Instalment Sales Agreement: an alternative home financing option in the property market.

By

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DECLARATION

I declare that this research is entirely my own, unaided work, except where otherwise stated. All sources referred to are adequately acknowledged in the text and listed.

I accept the rules of assessment of the University of Pretoria and the consequences of transgressing them.

This treatise is being submitted in partial fulfilment of the requirements for the degree of MSc (Real Estate) at the University of Pretoria.

It has not been submitted before for any degree or examination at any other university.

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Eduan Kruger

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“…the aspiration to house the nation is an

important part of strengthening the social fabric

of the country and will give people

self-esteem and dignity.”

Gavin Opperman – previous Absa Retail Bank CEO

ABSTRACT

Title of treatise:	**INSTALMENT SALES AGREEMENT: an alternative residential property financing option in the property market.**
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The study was conducted in attempt to investigate the viability of the *INSTALMENT SALE AGREEMENTS* concept in the South African residential property market. The study aimed to answer the pressing question on whether the concept of an *Instalment Sales Agreement* would stand ground as a viable alternative/option for both the purchaser as well as the credit provider for properties ranged above the governmental subsidy schemes and programmes and below R500 000 niche market of Gauteng.

This particular research aimed to investigate the core challenges as experienced and viewed by the main stakeholders in the process of furnishing and/or the acquisition of residential property whilst investigating and addressing adequate solutions beneficial to the respective parties as viewed and interpreted from their respective vantage points. The main concerns identified include primarily whether developers would find it feasible to develop and sell the said properties on the basis of an *Instalment Sales Agreement.* Secondarily whether prospective clients will be willing and able to purchase and secure residential property on the basis of an *Instalment Sales Agreement* as an viable alternative sales model whilst, accepting the concept

as a feasible and reasonable alternative to conventional and traditional property purchasing and acquisition methods on offer in order to achieve property ownership as opposed to possibly not being successful nor able to qualify to secure a home loans or government subsidy.

The research was undertaken in two sections. The first section of the research is a literature review that involves research on academic and other published sources which focused on the property industry as well as housing and/or finance methods of housing.

The second section of the research is the empirical research which was based on structured interviews and survey questionnaires. The empirical research was in addition based on an actual case study conducted and founded on an actual residential property development project by an influential and reputable property developer. The houses in this development project are sold on an *Instalment Sales Agreement* basis.

After comprehensively analysing all possible information and feedback at hand, it was clear to deduct that the *Instalment Sales Agreement* does undoubtedly offer an option whereby more prospective home buyers could qualify in order to purchase property due to the unique structuring of the financial responsibilities in such an agreement. It does however come with a few challenges in the market as well.

The *Instalment Sales Agreement* offers developers the potential of greater and accelerated demand in the marketplace resulting in more scope and opportunity in order to develop potential properties for prospective home owners. This phenomenon is mainly due to the revival and the establishment of a market segment that was previously lost to the developer. The Nett result will culminate in the provision of more financially feasible developments for the developer to explore. This in turn implies better income and profit margins for the developers.

With improved advertising and tenant education on instalment sales in the property market, the *Instalment Sales Agreement* is deemed to be a viable property financing alternative/option for both the purchaser as well as the credit provider in the residential property market for properties at a value above any government subsidy programmes but at the same time below R500 000 in the Gauteng province of South Africa.

Table of Contents

LIST OF TABLES

LIST OF FIGURES

LIST OF ABREVIATIONS

FLISP - Finance Linked Individual Subsidy Program

FNB - First National Bank

ISA - Instalment Sale Agreement

RDP - Reconstruction and Development Program

1. CHAPTER 1 – INTRODUCTION

1.1 Introduction

A house is a physical structure on a piece of land suitable for human habitation. It is a general tendency for people to strive and labour towards a sound financial position which will enable them to own a residential property that may become their home. Ownership of a property or merely just the ability to rent a property from someone else is often enough to grant people a sense of ownership, security and protection that they strive for. The first option, being ownership, requires a much larger capital investment but is mostly the preferred choice.

Traditionally in South Africa, as in many countries in the world, there are limited legal options available to the prospective home owner to gain formal access in order to secure ownership of residential property. These options range from purchasing a residential unit by means of a registered bond, obtaining ownership of a property by means of the Reconstruction and Development Programme (RDP) or renting a property, either from private owners or organisations like social housing institutions.

1.2 Background

The purchase of a residential property can be a stressful, but at the same time an rewarding experience. For the majority of people, the purchase and ownership of a residential property, constitutes the most valuable and expensive financial investment ever to be made by them.

Although most prospective home owners would need to finance the purchase of such a preferred residential property by means of an approved loan/bond, it would also represent their most valuable asset secured of their personal estate.

Griffin (2012:1) shortlisted some of the challenges that prospective residential property purchasers are faced with in the current South African economic climate when attempting to secure a property:

- Prospective home owners find it difficult to qualify for adequate funding due to strict NCA loan criteria.
- They find it increasingly more difficult to raise/save the deposit required by the financial institutions.
- Once the deposit and finance has been secured, most purchasers are unable to pay the transfer and bonds fees, including transfer duty and initiation fees.
- Distressed sellers cannot get their properties sold at market related prices and are left with no option but to face foreclosure by the Bank/Bondholder. Entering into an *Instalment Sales Agreement* will empower distressed sellers to manage their financial obligations to the bank without having to foreclose and the banks no longer face the prospect of having to sell property at a loss.
- In circumstances where prospective home owners with adverse credit records are forced to settle for rental option irrespective the fact or possibility that they may have the financial means to afford monthly bond repayments."

Traditionally the prospective home owner had only one of two finance options available to them. They either had to have had enough money saved up in order to purchase the property in cash or they could apply at a registered and accredited bank or financial institution for mortgage funding.

Due to the difficulty in raising funds to purchase a property, buyers are forced to explore alternative ways and means of securing and purchasing properties. *Instalment Sales Agreement*s are possibly one of the options for the prospective home owner to utilise. This entails that an approved credit provider may lend the purchaser money to purchase a residential property by means of an *Instalment Sales Agreement* (ISA). Through this option the credit provider will source and identify suitable clients in terms of their credit policy and offer an instalment sale option to them. Once the client has indicated and declared the intent and desire to purchase a particular property by means of the *Instalment Sales Agreement* option, the credit provider will initiate and proceed with a formal credit process.

The principals of an *Instalment Sales Agreement* contract applicable on a residential property are similar to that of for instance the principals of purchasing and securing motor vehicle finance and furniture finance.

The Alienation of Land Act, 1981 as cited by Griffon (2012:1), defines an *Instalment Sales Agreement* as an agreement of sale of land as defined in terms of the Alienation of Land Act, 1981 used or intended to be used mainly for residential purposes and in terms of a contract as defined in terms of the Alienation of Land Act, 1981 in terms of which the purchase price is paid to the seller by way of more than two instalments over a period of longer than one year. If the land is not held under a separate title deed at the point of entering into legal purchase contract, the period of repayment in terms of the contract may not exceed five years.

Lockyear (2008:1) states; “The seller retains ownership of the real estate and, therefore, has ultimate control over the title to the property. This is called “legal title” to the real estate.”

Ownership of the title deed of the particular asset only transfers from the legal owner of the property to the legal purchaser once the loan granted has been settled and covered in full. The legal buyer/purchaser will however retain the same rights, benefits and responsibilities as with mortgage bond finance.

In order to investigate whether an *Instalment Sales Agreement* is a viable alternative to home financing, knowledge of instalment sale funding and mortgage bond funding is essential. A brief discussion follows below

1.2.1 Basic comparison between instalment sale and mortgage bond funding

1.2.1.1 Instalment sale funding

A short discussion on instalment sales follows below in order to indicate some key aspects of the financing option.

- As stated earlier, Lockyear (2008:1, 2) indicated that, the title deed will remain in the name of the credit provider until such time that the purchaser has redeemed his/her debt in full.
- The client's interest (ownership) will be endorsed on the title deed of the property.
- Therefore on the title deed it will state that the purchaser bought the property and is repaying a financial loan (obligation) granted by the credit provider. The purchaser will therefore eventually become the lawful and rightful owner of the property, provided the agreement and terms of the loan are adhered to and the commitment to the credit provider is honoured.
- According to the Western Cape Office of Consumer Protector (2012:2), the purchaser will enjoy full rights and responsibilities of ownership of the property (purchased item). Normally a deposit will be required and the property can be

repossessed by the seller if the purchaser cannot honour his financial commitment.

- If the purchaser cannot meet the commitment as stipulated by the *Instalment Sales Agreement* the parties could cancel the credit agreement and voluntary vacate and surrender the property. No legal action will be instituted for breach of contract.
- Foreclosure with legal process ensuing on instalment default or contract breach.
- "Purchaser can sell the property at any time during the course of the *Instalment Sales Agreement*" (Smith, 2013:2)
- In the event of the purchaser passing away, their life insurance could settle the outstanding loan with the credit provider resulting in the title deed on the property being transferred to a legal beneficiary.

1.2.1.2 Mortgage bond funding

According to Lockyear (2008:1, 2):

- The title deed will immediately be transferred to the purchaser.
- A mortgage bond in favour of the bank will be registered on the property.
- It will therefore state on the title deed that a particular financial institution has provided funding for the purchase of the house.
- The bank will hold the original title deed, with the bond as security until the mortgage bond has been covered or repaid in full or legally cancelled.
- Cancellation of the mortgage bond will only be affected once the loan amount has been covered or repaid in full.
- Owner has full rights and responsibilities of ownership and use of the property.

- No option to cancel the credit agreement without full settlement of the outstanding amount. The purchaser must settle his financial duties to avoid legal action taken against him/her.
- Foreclosure with legal process ensuing on instalment default or contract breach.
- Owner can sell the property, settle the outstanding mortgage bond with the bank and make a possible profit during the contract period.
- In the event of the purchaser passing away, their life insurance could settle the outstanding mortgage bond with the credit provider and the deed on the property will be transferred to a legal beneficiary.

1.3 Problem statement and objectives

Financial institutions and banks in particular are bound by law, policy and set criteria that they have to adhere to when calculating and/or the assessment on whether or not a client qualifies for a bond. These criteria used by the financial institutions are often rigid and not flexible. In reality, policy prevents financial institutions from assessing the application of a mortgage bond on the bases of true and real individual financial ability, current and future commitment, performance potential and prospects. As a result a vast number of potentially sound and quality clients are turned down when they apply for a home loan.

The preliminary investigation suggests that the instalment sale funding product is based on sound financial principles and may be considered as a feasible financial mortgage bond alternative and solution, especially for true and sound applicants in the market segment above government subsidy and below R500 000. In essence it will allow for vast numbers of potential, otherwise unsuccessful, applicants' to gain access to the property market via an alternative but unique financial funding scheme that could be offered by credible credit providers.

1.3.1 Research questions

The main question this study aims to investigate and answer is, whether an *Instalment Sales Agreement* is a viable alternative for both the purchaser as well as the credit provider for properties above the threshold of government subsidy programmes and beneath the R500 000 level in Gauteng.

The first sub question that this study will aim to clarify is whether developers will find it feasible to develop and sell the said properties on the basis of *Instalment Sales Agreement* for the specific target market.

The second sub question that this study will aim to answer is whether prospective clients will be willing to purchase residential property on the *Instalment Sales Agreement* model and accept this as a feasible alternative to the conventional methods of purchasing and acquiring property.

1.3.2 Research objectives

The main objective of the said research, based on the reputable findings of the research questions, is an attempt to provide conclusive proof and evidence on whether or not properties sold in terms of an *Instalment Sales Agreement* contract could in fact be considered and employed as a viable and feasible alternative/option by prospective home owners and credit providers. In addition, it will attempt to determine whether it could contribute in providing a solution to counter an ever escalating shortage of home ownership in South Africa.

1.3.3 Importance of research results

This study will add to the knowledge base of home loan options and the feasibility thereof. The primary benefactors of this research study will primarily be clients aspiring to purchase properties but who do not qualify for a traditional home loan (mortgage bond).

The secondary benefactors will be the credit providers who will ultimately decide on whether or not to offer the *Instalment Sales Agreement* contracts to potential and aspiring property owners who otherwise do not qualify for the conventional mortgage bond.

On the tertiary level, this research could also be extended to further investigate the possible influence of the *Instalment Sales Agreement* funding scheme on work security and job creation within the building sector as it is envisaged that the benefits it holds could propel the demand for residential property to the next level.

