BIZCOMMUNITY

How interest rate hikes impact the homebuying market

Historically, interest rate hikes have had a dampening effect on the local residential property market, says Rhys Dyer, CEO of Ooba Group, along with reduced applications for home loans as buyers hesitate making a long-term commitment until rates stabilise and they can plan accordingly.

Rhys Dyer, CEO of Ooba Group

"Increased buyer education and understanding the purpose of why interest rate hikes are implemented can be a helpful tool in alleviating the affordability concerns of would-be buyers," he says.

Why interest rate hikes are implemented

The purpose of interest rate hikes is to curb inflation, i.e., the higher price of goods and services. The South African Reserve Bank (Sarb) chooses to implement a rate hike when inflation levels are high locally, as is the case at present, to 'cool off' the economy.

"To put this into context, the Sarb has an inflation target range of between 3 and 6%, and we are currently well above that with inflation at 7.6% in South Africa," explains Dyer.

"High inflation increases the cost of living for consumers and interest rate hikes are intended to slow down demand and spending, to reduce inflation again. Unfortunately, higher inflation also slows growth in the economy and getting the balance correct is essential."

When interest rates are high, the cost of repaying loans becomes more expensive, so consumers are less likely to take on additional debt. This reduces the demand for goods and services which causes prices to fall. "Unfortunately, this has a knock-on effect in the financed economy, most significantly the home loan market."

Local property trends to keep on your radar
Andrea Tucker 19 Dec 2022

Looking at the 'bigger picture'

Some would-be-buyers and first-time homebuyers have adopted a 'wait-and-see' approach out of concerns around affordability and repayments at a higher rate.

"This is a natural reaction, but it's important to put these rate hikes in context. The homebuying frenzy of 2020 and 2021 was the result of record-low interest rates introduced by the Sarb to stimulate the economy during a global pandemic. The latest round of interest rate increases has returned the prime rate to pre-Covid levels and should not be cause for panic," Dyer says.

"The revised interest rate is still well below the long-term average experienced over the past 25-years."

He believes that consumers should look beyond the current interest rate cycle and take note of the several 'big picture' factors that indicate that now is still a good time to invest in property. These include the bank's competitiveness and approving loans on attractive terms, the fact that we are moving into a buyers' market and that property prices remain affordable in many parts of the country.

7 residential property trends to look out for in 2023
14 Dec 2022

Buying vs renting: Which is better in the long-term?

Dyer acknowledges that some consumers may take these factors into account and still opt to rent rather than buy. "Buying a home is a decades-long commitment and in these turbulent times, some may prefer the flexibility offered by renting or are in a life stage where renting simply makes more sense than buying."

"However, to the question of whether it is cheaper to rent rather than buy a home following an interest rate hike, the answer is not necessarily straightforward. Landlords will often increase their rental charge following a significant hike as they look to cover their own increased costs."

Here, he reinforces the importance of thinking long-term and opting to pay off your own bond rather than someone else's. "Renting may be more affordable monthly but over the course of a decade (or more), you may walk away having spent a similar amount on rent as you would have on loan repayments and with nothing to show for it. In contrast, the value of a property asset will only appreciate over time."

Property outlook positive into 2023 despite rate hikes
Samuel Seeff 6 Dec 2022

The importance of shopping around for a home loan

The most effective tool that prospective homebuyers have at their disposal to reduce the negative impact of interest rate hikes is budgeting accordingly and cutting out unnecessary expenditure to ensure that they can afford to cover the additional monthly repayment costs.

The second is using a bond originator before embarking on their homebuying journey, says Dyer.

"The banks are still actively competing for home loan business and by using a bond originator to apply to multiple banks on your behalf, you are far more likely to get a better deal than if you'd applied to just one," he explains.

"A bond originator is also able to help negotiate a better rate and terms on your behalf when necessary. Our research shows that homebuyers who obtain multiple quotes will repay their home loan at an interest rate that is on average 1.03% (103 basis points) lower than those who obtained a single quote. This helps to reduce the affordability challenges brought on by rate hikes," he concludes.