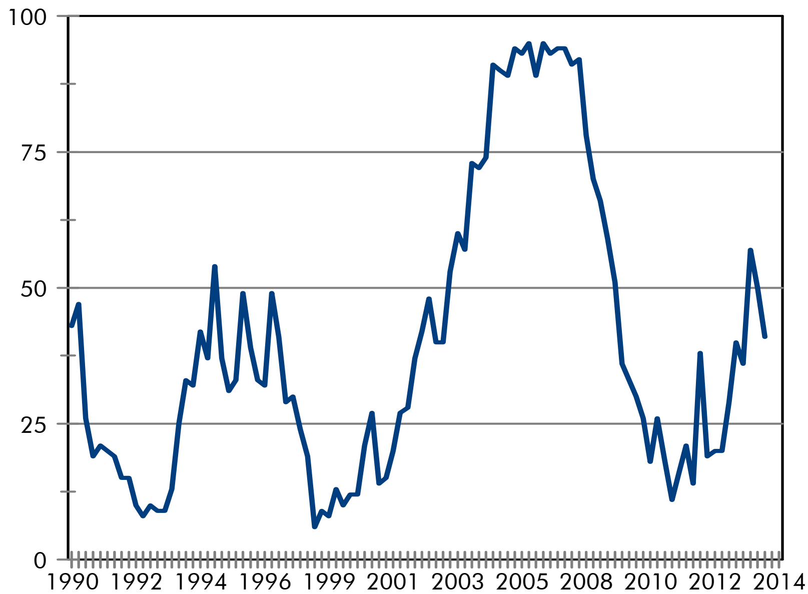
Business confidence



Source: BER, Stellenbosch University.

Non-residential contractors:

Business confidence



Source: BER, Stellenbosch University.