Put in different terms, should the outcomes of this study reflect positively and prove beyond doubt that the *Instalment Sales Agreement* funding product can undoubtedly be regarded as a reliable and feasible alternative to conventional mortgage loans, and that as a direct result will enable more clients to afford residential property ownership resulting in the willingness of the prospective property owners to take up the financial responsibility of purchasing a property and start building on their personal financial 'empire', the *Instalment Sales Agreement* method of finance will gain its rightful support from developers and buyers alike.

1.3.4 Limitations and assumptions

The study will mainly be limited to affordable residential properties sector developed in the Gauteng province of South Africa.

Furthermore, the reality that only a limited number of registered private credit providers are currently providing the option of *Instalment Sales Agreement* as a product and option to property purchasing clients, might influence the diversity of the information gathered and as a result impact negatively on the results of this study.

1.4 Research approach and methodology

1.4.1 Research methods

Journal articles, structured interviews and questioners were the main methods utilised in order to gather information from the participating parties in an effort to obtain credible information for the study. In addition, the use of questionnaires and case studies formed an integral part of the research in order to ensure credible and reliable research results.

The following research methods were be used to conduct the research study:

<u>Literature studies:</u>

- A literature study on *Instalment Sales Agreement* conducted by various financial institutions, private credit providers as well as the Alienation of Land act 68 of 1981.

- Literature study on basic instalment sale concepts.
- Literature study on mortgage bond finance and other alternatives to instalment sales.

The literature resources that were used include journal articles, the internet and books.

Empirical research:

Empirical research were conducted and consisted of the following:

- Interviews with relevant stakeholders involved with property developers.
- Interviews and questioners with the financial director of property development companies.
- Interviews or/and questioners with prospective clients of *Instalment Sales Agreement* units.
- Case study on an actual property development project based on *Instalment Sales Agreement*.

The information obtained was accepted into the research full knowing that it had a particular influential impact on the outcomes and result of the study. This was done in order to further strengthen and secure the validity and reliability of the research results.

1.5 Conclusion

Purchasing a residential property can be an exciting yet stressful experience because of the difficulty in securing and qualifying for adequate finance. Traditionally home owners could only opt to qualify for a mortgage bond, usually hindered by an impending substantial deposit, at a financial institution or purchase the desired property in cash money.

The main objectives of the research were to obtain answers and direction that will serve as indicators on whether or not the *Instalment Sales Agreement* product is a viable option for residential properties above the government subsidy program qualifying brackets and less than R500 000 in Gauteng province, South Africa.

The research result will serve to indicate and advise private credit providers on how to go about offering the *Instalment Sales Agreement* Contract to prospective home buyers in future. The research will also indicate whether clients who do not qualify for a bond at a financial institution would be willing to purchase a residential property by means of the *Instalment Sales Agreement* contract. The study results also aim to clarify and point out the different characteristics between the conventional mortgage bond and *Instalment Sales Agreement* funding.

Credit providers will be able to lend prospective home owners the funds to purchase a property on an *Instalment Sales Agreement* Contract (ISA). The credit provider will identify suitable clients in terms of their credit policy and offer the *Instalment Sales Agreement* option to them. The title deed will transfer to the purchaser once the loan has been repaid in full. The buyer has the same benefits and responsibilities towards the property as with mortgage bond finance.

This study will look into the workability of this finance method, from a developers and also purchaser’s point of view.

2. CHAPTER 2 – LITERATURE STUDY

2.1 Introduction

For the majority of citizens security and dignity are non-negotiable fundamentals and of utmost importance in their own and their families live. There is little, if any, dignity in living on the street with no shelter from the elements or privacy to retract from the rest of the world.

Housing, by means of property ownership or merely just the ability to rent a property from someone else, is often enough to evoke or grant a sense of ownership, protection and the self-respect that they strive towards. A safe and secure environment, once acquired or secured, is often seen by the majority of society as the platform required from where an aspiring individual with potential will be able to excel and achieve set goals in life.

The purchase of the property, will more than likely, represent the most valuable asset secured by a legal person or persons and therefore will be considered to be of the most financial value of the individual's personal estate. Although housing provides for as a shelter and indeed as the most influential long-term financial investment and as a result will indeed influence the household's lifetime wealth prospects, affordability of housing requires a constant and relative sound sustainable source of income coupled with a remarkable cash flow burden in order to secure and ensure longevity of the investment (Xin Ge, 2009:34).

Affordability remains the single most key constraint for the majority of individuals in the South African housing market. The paramount issue in the affordable housing sector is credit worthiness and buyer affordability (Mhlanga, 2013:1).

Traditionally the prospective home owner had only one of few finance options available to them in order to secure a property. They either had to have enough and ample finances in the form of available cash money in order to purchase the property outright or, the prospective homeowner could follow the more preferred and traditional route by applying for a home loan or bond, as it commonly referred to, or mortgage funding at a registered and accredited bank or financial institution.

Obtaining and securing financing in order to successfully purchase a property is no new challenge for prospective buyers in today's day and age. It has been an age old challenge and dilemma for the majority individuals who are not necessarily wealthy enough to fund their own property purchases. The situation has of late, with the introduction of new financing legislation, escalated to near impossible and it is now even more difficult than ever before for prospective South African home owner or buyers to secure and obtain finance in order to purchase a property. In addition to the above mentioned legislation, the current global financial crisis has culminated into a situation whereby lenders are virtually and literally forced to be increasingly more selective about borrowers in the aftermath of the subprime mortgage crisis (Palmer, 2013:1).

Cited by Palmer, Keith Gumbinger (2013) believes that it is becoming increasingly more important and necessity for prospective home buyers to have a second source of funding available in the event of the initial deal being unsuccessful or collapse due to failure of securing finance.

Some of these options may include Government and private initiatives like Social Housing, Reconstruction and development program (RDP), Finance Linked Individual Subsidy Program (FLISP) and other Government Subsidies (depending on where the prospective buyer is positioned within general income group classification in South Africa).

Notwithstanding and even with intervention and aid of the above mentioned Government subsidy programs, only a minuet group of applicants do qualify for the said Government ‘bail-out’ options.

Thus, prospective home buyers that do not qualify for the above mentioned options still needs to seek alternative options when they find it difficult or near impossible to secure or qualify for conventional housing finance from credit providers. Therefore it is believed that an *Instalment Sales Agreement* can prove to be a workable alternative and solution, if not the only option, for the prospective home owner to explore. Through this particular means of credit provision it would entail that an approved credit provider can allow the purchaser of a particular property to purchase a residential property by means of an *Instalment Sales Agreement* (ISA). According to the Alienation of Land Act, 1981, the purchase price is paid to the seller by way of more than two instalments over a period of longer than one year.

By implication, the credit provider will source and identify clients with a suitable financial profile, in terms of their credit policy, and offer or propose the *Instalment Sales Agreement* sale option as a possible alternative to conventional credit solutions. Once the client has indicated and declared intent and desire to purchase a particular property, by means of the *Instalment Sales Agreement* option, the credit provider could initiate and proceed with a formal credit approval process.

2.2 Housing finance

The concepts of housing finance and housing finance systems have been evolving over time. Analysing definitions from the mid-1980s, it is evident that housing finance was defined primarily in terms of residential mortgage finance: “The purpose of a housing finance system was solely to provide for the funds which home-buyers required in order to purchase their preferred residential property or put otherwise, home. This is a simple enough objective but, due to its very nature and simplicity, it implied that the number of ways, methods and options open the applicant in which to achieve finance was extremely limited. Notwithstanding its basic simplicity and objectives a number of countries, largely as a result of government action and intervention, developed complicated housing finance systems. However, the essential feature of any system that must remain is the ability to channel the funds of investors to those in need of capital to purchase their homes. (Boleat, 1985:1)”

Consequently, a number of subsequent and much wider definitions have appeared in more recent years:

“Put simply, housing finance is what allows for the production and consumption of housing. It refers to the money we use to build and maintain the nation’s housing stock. But it also refers to the money we need to pay for it, in the form of rents, mortgage loans and repayments (King, 2009:3)”

Or even broader:

“There is recognition of other relevant forms of housing finance [apart from residential mortgage finance] such as developer finance, rental finance, or microfinance applied to housing. Developer finance is often in the form of unregulated advance payments by buyers, and developers sometimes provide long-term finance to buyers through instalments sales when mortgages markets are not accessible. Microfinance for housing is typically used for home improvement or progressive housing purposes. Loans are typically granted without pledging properties. Although the overall impact of microfinance in housing remains limited, this activity can represent an important source of funding for those in the informal sector. (Chiquier, 2009:xxxii)"

Thus, the purpose of housing finance systems is solely to provide individuals with the necessary funds which they require in order to purchase a property or home.

2.3 Current housing market in South Africa

Loos & Swanepoel (2013:2), stated the following about the housing market: "The residential market is in an interesting "space" at present. On the one hand we have had signs of gradually improving demand along with increasing supply constraints. On the other hand, we have had a slowing pace of real household disposable income growth in recent times, resulting in weakened consumer confidence according to the FNB Consumer Confidence Index. It thus seems to be a case of the housing market moving in the opposite direction to the consumer economy"

But perhaps this is not the case, it might be a case of role-players in the property market having become so used to the weak performance in the housing market from 2008 onward, that 6-7% house price growth appears strong (Loos & Swanepoel, 2013:2).

Loos and Swanepoel (2013:2) added that the range of house price growth is only just keeping ahead of consumer price inflation, and is thus not yet strong in real terms. The First National Bank (FNB) Valuer's Market Strength Index remains below 50, which still indicates that supply is stronger than demand and in the FNB Estate Agent Survey, while more agents are pointing to stock constraints, the estimated average time of houses on the market still seems a bit longer at around 17 weeks (FNB 2013 2nd quarter survey) this supports earlier statements claiming that demand is still lower than supply currently.

Therefore, while the residential market has been on the mend for some time, in terms of demand relative to supply, it is a slow process, and 6-7% average house price growth should not be seen as strong, given where our country's general inflation rate is at the moment.

In the *House Review* of the second quarter of 2013, Jacques Du Toit, property analyst for Absa Home loans stated that the second quarter of 2013 saw the average nominal price growth of affordable housing (homes of 40m² - 79m² and priced up to R515 000 in 2013) continuing its gradual downward trend of the past three quarters to3,6% y/y since peaking at around 7% in the third quarter of 2012.

The slowdown in year-on-year price growth came on the back of the base effect of accelerating price growth in the corresponding quarters of the previous year. In reality prices in the affordable segment dropped by 2% year-on-year in the second quarter this year. The average price of a home in the affordable segment of the market was R345 600 in the second quarter of 2013 (Du Toit, 2013:5).

Figure 1 offers insight into the demand and supply in the residential property market since January 2001.

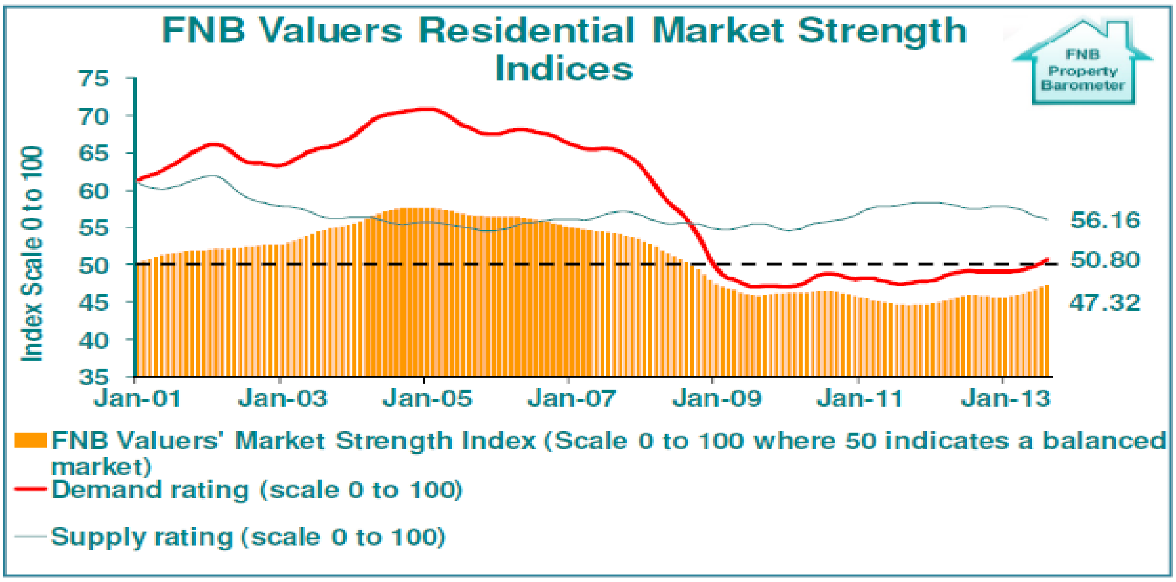

Figure 1: Valuers Residential Market Strength Indices

(Source: First National Bank)

Figure 1 shows that the residential property market strength indices are slowly recovering. The demand rating is slowly but surely catching up to the supply rating which in turn indicate that the residential housing market is recovering and that the consumer confidence is on the up.

Figure 2 offers insight into the residential market strength as well as house price growth since January 2002.

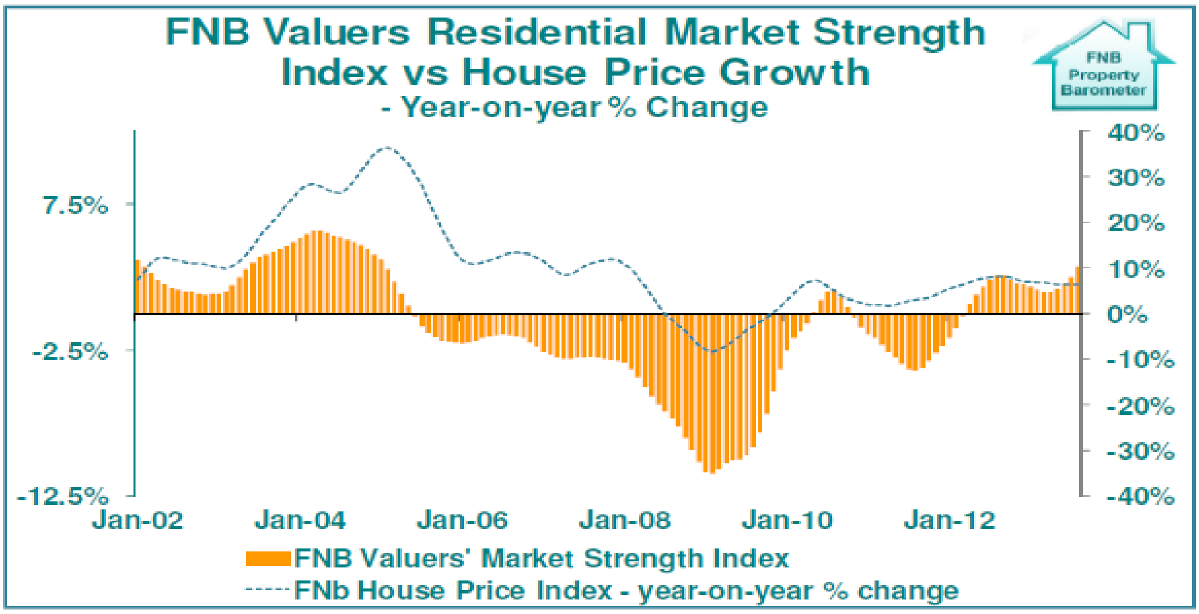

Figure 2: Valuers Residential Market Strength Index vs House Price Growth

(Source: First National Bank)

Figure 2 shows that a current 6-7% house price growth index, which is currently merely higher than inflation. This figure indicates that the recovery phase in the residential property market is a slow and long process.

2.3.1 Trends in the current household sector

Du Toit (2013:8) pointed out that trends in household sector finances will continue to be driven by macro-economic factors such as economic growth, employment, inflation and interest rates.

According to Du Toit (2013:8) the following trends are to be expected in household sector related variables in 2013:

- Employment growth of 0,9% is forecast following a growth of 0,6% in 2012.

- Growth in real household disposable income is expected to slow down to 2,6% from 3,8% in 2012, affected by upward pressure on inflation and only moderate employment growth.

- On the back of a continued low level of savings, real household consumption expenditure growth is projected at 2,6% (3,5% in 2012) and is expected to remain closely correlated with income growth.
- Household consumption expenditure is forecast at 60,7% of GDP in 2013 (60,4% in 2012), implying that the household sector will remain an important part of the economy and driver of economic growth.

- With lending rates forecast to remain low for longer and levels of saving not expected to show a substantial improvement, the household sector will continue to largely rely on credit for funding consumption expenditure, with the result that the debt-to-income ratio will remain above the 75% level after being at 75,6% in 2012.

- The cost of servicing household credit as a percentage of disposable income is forecast to remain under control in view of continued low interest rates and a relatively stable debt-to-income ratio.
- The credit-risk profiles of consumers are not expected to show a significant improvement from current levels, impacting the accessibility of credit and household consumption expenditure.

According to Du Toit (2013:8) summary it can be deducted that in the near future the proposed purchaser will most likely find it even harder to free up money for savings and residential purchasing property and they will rely immensely on the availability of credit to purchase property.

2.4 Government's influence on housing backlog in South Africa

Housing, along with education, was one of the new government's main promises to the black majority (Sally, 2001:1).

South Africa's housing and finance policies have paid explicit attention to housing affordability since 1994. Understanding that majority of the population could not afford housing and facing an estimated housing backlog of about three million units, the 1994 government implemented an ambitious and far-reaching national housing subsidy programme (FinMark Trust, 2012:125).

Figure 3 offers insight into the affordability of housing in South Africa in 2010.

Figure 3: South African Housing Affordable Pyramid (2010)

(Source: FINMARK TRUST 2010)

Figure 3 clearly indicates the lack of a housing product for 20% of the country's population.

In 1996 the Constitution of South Africa laid a new foundation for housing in South Africa. Housing was declared a fundamental human right, embodied in section 26 of the constitution, stating that every citizen of the country has a right to have access to adequate housing (Moss, 2001).

While the government provides a comprehensive and substantial housing subsidy, its capacity to meet the growing backlog is seriously challenged, especially given reduced GDP growth rates and rising unemployment. Current estimates suggest that while the government has been delivering houses for the poor through housing subsidy scheme, the housing backlog remains on the increase (Financial and Fiscal Commission, 2011). as shown in table 1.

Table 1: **Housing Backlog from 1996-2011**

Year	Housing backlog
1996	1,5 million
2001	1,8 million
2011	2,1 million

(Source: Department of Housing, 1994 and Department of Human settlement, 2011.)

The above table reflects that the backlog stood at 1.5million in 1996 only two years after a change in government in South Africa. The backlog was standing at 2.1million in 2011. This indicates that the housing backlog in South Africa is still inclining drastically despite all the efforts and subsidy programmes from the government.

Due to the massive backlog in the South African housing market, Government has since 1994 been constantly engaged in exploring and investigating new alternatives and methods of providing housing for the people of South Africa and or as an even better solution, to help finance people with the purchase of their own houses since. Through this approach, Government is aiding and attempting to help increasing the number of home owners countrywide and as previously stated housing in particular as ownership creates wealth.

2.4.1 Reconstruction and development program (RDP)

The Reconstruction and Development Programme or RDP subsidy, entitled all households earning less than R3 500 a month as well as meeting a range of criteria in addition, to apply for a fully subsidised residential property or put in different terms, a house. In terms of the RDP programme, subsidy beneficiaries get freehold title to a 250 m^2 serviced stand with a 40 m^2 top structure, entirely for free. The programme continues at present be it with a few modifications and has delivered an estimated 3 million housing units (FinMark Trust, 2012:125).

Despite the RDP scheme firmly in place for almost two decades, Financial and Fiscal Commission (2011) current estimates suggest that while the government has been delivering houses for the poor through housing subsidy schemes, the housing backlog continues to rise.

2.4.2 Subsidy program: Finance Linked Individual Subsidy Program (FLISP)

One of the most recent Government subsidy methods is a *Finance Linked Individual Subsidy Program* (FLISP)

2.4.2.1 Background on FLISP

In September 2004, the Minister of Housing Ms Lindiwe Sisulu presented her new housing strategy entitled "Breaking New Ground" to cabinet. The strategy was approved and now forms the basis of all government activity in respect of housing policy. The strategy included the new housing subsidy program linked to mortgage finance called *Finance Linked Individual Subsidy Program*.

Due to the structural and logistical difficulties during implementation of FLISP at the time (deposit requirements, claw back and other onerous factors), banks withdrew from all FLISP related activities.

During his state of the nation address, the President of South Africa announced that a revised FLISP will be implemented in April 2012. The National Housing Finance Corporation (NHFC) have been appointed as the implementation agent, they would interact between the Banks, Government departments and developers. The formal implementation of FLISP took place on 14 June 2013.

Figure 4 offers insight into the affordability of housing in South Africa in 2012 and also shows the introduction of FLISP in the South African Housing market and the target market of the FLISP programme.

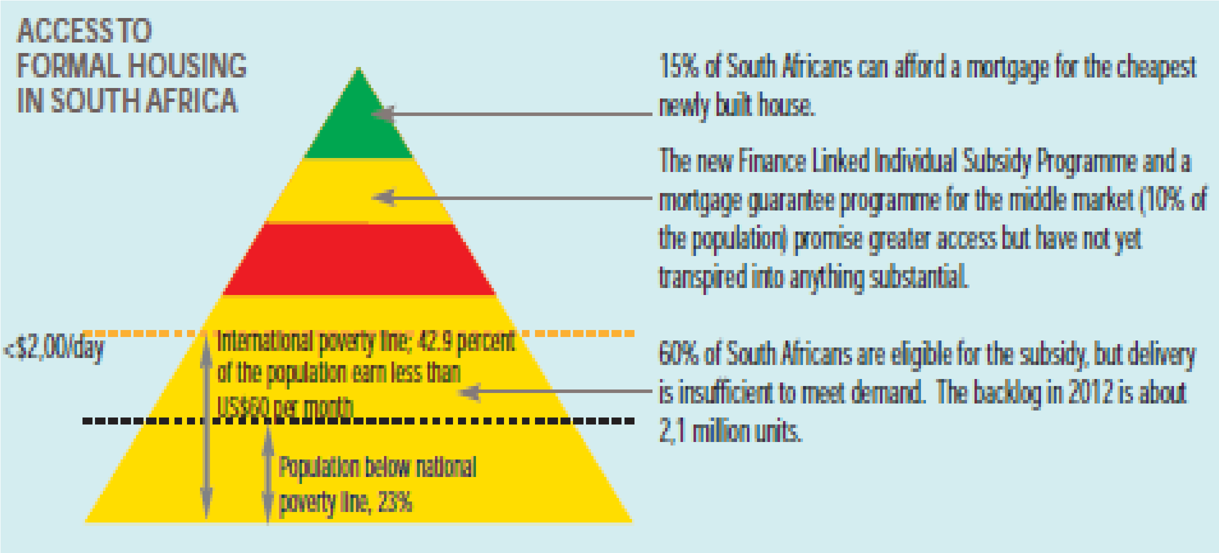

Figure 4: South African Housing Affordable Pyramid (2012)

(Source: FINMARK TRUST 2012)

Figure 4 indicates that 15% of South Africans are currently in a position to afford a mortgage bond for a residential property/house. Figure 4 further demonstrates that with the introduction of the FLISP programme, this margin could increase in order to accommodate approximately a further 10% of the population with the opportunity to also qualify for a subsidy which will provide them the opportunity to purchase a residential property.

The main objective of FLISP is to target the “GAP’ market in the South African housing pyramid (Indicated with the colour red in figure 3). FLISP is a response and proposed solution to affordability challenges faced by households earning between R3 501 and R15 000 per month, this income bracket has been classified as the so called “Gap Market”. This target market could qualify to receive a subsidy grant of between R87 000 (income R3501) and R10 050 (income R15000). The criteria set in order to qualify, includes the maximum purchase price of a property to be financed to be no more than R300 000. In addition, the FLISP subsidy must be utilised to reduce the principal debt to render the amortisation of the loan balance over the loan period more affordable.

FLISP will provide a subsidy to qualifying households that have secured mortgage finance to:

- Acquire ownership of existing improved residential property.
- Obtain vacant serviced residential stands that are linked to household building contracts with home builders registered with the National Home Builders Registration Council ("NHBRC").
- Construct a new residential dwelling, assisted by a homebuilder registered with the NHBRC, on a serviced residential stand that is already owned by the beneficiary.

2.4.2.2 FLISP Target Market:

The target market that FLISP is aimed at is specific. This market includes the following:

- Income between R3501 to R15000.
- Property Purchase Price of the less than or equal to R300000.
- First Time Home Buyer.

2.4.2.3 FLISP benefits to customer

Table 2 demonstrates the two different options, pre and post bond application benefits, that the FLISP programme offers to benefit the buyer.

Table 2: FLISP options

Option 1 (FLISP applied pre-bond registration to lower loan amount at application)			**Option 2 (FLISP applied post bond registration)**		
Purchase Price	R 300,000		Purchase Price	R 300,000
FLISP	R 50,000		FLISP	R 50,000
Approved Loan Amount	R 250,000		Approved Loan Amount	R 300,000
Balance after REG	R 250,000		Balance after REG	R 250,000
	Better interest rate			Higher interest rate
	Lower LTV			Impact on LTV
	No impact on Mandates &Scales			Impact on Mandates &Scales

(Source: National Housing Finance Corporation Soc Lt)

Table 2 indicates that both options are available to the customers, as detailed above. However, through Option 1 the customer will receive better benefits from the bank in terms of:

- Better interest rates for customers through lower Loan to Value.
- Lower instalment repayments for customers, by means of lower interest rates applicable (FLISP).

- Normal lending credit criteria will apply as prescribed by the National Credit Act.

Thus option 1 would be the preferable option for the home buyer.

2.5 Implications of the National Credit Act on housing finance

The National Credit Act of 2005 was found to promote a fair and non-discriminatory marketplace for access to consumer credit. It stands to provide for the general regulation of consumer credit and improved standards of consumer information. It further seeks to promote black economic empowerment and ownership within the consumer credit industry and to prohibit certain unfair credit and credit-marketing practices (Government Gazette, Republic of South Africa, 2006).

One of the act's main purposes is to promote responsible credit granting and to serve as a tool to prohibit and eradicate the practice of reckless credit granting.

According to Davies (2013:1), the *Instalment Sale Agreement* would appear to be the solution in situations whereby a prospective home purchaser does not qualify to purchase a property. Unfortunately, due to the introduction of the National Credit Act, there are as a result a number of challenges in concluding an *Instalment Sale Agreement*.

Davies added that ultimately it is the seller who provides the credit and therefore has to comply with the National credit Act. This implies that, if the amount that needs to be paid off is more than R500 000, the seller will have to register as a credit provider. As the credit provider, the developer is therefore by implication faced with the predicament to establish and ensure that the purchaser can afford and repay the amount in monthly instalments as well as service outstanding financial responsibilities due and owed. This entails that the seller must assess and evaluate the full financial situation and position of a purchaser.

The *Instalment Sale Agreement* as an option is primarily chosen as a direct result of a bank or financial institution opting not to finance the purchaser after, what is considered to be, a full financial assessment and evaluation of the prospective client. Thus, the seller/developer are now faced with the challenge and predicament to establish and prove why he/she believes the purchaser can in fact cover, repay and meet the purchase price in instalments in contradiction to the bank's findings and choice not to finance the purchaser. The mere fact that the bank didn't accept the purchaser's application indicates the possibility that the purchaser does not have the necessary financial resources, discipline or backing to qualify for the credit margins applied for. By implication it could imply therefore that should the credit provider approve and accept to finance the said purchaser on an *Instalment Sale Agreement* contract it might be considered to be viewed as reckless lending practices. This however might not necessarily be the case due to different criteria employed and utilized and applied to assess and evaluate the purchaser's application. In addition, interest rates which the seller is prepared to charge, may be less than those of the financial institution.

While many believe the National Credit Act saved South Africa from the credit crunch, others believe it shouldn't have been introduced in South African property realm, because there were enough evidence and it was crystal clear that the banks were not involved in malpractices of lending money recklessly, before the introduction of the Act.(Davies 2013:1)

Davies added that the Act is now hurting the very people that it intended to protect. As a direct result of the constraints imposed by the National Credit Act, many aspiring home owners do not have access nor have the ability to qualify for financial assistance and are therefore deprived of the possibility to obtain mortgage bonds which in effect reduces the property values in the country. The net effect of which is that many people are now in a disposition and as a result cannot purchase a property in South Africa. They are forced to rent a property, resulting in an inflated increase in the demand for rentals. The outcome of which is an increase of rentals to a point higher than it would have been had more people been able to purchase properties. The result is that the very people that were supposed to be protected are now suffering most because they cannot afford a residential property. To make matters worse they are now increasingly faced with the prospect of also paying inflated rentals due to ever growing and over demand for rental properties and the pending under supply.

2.6 Instalment sale funding

Instalment Sale Agreement funding was relatively fashionable in the late 1990's in South Africa. At the time interest rates were peak of 26%. Currently, consistent with the recent credit crunch, purchasers are again experiencing difficulty in obtaining finance from the banks and hence the revival of the Instalment Sale (Forrest, 2011:2).

Over the years the property market has seen many up and down turns. An ever-changing and evolving economic climate and environment has forced property owners, prospective owners and marketers to develop new and indifferent ways and methods of marketing, selling and acquiring real estate. The options favoured will most likely proof to be the option that suits the consumers pocket as opposed to the most convenient option. Recent years have proved to be especially tough on all buyers, whether it is prospective first time home buyers or even current property owners. In the aftermath of the economic crises it is virtually impossible to secure a home loan in some cases, while many home owners faced foreclosure due to the recent recession. Another challenge the seller face nowadays, is a considerably diminished sized market that transpired as a direct result in which to sell their properties in. It is at times like these, if one wants to stay ahead of the ever changing economic market, that one should consider alternative methods when purchasing or selling property. One option to consider is the *Instalment Sale Agreement*, an option that was widely used in the nineteen seventies in the South African Property market.

Instalment Sale Agreements are contracts between the buyer and seller for the transfer of the property over a period of time. Under this agreement, the buyer makes periodic (normally monthly) payments to the seller of the property. The seller retains ownership of the property and therefore has ultimate control over the title to the property (Cathey, 1982:15).

It is better known as the "legal title" to the real estate environment. In terms of the Alienation of Land Act, 1981 the purchase price is paid to the seller by way of more than two instalments over a period of longer than one year. The Act also states by definition of *Instalment Sale Agreement*, that it is mainly intended for and focused on residential property transactions.

According to Lockyear (2008:1) "Since the buyer has the rights set forth in the agreement and is making payments toward the purchase of the real estate, the buyer holds "equitable title" to the real estate. The term "equitable" is meant to impart what is just and right. It therefore implies in this situation that the buyer does have vested interest in the real estate that amounts to or is dependent upon how fiscal value the purchaser has contributed towards the purchase of the property"

In the event of the seller filing for insolvency, the purchaser could take transfer of the property by settling the balance of the purchase price, or by passing a mortgage in favour of the seller's estate on under the same terms and conditions as stipulated in the *Instalment Sale Agreement*. The same would apply should the seller pass away.

In practice, the instalments are paid by the purchaser to the credit of the sellers bond account. To guaranty that the balance under the bond do not exceed the balance of purchase price, the seller’s bond account is “frozen” and as a result the seller cannot pass any further bond over the property, nor can the seller apply for any re-advance.

It is believed that *Instalment Sale Agreements* tend to provide more benefits to the seller than the purchaser. This perception is based on the fact that seller still holds title to the deed and is therefore able to use the real estate as collateral unless otherwise prohibited by the agreement. Even more importantly, if the purchaser defaults on his payments, the seller may have the option to declare the buyer’s rights forfeited and will effectively imply that the buyer no longer has an interest in the real estate and that the seller will retain the purchaser’s previous payments as liquidated damages (Lockyear, 2008:1).

However, forfeiture is not favoured by law. While there are no statutory laws outlining the rights of an instalment purchaser to its equitable title, the courts over the years have issued rulings designed to protect the purchaser’s equitable interests. In a 1973 lawsuit, where an instalment purchaser had paid well over one-half (1/2) of the purchase price under the *Instalment Sale Agreement*, the Indiana Supreme Court ruled that forfeiture was excessive and that foreclosure was a more appropriate remedy. Accordingly, the ability to forfeit a purchaser’s equitable interest is limited to what the legal system views as fair and just, generally where little money has been paid toward the purchase (Lockyear ; 2008).

2.6.1 History on instalment sales used for property transactions

Instalment Sale Agreements (previously known as suspensive sale agreements) became very popular within the South African property industry in the late 1970’s early 1980’s when mortgage finance from the then Building Society movement was very hard to come by. Building Societies at the time generally only granted loans to potential purchasers if the seller was prepared and in the position to make, what was euphemistically labelled a matching investment, with the building society for a generally accepted period of five years. Sellers were not prepared to lock away their sale proceeds in generally low performing building society investments, and as a result they resorted to the so called suspensive sale route *Instalment Sale Agreement)*. There was no legislation in position to protect purchasers who entered into these agreements at the time prompting the occurrence of countless abuses. To counter these abuses, government introduced the Alienation of Land Act, better known by its acronym ALA.

ALA, which applied to most sale transactions of land, introduced two profound additions to the traditional South African laws relating to the sale of land.

- No individual was allowed to take money up front for the sale of immovable property unless the property was registerable. This had a profound effect on township property as well as sectional title developments. A partial exemption was granted which implied that a seller could take money up front on unregisterable property, provided that a bank or insurance company issued the purchaser with a back to back guarantee for a refund in the event of loss caused by the seller's failure to affect the transfer of the land being sold.

- It regulated the so called suspensive sales (*Instalment Sale Agreement*) which is now termed as a sale of land by instalments would qualify under the Act. A sale of land by instalments was defined as a sale of urban immovable property where the purchase price is paid in more than two instalments over a period of more than twelve months (i.e.12 months and 1 day would qualify).

Alienation of Land Act further provides the following with regards to instalment sales:

- The purchaser can take transfer of the land after one year of the date of sale or at any given time during the course of the term of the existing bond (in the name of seller). It is general practice to allow the purchaser five years to take transfer, but the period is flexible and can be negotiated.

- The purchaser could protect his vested interests by recording the contract against the title deed to the property within 90 days of sale.

- Any registered mortgage bond holder over the property must be informed and advised of the existence of an *Instalment Sale Agreement* in writing and had to be furnished with the Purchaser's contact details.

- The purchaser had to be advised of transfer duty costs payable within six months from date of agreement to avoid incurring penalties. This of course (current, i.e. 2012) does not apply to property that was sold for less than R 600 000.

- The Seller is to supply the Purchaser once every twelve months with a detailed breakdown confirming:

  - Balance of Purchase Price outstanding.

  - Balance outstanding under the existing bond.

- The purchaser is to be given thirty day notice of any defaults caused and affected by the purchaser. Should the purchaser be given two of these recurring notices in any twelve calendar month period, the purchaser could be given a seven day notice on the third occasion that he/she is in breach of contract within this period and that the agreement is terminated.

- The agreement could be cancelled in the event of a purchaser's default but, in terms of the Conventional Penalties Act, the seller might be required to refund the purchaser portion of his payments made if it totals more than the seller's actual damages. Furthermore, the purchaser would face eviction on cancellation, subject to his rights under impacting laws.

2.6.2 Frequently asked questions on the Alienation of Land Act 1981

The Alienation of Land Act was introduced to affect improved regulating of transfers of properties. The following frequently asked questions need to be answered in order to better understand the Act and the role it plays in instalment sales of properties.

2.6.2.1 Why would the seller want to sell his property by means of a Sale of Land on Instalments?

- The seller might be in a position where he can no longer afford his bond repayment, land levy and/or rates & taxes, endangering his credit record, but is unable to sell the property for the outstanding balance on his bond plus commission.

- The outstanding balance on the seller's bond might exceed the present realisable market value, but the seller wishes to sell the property – e.g. to buy another property and does not expect to receive any Nett proceeds.

- The seller had paid off part of his mortgage and wishes to maximise and grow his investment through the interest being charged on his equity in the property, whilst benefitting from the security provided by the ALA and the fact that the purchaser shall be responsible for all expenditure in respect of the property, e.g. levy/rates & taxes, maintenance, insurance.

- Property developers may choose to sell part of their developments.

- Sell the property on the *Instalment Sale Agreement* basis as medium/long term investment. Thus earning interest on their capital investment.

- The developer may contractually escalate the purchase price (e.g. a 5% escalation per year), thereby earning interest and capital growth. This escalation clause needs to be clearly stipulated in the agreement and agreed upon by the parties (Van Staden, 2012:3).

- Selling the property by means of *Instalment Sale Agreement* the developer utilises it as a mechanism to service part of the development bond, during development of further phases.

2.6.2.2 Why the purchaser would want to buy a property by means of an ALA contract?

- No deposit is required unless parties agree that a deposit needs to be paid (Smith, 2013:2).

- The purchaser might not be in a position to qualify for the mortgage loan, due to e.g. the banks' deposit requirements or does not have the registration costs and fees available, but has the resources/income to cover the full bond repayment. The purchaser would then be afforded time to save enough to put together the deposit and other costs, whilst having the benefit of occupation and possession of the property.

- Newly registered or inactive trusts and companies generally do not qualify for bond finance due to a lack of credit history and cash-flow. The purchaser, in an ALA transaction, does not apply for bond finance and is afforded the opportunity, through the ALA structure, to "activate" the trust or company, build up equity, a credit history and show cash-flow.

- Investors could apply available resources towards provision for "shortfalls" rather than deposits.

2.6.2.3 Is there a time frame involved for the purchaser to obtain finance to settle the outstanding bond?

Only if:

- The term of the ALA contract (e.g. five years) and amount of the instalments result in a "balloon payment" at the end of the contract term. In this event the purchaser must be able to obtain finance prior to expiry of the contract term (Smith, 2013:2).

- The purchaser wishes to take transfer during the term of the ALA contract (e.g. five years into the fifteen year term). In terms of the ALA the purchaser is required to make payments before the due date(s) and to make larger payments than what is required by the contract.

2.6.2.4 Does the purchaser have to obtain finance from a financial institution?

- No, in the event that the term of the contract is the same as the remaining term of the seller's bond (e.g. fifteen years), the purchaser may simply pay the instalments until the purchase price is fully paid by the end of the term.

- In the event that the term of the contract (e.g. five years) is shorter than the remaining term of the seller's bond (e.g. fifteen years), refer to 2.5.2.3 above.

2.6.2.5 When is transfer duty payable?

- Transfer duty must is due within six months of date of signature of the contract, thereafter the purchaser will be liable for a 10% penalty charge per month, calculated on the amount transfer duty payable (Da Costa, 2010:1).

2.6.2.6 What happens to funds paid towards transfer duty if the sale does not proceed?

- All monies paid towards transfer duty will be refunded to the purchaser by the South African Revenue Service (SARS).

2.6.2.7 What is the responsibility of the Attorney appointed in the contract?

The Attorney:

- Will draft the contract and ensure that it is a legally just and binding.

- Will notify the seller's bank of the transaction, provide the bank with the information required by the Act and request the original Deed of Transfer.

- Will draft the application to record the contract against the title deed, tend to the signature thereof and lodge the application in the Deeds office for registration.

- Will receive in trust and disburse the deposit, if any, in terms of the provisions of the contract.

2.6.2.8 Will the Purchaser obtain a Title Deed in respect of the property?

- The purchaser will only receive a title deed upon full payment of the agreed purchase price and after the property had been transferred to the purchaser (Griffon, 2012:2).

2.6.2.9 Who is responsible to settle any arrears on the existing bond, should there be an arrear amount?

- The seller will remain liable for any arrears, however and by means of a mutual contractual agreement, the purchaser may pay a deposit to settle the arrears.

2.6.2.10 In which account does the purchaser make payments towards the property?

- As long as the property is still subject to a mortgage bond, all instalments must be paid directly into the bond account (Smith, 2013:2).

- If the property is not subject to a bond, all instalments must be made payable to the seller's designated account.

- Rates & taxes and/or levies must be paid directly to the Local Authority and the managing agents, whichever is applicable (Griffon, 2012:2).

- Legal costs & fees must be paid directly to the attorneys.

- Transfer duty and costs should be paid by the purchaser to SARS within six months of the date of conclusion sale agreement. In the event of failing to comply, the transfer duty will attract penalties (Da Costa, 2010:1).

2.6.2.11 Can the purchaser resell the property if the purchase price has not yet been settled in full or transfer affected?

- Yes, the purchaser may sell the property, subject to the rights of the seller.

2.7 Instalment sale versus Mortgage bond

What is the difference between a conventional sale agreement and an *Instalment Sale Agreement*?

In terms of a conventional sale of a property the property is sold on a cash and/or bond basis and once the mortgage loan has been secured, registration of transfer takes place whereby the purchaser becomes the registered owner. The seller will receive the nett proceeds generated as a result of the sale from the conveyancer on registration of transfer of the said property (Hunter, 2008:1).

The Alienation of Land Act regulates agreements of sale of land on instalments. (Sections 4-25) and the Act prescribes and sets out the information that must be contained in an agreement of this nature. For example, the annual rate at which interest is payable and the amount of each instalment must be set out in the agreement (Hunter, 2008:1).

In essence, with an *Instalment Sale Agreement*:

- The purchase price will be payable to the seller over a period of time (longer than one year) and in two or more instalments (Forrest, 2011:1).
- The purchaser will usually be required to pay a deposit which should be sufficient to cover at least the legal and estate agent's commission (Griffon, 2012:2).
- The instalments will usually be agreed on an amount sufficient to at least cover the seller's bond repayments (Hunter, 2008:1).
- Agreements are registered against the title deeds at the Deeds Office by means of a recordal which must be registered within 90 days of signature of the agreement. This implies that the seller would not be able to take out any further bonds on the property, nor sell the property without the buyer's consent (Hunter, 2008:1).

- The *Instalment Sale Agreement* must be registered against the title deeds of the property before any payments are made to the seller.
- Transfer duty and costs are payable, by the purchaser, to SARS within a period of six months from the date of concluded sale agreement in order to avoid penalties (Smith, 2013:1).
- Should the purchaser default with any monthly payments, all payments made by him, will be forfeited as damages and the property will revert to the seller.
- If the seller goes insolvent, the purchaser will have a preferent claim in respect of the proceeds of the sale of the property (Hunter, 2008:1)

2.8 Conclusion

Government and private initiatives like the Social Housing, Reconstruction and development program (RDP), Finance Linked Individual Subsidy Program (FLISP) and other Government subsidies are in place and were incorporated in the South African Housing strategy. However, there is still a massive backlog in the housing and especially affordable housing market of South Africa. In addition to the backlog, the recent global financial crisis has forced credit providers to be a lot more mindful, careful and stricter with their lending strategies. Thus we find that there are numerous prospective property investors and homeowners in South Africa that earn more than the maximum allowable income required to qualify for the above mentioned subsidy programs, but at the same time earn less than required to qualify for a mortgage bond from a financial institution to afford them the privilege purchase a house.

Instalment Sale Agreement offer an alternative opportunity to the prospective home owner that doesn’t qualify for a conventional home loan, to legally obtain financing on an installment basis. This option will service a different and somewhat neglected sector of the income group in South Africa, and can serve as a viable and sound alternative financing method to aid to counter the current backlog in housing in South Africa.

3. CHAPTER 3 – METHODOLOGY STATEMENT

3.1 Introduction

This research was undertaken in response to the Research Questions indicated in Chapter 1. The main aim of the research was to determine whether an *Instalment Sale Agreement* would be a viable alternative to both the purchaser, as well as the credit provider of residential properties ranged above the stipulated government subsidy programmes but simultaneously beneath the R500 000 mark in the Gauteng province of South Africa. The said research was also conducted to establish whether *Instalment Sale Agreement* could be considered as a viable alternative option of financing to accommodate additional potential buyers supporting them in their efforts to acquire residential property as well as to determine whether it could aid in countering the current backlog and shortage in South African housing market, especially in the range where individuals does not qualify for any government subsidies.

This research will aim to answer these main challenges from two angles. Firstly whether developers will find it feasible to develop and sell these properties on the basis of *Instalment Sale Agreement* and secondly study whether prospective clients will be willing to purchase residential property on the *Instalment Sale Agreement* model and accept the limitations attached as a feasible alternative as opposed to the conventional methods of purchasing a property in the event of not qualifying for adequate home loans or government subsidies.

The research was undertaken in two sections. The first section of the research was conducted as a literature review that involved research on academic and other published sources which focused on the property industry as well as housing and/or finance methods of housing. This section was covered in Chapter2.

The second section is the empirical research that was based on structured interviews and survey questionnaires.

In addition, the empirical research was also further based on a case study that was conducted and founded on an actual residential property development project from a reputable large scale property developer considered to be influential in the market. The properties of the above mentioned development project are sold on the *Instalment Sale Agreement* basis.

The questionnaires and interviews were conducted from the vantage point of two approaches. The first angle was observed and formulated with the aid and input from professionals involved as credit providers and property developers whilst the second was approached from the prospective homebuyers angle who might consider the *Instalment Sale Agreement* method of financing option.

The following paragraphs describe the process undertaken and methodology utilised.

3.2 Structured Interviews and questionnaires

Interviews and questionnaires were based on the typical qualitative methods of research frequently used in research studies. Qualitative methods included a wide spectrum of techniques utilised to collect data based on various interactions between researchers and respondents. These respondents are, as usual, considered to be experts in the relevant field of study based on either an academic realm or their valuable practical experience in the field.

3.2.1 Interviews with stakeholders from property developers and credit providers

Structured interviews were conducted with a number of property developers currently active in the property profession. The sample chosen was based on developers and financial credit providers with a residential background. Adequate residential background was a key factor and non-negotiable due to the study's focus on housing and in particular the *Instalment Sale Agreement* as an alternative method of financing and purchasing residential properties.

The initial structured interviews were conducted during November 2012 and subsequently were continued in September and October 2013 with an additional round of interviews that were conducted. Interviews were conducted in person as well as telephonically with the general response received perceived as contributing, meaningful, sound and of quality input.

The answers and comments from the respondents were recorded in writing during the interview process and were categorised, summarised and combined with the questionnaire answers received. Various similarities in the form of repetitions of responses were received and as a result indicated general consensus and consistency amongst the credit providers and developers.

The respondent interview and questionnaire were conducted simultaneously due to time constraints as indicated by the respondent's point of view. Each interview was unique but the interviews were structured on the basis of the following interview and questionnaire questions:

Questions to Credit providers and Developers:

- Why do you believe housing is important?
- Why do potential home buyers struggle to qualify for financing and home loans in recent years?
- What alternative methods do exist when a person does not qualify for a home loan?
- What is your opinion on instalment sales funding option with regards to residential property?
- What benefits does Instalment sales funding offer the developer?
- What benefits does Instalment sales funding offer the credit provider?
- What benefits do you believe the Instalment sales funding method could offer a home buyer?
- How do you get in contact with possible home buyers that don't qualify for a conventional home loan?
- Do you believe that *Instalment Sale Agreement* can be successfully employed in the South African low cost residential property market?
- Are you generally for or against the *Instalment Sale Agreement* as a method of financing residential property?

3.2.2 Questionnaires

A standard questionnaire was compiled for completion by participating respondents. The questionnaires was distributed to credit providers and developers as well as possible potential home buyers who were interested in, were contemplating or seeking to purchase homes beneath the R400 000 benchmark but didn’t qualify for any Government subsidy programmes.

A standard copy of the questionnaire is attached under Annexure A and Annexure B.

The questions asked in the questionnaires were compiled in different formats. The main objective was to keep it as brief as possible, but at the same time it had to extract thorough and valuable information.

The questions range from short questions with uncomplicated answers to longer open ended questions in order to stimulate both gut feeling opinions and additional opinions. A number of answers and opinions evolved from the questionnaires and a summary of the responses is discussed in chapter 4.

3.2.2.1 Questionnaires to proposed homebuyers

Eleven questions were posed to some 46 proposed and potential purchasers by means of an internet survey. The questionnaires evolved with additional data and information.

Questionnaires to homebuyers who might consider the instalment sale method of financing:

- In what age category are you?
- Do you currently own a residential property?

- Have you previously applied for a home loan?
- If your application for a home loan was not successful, please indicate the reason/s.
- What is the possibility that you would apply for a home loan within the next few years?
- If you currently had to apply for a home loan, within what range would you be able to apply for financing?
- Have you previously been introduced to alternative financing methods to purchase a residential property?

The respondents were educated regarding the *Instalment Sale Agreement* concept at this stage. The following questions then focussed on the essence of the concept:

- Would you consider *Instalment Sale Agreement* (method which is commonly used for motor vehicle finance) as a financing option to purchase a residential property if you do not qualify for a conventional home loan?
- Do you think that *Instalment Sale Agreements*, as a property financing method, can be successfully utilize in the South African residential property market?
- The government low cost housing waiting list currently has a huge backlog. In your option, would the *Instalment Sale Agreement* decrease the backlog by drawing people to buy and finance their properties?

Some questions were compiled as open ended in order to stimulate additional opinions. A number of opinions evolved from the structured interviews and a summary of the responses is discussed in chapter 4.

3.3 Case Study

A case study was conducted. It consisted of an actual residential property development project from a large and influential property developer based within Gauteng. The houses in this development project are sold on an instalment sale basis.

The case study was conducted and the conclusions were analysed and the outcomes and results of it discussed in chapter 4.

3.4 Validity and reliability

The empirical research conducted included interviews, questionnaires as well as a case study on an actual property development project. This was done to establish and add to the reliability and validity of the study.

3.5 Conclusion

The research methodology employed aimed to provide a solution to the research problems posed in chapter 1 and chapter 2: Whether an Instalment Sale Agreement would be a viable alternative to both the purchaser, as well as the credit provider of residential properties ranged above the stipulated government subsidy programmes but simultaneously beneath the R500 000 mark in the Gauteng province of South Africa. Data was collected through literature reviews as well as empirical research, which included interviews, questionnaires.

The Literature review was used and for this purpose academic published articles, models and information as well as published data from commercial institutions was procured to test the proposed model based on provincial, national and international literature research.

4. CHAPTER 4 – RESEARCH FINDING AND DATA DISCUSSION

4.1 Introduction

This chapter presents data that was collected from structured interviews, questionnaires and a case study. The questionnaires and interviews were conducted in order to determine whether an Instalment Sale Agreement would be a viable alternative to both the purchaser, as well as the credit provider of residential properties ranged above the stipulated government subsidy programmes but simultaneously beneath the R500 000 mark in the Gauteng province of South Africa.

The questionnaires and interviews were conducted from two angles. Professionals from registered credit providers as well as property developers were interviewed and questioned on relevant issues by means of carefully formulated questions in order to determine their confidence in the *Instalment Sale Agreement* funding option. Questionnaires were also conducted with prospective homebuyers who considered the *Instalment Sale Agreement* method of financing at the time. The case study conducted was based on an actual residential property development project developed by large and influential property developer based within Gauteng province. The houses in this development project are sold on an instalment sale basis.

4.2 Developers and Credit providers

The property developers that were involved in the study have all been involved in the residential property development industry for a minimum period of ten years. These developers specialise in focusing on developing property for the residential market that is tailor made to supply the niche demand in the market. The development and supply of quality yet affordable housing is their speciality.

The participating stakeholders in the respective property development companies interviewed are without exception well respected in their profession. However, only one property development company that was interviewed has used the *Instalment Sale Agreement* method for financing residential properties prior to this study.

4.2.1 Feedback on questionnaires

4.2.1.1 Housing

- **The importance of housing and the important role housing plays in South African economy.**

Home ownership is one of few opportunities available to South Africans to generate capital and by doing so ensuring a more prosperous future and lifetime wealth for themselves, their families, communities and ultimately the country.

- **Housing in South Africa**

There is currently, and has been for an extended period of time, a backlog of housing in South Africa. The government has put strategies in place to counter for this backlog by providing more houses to those who do not have the privilege of owning a house.

The strategies that the government has in place include subsidy programmes such as FLISP and RDP.

Although these programmes are in place, there is an ever escalating ‘Gap’ market present in the residential property market. This phenomenon constitutes a substantial portion of the population. These prospective home owners are unfortunate not to have means of adequate financial resources to their disposal nor do they qualify for any Government subsidy programs and to make matters even worse they do not qualify for a mortgage bond to acquire a residential property.

Affordable housing at the very low portion of the market, for example RDP subsidy program in South Africa, faces another daunting challenge of maintenance to the property. It is considered near impossible for the individual at this end of the market, who received a house by means of the RDP system because he/she cannot afford a property, to afford to maintain the house?

Thus it is deducted that housing in South Africa, as for most countries in the world, goes hand on hand with national employment. The more people the country can afford to employ, the more people will afford houses and also afford to maintain their houses.

4.2.1.2 Conventional housing finance

- **The struggle to qualify for financing and mortgage bonds**

The average individual has too much personal debt. The credit providers are partially to blame due to the lending criteria that were not strict enough. The lending criteria of earlier years made it too easy for individuals to qualify for mortgage bonds and at the same for other credit while in reality they shouldn’t have been allowed to qualify for the credit margins acquired or should it be said accumulated.

By contrast, short term and long term interest rates are reasonably positioned

despite low lender confidence. The Reserve Bank of South Africa is somewhat held at ransom, in order to stimulate economic growth through investment but at the same time attempting to curve the high rate of irresponsible borrowing and lending practices. This has already in turn affected the affordability of Mortgage bonds as a result of the unsecured lending market.

- **Credit providers area of focus**

Credit providers tend to focus on the following aspects when evaluating applicants:

- Affordability
- Credit record
- Stability in employment
- Income-expenses ratio

- **Main reason for default on home loan applications**

The main reasons for default on applicants home loan applications include; recent unemployment, high personal debt, high level of leverage, bad credit rating and applicants not being honest on their application forms.

4.2.1.3 Alternative financing options

- **Current alternative financing methods**

Should the individual have a substantial amount of money available to put down for deposit it is advisable to do so. This will in turn enhance lender confidence and will provide the individual with a better prospect to qualify and secure the desired mortgage bond. It could also put the individual in a position to qualify for a reduced interest rate.

From an alternative financing method point of view, the only real feasible alternative as deducted from this study is considered to be the *Instalment Sale Agreement*. This option has the potential to be used more regularly especially in troublesome financial periods when lender confidence is down and the criteria for lending are rather strict.

- **The benefits of Instalment sales funding for the developer**

The developer will be in the fortunate position of having access to an additional option or sales mechanism to sell residential properties. Should this method be considered viable and sales strategies adapt accordingly, sales could once again be revived to reach acceptable levels and allow for more people to be in the position to purchase a house. This in turn will raise the demand for residential property which will stimulate the construction industry and development as a whole .It will lead to improved income and profit margins being realized and as a direct result of more units required. Developers would then be in a position focus more on job creation, work satisfaction and continuation. Let’s not forget that the housing industry service, and support and influence a large section of the South African economy. Therefore it can be deducted that growth, be it however small, will translate through the entire economy thus leading and playing its part in the stability of South Africa.

- **Benefits of Instalment sales for the credit provider**

High income margins as a result of more interest being generated over a period of time as more units are being sold, will be one of the main attractions for credit providers. They can use this to settle funding debt.

- **Benefits of Instalment sales for the buyer**

The instalment sales funding offers the following to buyers:

- It offers an extra purchasing option for the home buyer.
- Same benefits as the normal mortgage bond.
- Full rights and obligations over the property.
- Purchasers may sell their house at any time and possibly make a profit after debt is settled.

- **Possible short comings with regards to the instalment sale funding option**

It is a relatively unknown product in the South African housing context. Although it has been used in the past, it has not yet settled in the South African Housing market and thus individuals do not really have knowledge about the option. Product education would be vital as many individuals stand oblivious of the existence of the option. Should they therefore suddenly learn of the possibilities it posses, they wouldn’t necessarily trust the financing model immediately. Also take into consideration that not all credit providers are willing to take the *Instalment Sale Agreement* route.

- **Awareness of Instalment Sale Agreement option**

How to make more people aware of the *Instalment Sale Agreement* option?

Industry would need to focus on hands on marketing such as flyer distribution, bill board advertisements, radio and TV etc. But also very important you need to educate the individuals who are willing to consider the *Instalment Sale Agreement* as an option to purchase a residential property in order to familiarise them with the option and truly trust it.

- **Do you believe that instalment sales can be successfully employed in the South African low cost residential property market and help counter the backlog in home ownership in the country?**

Without a doubt yes, but it will take time to get all role-players in on it.

- **Would developers be willing to utilize the Instalment sale funding method especially for proposed home buyers under the R500 000 mark?**

Depending on the state of the market and how it positions itself regarding the type (price-range) of product coupled with the supply and demand ratio in the housing industry at any giving time. Developers might be very keen to make use this option because if it makes funding easier and it will create an extra option for developers to develop and sell more units.

4.2.2 Feedback from structured interviews

In an interview conducted with Anton Crouse, MD and founder of Cosmopolitan Projects Property Group on 15 November 2012, Crouse pointed out the importance of housing and the importance for all South Africans to own a house. The sad part is that once a prospective client's application for a home loan was unsuccessful and/or turned down as a result of/or due to some default by the applicant according to the financial credit provider's criteria, it is highly unlikely that such a person will ever re-apply for a home loan again, thus he or she will invest their money in other asset groups or most likely spend their money and never own a house and reap the benefits that comes with owning a house.

Thus an alternative option, such as an *Instalment Sale Agreement* option, could be an excellent alternative in order to accommodate marginal clients that should be able to get funding had the banks been interested and willing to marginally increase their appetite/scorecards for potential business and taken into account the client's sound financial track record over a period of time.

In a conversation on 25 January 2013, Suzanne Coetzee, financial director at a large residential property development company, mentioned that traditionally the prospective home owner didn't have a variety of options available to them when they wanted to purchase a house. They either had to have had enough money saved up in order to purchase the property in cash or they could apply at a registered and accredited bank or financial institution for mortgage funding.

Coetzee added that an unfamiliar yet exciting additional alternative option is becoming more popular for the prospective home owner to exploit. This entails that an approved credit provider may be able to lend you money to purchase a residential property by means of an *Instalment Sale Agreement* Contract. Through this option the credit provider will source and identify suitable clients in terms of their credit policy and offer an instalment sale option to them. Once the client has indicated and declared intent and desire to purchase a particular property by means of the *Instalment Sale Agreement* option (funding option), the credit provider will initiate and proceed with a formal credit process.

The principals of an *Instalment Sale Agreement* contract for a residential property are similar to that of the principals of purchasing and securing motor vehicle-, furniture finance, etc. Ownership of the title deed of the particular asset only transfers from the credit provider (in this case the owner of the property) to the purchaser once the loan granted has been settled and covered in full. The buyer/purchaser has the same benefits and responsibilities as with mortgage bond finance.

The following table illustrates the differences and similarities of homeownership through an Instalment Sales contract versus a traditional Mortgage Bond:

Table 3: Basic comparison between instalment sale and mortgage bond funding

INSTALMENT SALE FUNDING	**MORTGAGE BOND FUNDING**

INSTALMENT SALE FUNDING	**MORTGAGE BOND FUNDING**
The title deed will remain in the name of the credit provider until such time that the purchaser has redeemed his/her debt in full.	The title deed will be transferred to the purchaser.
The client's interest (ownership) will be endorsed on the title deed of the property. **Therefore on the title deed it will state that the purchaser bought the property and is repaying a financial loan granted by the credit provider. The purchaser will therefore eventually become the rightful owner of the property, provided agreement and terms of the loan are adhered to and the commitment to the credit provider is honoured.**	A mortgage bond in favour of the bank will be registered on the property. It will therefore state on the title deed that a particular financial institution has provided funding for the purchase of the house. The Bank will hold the original title deed, with the bond as security until the mortgage bond has been covered or repaid in full or legally cancelled.
Transfer of the title deed to the purchasers name will only be affected once the loan has been covered/repaid in full.	Cancellation of the mortgage bond will take place once the loan has been covered/repaid in full.
Full rights and responsibilities of ownership.	Full rights and responsibilities of ownership.
If the purchaser cannot meet the commitment as a result of the ISC they can cancel the credit agreement and voluntary vacate and surrender the property. No legal action will be instituted for breach of contract.	No option to cancel the credit agreement without full settlement of the outstanding amount.
Foreclosure with legal process	Foreclosure with legal process ensuing on

INSTALMENT SALE FUNDING	MORTGAGE BOND FUNDING
ensuing on instalment default or contract breach.	instalment default or contract breach.
Original purchaser can sell the property, settle the outstanding loan with CFS and make a possible profit during the contract period.	Owner can sell the property, settle the outstanding mortgage bond with the bank and make a possible profit during the contract period.
In the event of the purchaser passing away, their life insurance could settle the outstanding loan with the credit provider and the deed on the property is transferred to a legal inheritant.	In the event of the purchaser passing away, their life insurance could settle the outstanding mortgage bond with the credit provider and the deed on the property will be transferred to a legal inheritant.

(Source: Cosmopolitan Financial Services (Pty) Ltd.)

4.3 Prospective buyers

4.3.1 Feedback on survey and questionnaires

A total of 31 questionnaires and surveys (combined) were completed and received back from the original 60 sent out. Feedback on the survey and questionnaires are disclosed and have been summarised under sub-categories for the convenience of the reader.

4.3.1.1 General questions

- **Age categories**

The questionnaire was sent to respondents of various age groups. Figure 5 identifies the age categories of the respondents to the survey.

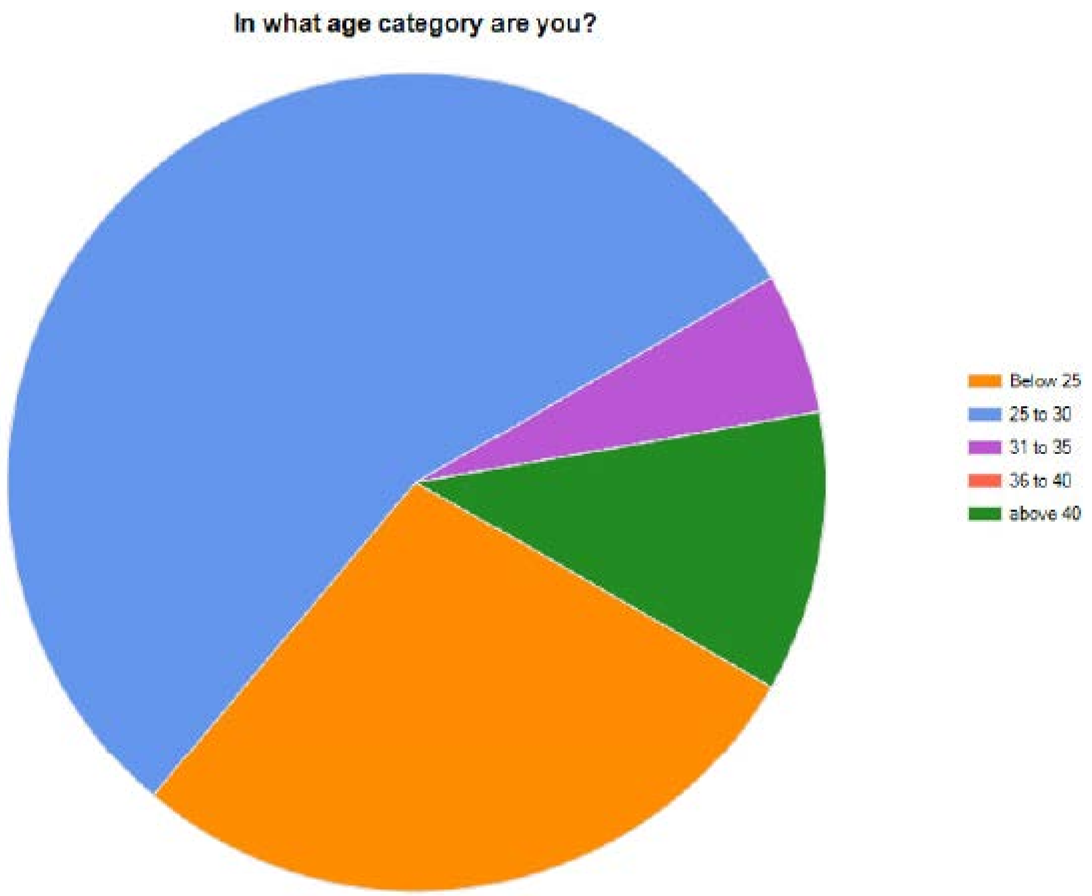

Figure 5: Age categories of the respondents

(Source: Survey monkey. Instalment sale agreement survey 2013)

Figure 5 indicates that most of respondents are younger than 30 with the majority of the proposed buyers being between 25 and 30.

Figure 5 indicates that 27.8% respondents are under the age of 25 years and 55.6% are between 25 and 30 years old. 5.6% are between 31 and 35 years old, and no respondents were between the ages 36 and 40, but a further 11.1% were 40 years and older.

- **Reasons for previous unsuccessful application attempts**

The questionnaire attempted to establish whether respondents have had an unsuccessful property finance application. To those that replied that they have had an application turned down, the reasons that contributed to this were requested.

It became apparent that applicants do not necessarily always know why there application for a mortgage bond has not been approved. Provided are some of the main reasons by the participation respondents (as mentioned under section 4.1.1.2):

- Recent loss of job
- High personal debt
- High level leverage
- Bad credit record
- Affordability

- **Importance of housing and the important role housing plays in South African economy**

From the respondents that completed the questionnaire it became apparent that many of them are not quite aware of the macro economic importance of housing in

South Africa. They understood that it provides security and comfort for them and their families, but stand oblivious or doubtful to the notion that the majority of the low income population truly understand what the major impact it might have on their and the country’s long term wealth creation and financial stability.

4.3.1.2 Conventional home loans and alternative funding options

- **Aspects that credit providers focus on when evaluating a prospective home buyer's application for a home loan**

The average respondent was to some extent aware of the contributing factors and aspects that the credit providers focus on when evaluating a home loan application. Individuals clearly understand that their credit record and income-expense ratio plays a big part, but one gets the impression that other criteria such as employment history and affordability are not fully grasped by the average individual applying for a mortgage bond.

- **Introduction to alternative funding methods to purchase residential property?**

Alternative funding methods are not introduced or promoted to individuals adequately and frequently enough. As Figure 6 will indicate, 90% of respondents have not been introduced to alternative financing methods.

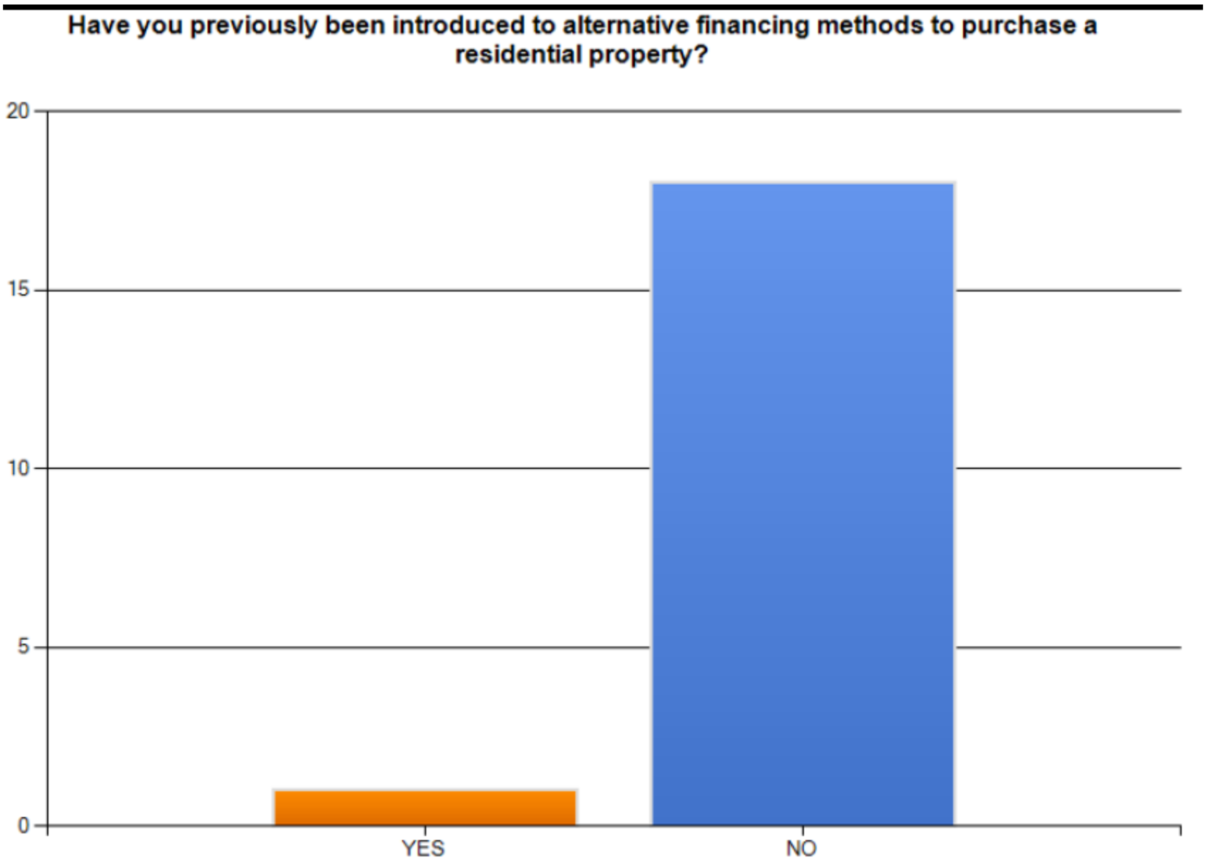

Figure 6: Promotion of alternative financing methods

(Source: Survey monkey. Instalment sale agreement survey 2013)

Each individual at this point of the questionnaire is educated on the Instalment Sale Agreement.

- **Opinion on instalment sales funding option as a financing option to purchase a house**

As soon as individuals were enlightened on the subject matter, real interest were displayed with regards to the *Instalment Sale Agreement* financing option. Respondents seem to regard housing as very important and are willing to investigate the *Instalment Sale Agreement* option readily further with the survey deducting that the majority of respondents will be willing to settle for the option of *Instalment Sale Agreement* if it means that they are able to afford a house.

- **Attractive benefits that the *Instalment Sale Agreement* method offers**

The following benefits seem to be the most attractive to the prospective home buyers:

- Affordability
- Legal aspects
- Possibility to change over to a conventional bond in time as their credit rating improves.

- **Possible short comings with regards to the *Instalment Sale Agreement* option**

It is clear that the conventional home loan is preferred over an *Instalment Sale Agreement*. The main reason might be due the fact that *Instalment Sale Agreement* is still regarded as unfamiliar territory for the majority of prospective home buyers.

- **Would you be willing to purchase a house on an *Instalment Sales Funding* method?**

If it means that a person can afford to own his or her very own house it will be a method that will be welcomed by most of those individuals who would not necessarily have qualified for a conventional home loan.

Figure 7 reflects the findings and indicates that very few people will not consider it at least as an option of financing.

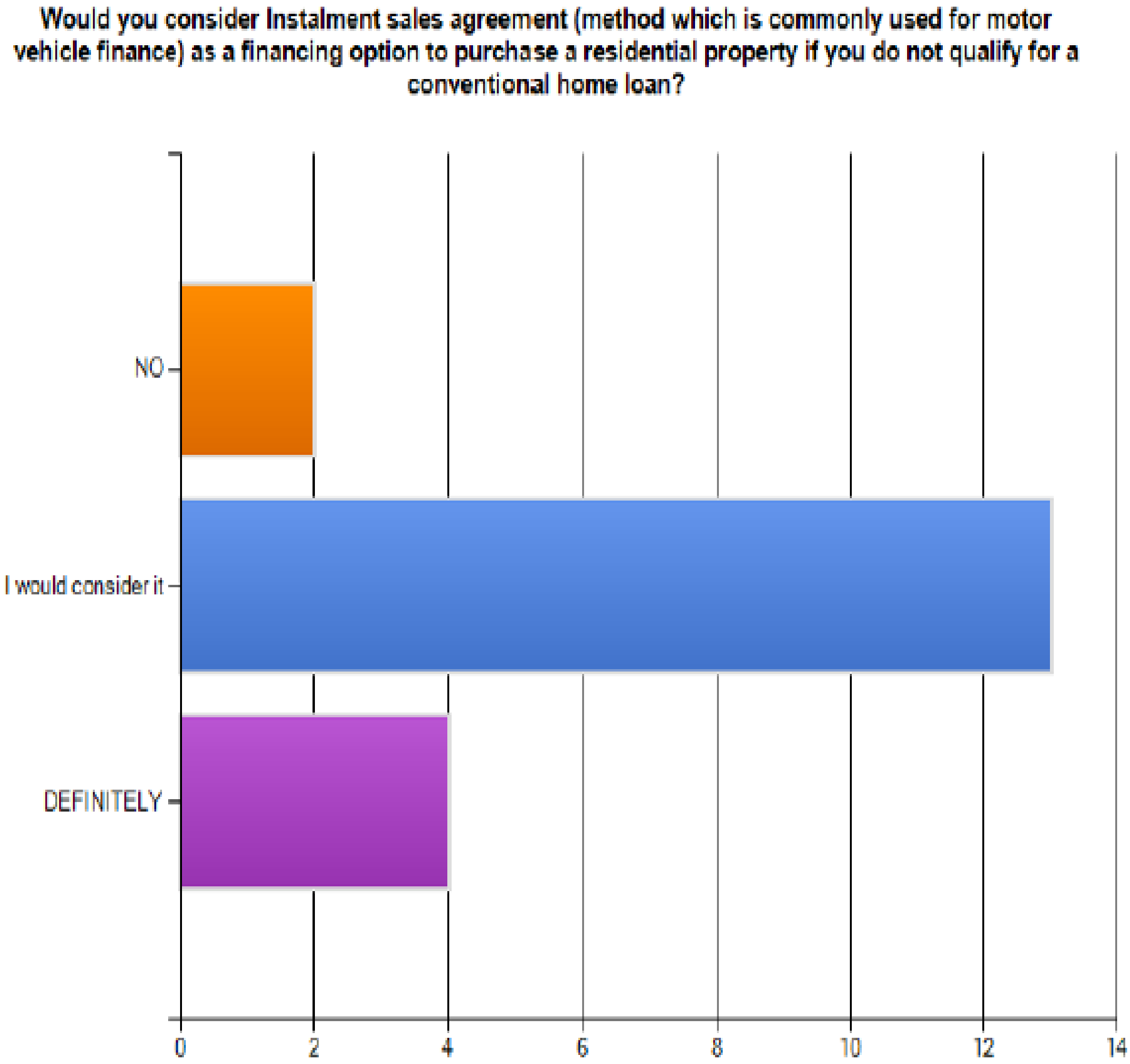

Figure 7: Interest shown in alternative financing options

(Source: Survey monkey. Instalment sale agreement survey 2013)

Figure 7 shows that 70% of the respondents would consider in alternative funding method and a further 20% would definitely apply through alternative funding methods if it provides the buyer with a possible opportunity to successfully qualify to purchase a property where they would under normal circumstances be rejected when applying for a mortgage bond.

- **Do you believe that *Instalment Sale Agreement* can be successfully implemented in the South African low cost residential property market and help counter the backlog in home ownership in the country?**

Once again, it is seen that the average individual out there are not quite aware of the macro economic importance of housing in South Africa. They understand that it provides security and comfort for them and their families, but it is doubtful whether that the majority of the low income population truly understand what the major impact it might have on their and the country's long term wealth creation and financial stability.

Figure 8 suggests that the proposed homebuyers do feel that *Instalment Sale Agreement* will make it easier to qualify for housing finance and therefore it will benefit the industry and can be successfully implemented in the market.

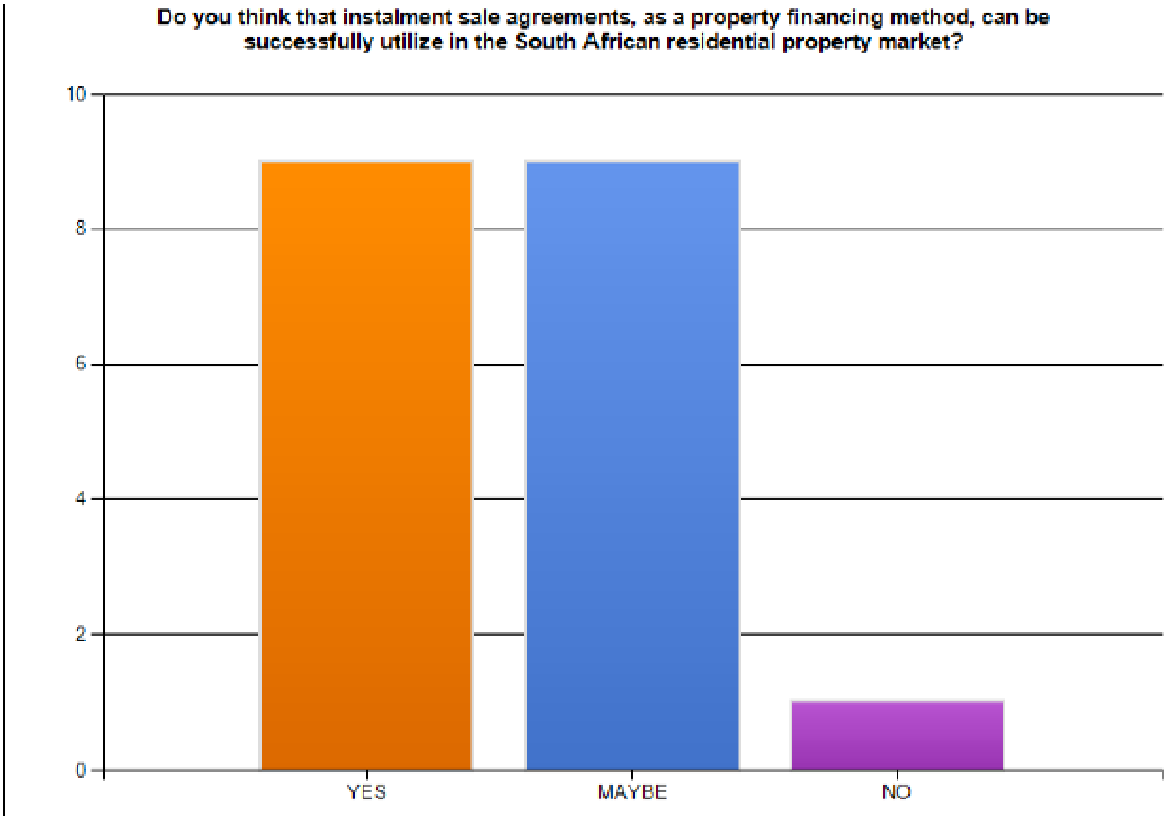

Figure 8: Instalment sale agreement option utilized in the property market

(Source: Survey monkey. Instalment sale agreement survey 2013)

Figure 8 indicates that only 5% of the respondents do not believe that instalment sale agreements can be a success in the residential property market.

4.4 Case study on a Real Estate *Instalment Sale Agreement* development project

A project was investigated as part of the case study. The project aimed to make use of *Instalment Sale Agreement*s as primary funding method to sell the properties. The case study discussion follows:

4.4.1 Initial project plan:

Year:	2013
Project name:	Protea Glen x27
Location:	Protea Glen, Johannesburg South

Note*: The Developer, Project managers and the contractor requested not to be mentioned by name.*

Products:	$45m^2$ Simplex (2 Bedroom, 1 bathroom)
	$50m^2$ Simplex, (2 Bedroom, 1 and a half bathroom)
	$55m^2$ Simplex, (3 Bedroom, 1 and a half bathroom)
	$60m^2$ Simplex, (3 Bedroom, 2 bathrooms)
Specification of product:	High quality face brick houses for the “just above affordable market”
Scope of Work:	$45m^2$ Simplex – 151 units
	$50m^2$ Simplex – 114 units
	$55m^2$ Simplex – 76 units
	$60m^2$ Simplex – 38 units

Project Phasing:

Project was programmed over 12 months.

379 Simplexes total.

6 phases of construction.

- Phase 1 – 61 simplexes
- Phase 2 – 61 simplexes
- Phase 3 – 63 simplexes
- Phase 4 – 58 simplexes
- Phase 5 – 67 simplexes
- Phase 6 – 69 simplexes

Note: *The construction followed a 'fast-track' construction programme. Thus, by the time the last foundation was poured on phase 1 the first few houses of phase 1 would have been 100% complete and foundation construction would roll over to phase 2 while the houses of phase 1 are completed. This form of programming ensured continuity from the construction and project management side of the project.*

Project period & dates: Project Start date: May 2013

Project End date: April 2014

Interim phasing programmes: roughly 63 days per phase from start to practical completion of the phase.

Selling Prices of houses:	45m²	-	R380 000
	50m²	-	R410 000
	55m²	-	R430 000
	60m²	-	R455 000

4.4.2 Actual programme and events of the project

The project started in May 2013. Phase 1, 2 and 3 were completed by 15 November 2013. In total 185 houses were built in this time frame. Approximately 33% of the 185 houses were already sold on the instalment sale agreement bases by the end of October 2013.

On the positive side, a further 35% of the 185 houses are in progress with financing approvals, which indicates that there is a definite demand and progress were made with the sale of the units.

Earlier in September 2013 the developer took a decision to only develop up to the completion of phase 3 and then to put Protea Glen x 27, an *Instalment Sale Agreement* development, on hold for an indefinite period until the actual secured sales have improved.

The reason for the delay on the contract was due the fact that the sales were behind the construction to such an extent that it doesn't make financial sense to continue building any additional units until such time that the sales caught up with the development progress. The developer has subsequently announced that the development of phase 4, 5 and 6 will commence early in 2014. The last 3 phases are estimated to take up to 7 months to complete. Marketing and tenant education has subsequently been put in operation to affect accelerated sales. The sales for phase 4, 5 and 6 are scheduled to commence before phase 3 is completed.

The developer has reported on the reason for the sales that lacked behind and attributed it to phases 1-3 being the starting phases of the project. Marketing and tenant education needed to be more efficient and effective from the point of initiation of the project, especially due to the fact that the units were being sold by means of a unique financing method.

Protea Glen x 27 is being developed adjacent to previous “Gap” market developments from the same and other developers. The neighbouring developments were developed on either an affordable housing project principle for the rental market or to be sold on the conventional mortgage bond financing method. Though not inferior, the projects are of lower standard, quality and aesthetic value, but the financing method of these projects was based on financing products that the potential buyers were familiar with. On the other hand, *Instalment Sale Agreement* is a new financing method available to the market and it seems that instalment sales, with regards to property, are slow to catch on with potential home buyers and as a direct result it attributes to unfounded consumer insecurity.

In analysing the trends observed with the said development one can only deduct that even with an intensive marketing strategy, buyer education as well as the initial positive reaction by most of the target market, the potential residential property buyers probably still feel that buying a home is a huge financial commitment and in order to minimise risks, they are more likely to purchase the house by means of a financing method that has been tried and tested. It seems that some would even resort to renting a property rather than, what they would consider, to risk purchasing a property on a relatively new and unknown financing option.

4.4.3 Summary of lessons learnt in the project thus far:

- Some potential homebuyers regard the *Instalment Sale Agreement* as a new financing product that they are not familiar and trusted with.
- Hands-on marketing and tenant education are considered absolute necessities to ensure credible interest in developments sold by means of *Instalment Sale Agreement* method.
- Rental and conventional bond methods are trusted and preferred to the *Instalment Sale Agreement* financing method, but intensive marketing strategies, tenant education and affordability to the purchaser have the potential to change the general perspective.
- Of the plan sales should be utilised in marketing and selling phases 2 to 6. Once completed, phase 1 must be employed to demonstrate and illustrate the feasibility and inherent possibilities with units developed and marketed by means of the *Instalment Sale Agreement* product.

4.5 Conclusion

In order for the *Instalment Sale Agreement* option to be used, both sellers and buyers need to be open to this financing option.

Depending on the housing market dynamics, as well as the supply and demand ratio in the housing industry and the lending appetite of the credit providers, residential developers might be very keen to investigate the possibilities and make increased use of the *Instalment Sale Agreement* option.

The *Instalment Sale Agreement* option will lead to improved affordability of residential property for the average individual and thus provide the developers with the potential to develop and sell more units.

The *Instalment Sale Agreement* concept is still considered a fairly unfamiliar funding option in South African housing market, but as it is increasingly introduced in the market place the average prospective buyer will be more willing to accept the concept due to the underlying advantages and more individuals able to qualify for housing finance.

5. CHAPTER 5 – SUMMARY AND CONCLUSION

5.1 Introduction

Ownership of a property is often enough to grant people a sense of achievement, security and protection that they strive for in life. Traditionally in South Africa, there are limited legal options available to the prospective home owner to gain formal access in order to secure ownership of residential property. These options range from purchasing a residential unit by means of a registered mortgage bond, with or without government subsidies, obtaining ownership of a property by means of the Reconstruction and Development Programme (RDP) or renting a property.

For the majority of people, the purchase and ownership of a residential property constitutes their most prized yet expensive financial investment. They normally have to finance the purchase of a preferred residential property by means of an approved mortgage bond which implies that they often have to qualify in accordance with strenuous and at times virtually impossible criteria set by the financial credit provider.

The prospective South African home owner has only one of two finance options available to them. They either have to have enough money saved up in order to purchase the property in cash money or they could apply at a registered credit provider for mortgage funding.

Due to the difficulty in raising funds, prospective property owners are forced to look elsewhere for alternative options of purchasing properties. The *Instalment Sale Agreement* could possibly be considered as one of the options available to the prospective home owner to explore.

An instalment sale entails that an approved credit provider may lend the purchaser money to purchase a residential property by means of an *Instalment Sale Agreement* (ISA). The credit provider will source and identify suitable clients in terms of their credit policy and offer an *Instalment Sale Agreement* option to them. Once the client has been informed and educated on the *Instalment Sale Agreement* method of financing and he/she has indicated and declared intent and desire to purchase a particular property by means of the option, the credit provider will initiate and proceed with a formal credit process.

The principals of an *Instalment Sale Agreement* contract for a residential property are similar to that of the principals of purchasing and securing motor vehicle finance and furniture finance.

The Alienation of Land Act, 1981 as cited by Griffon (2012:1) defines an Instalment sale agreement as, an agreement of sale of land as defined in terms of the Alienation of Land Act, 1981 used or intended to be used mainly for residential purposes and in terms of a contract as defined in terms of the Alienation of Land Act, 1981 in terms of which the purchase price is paid to the seller by way of more than two instalments over a period of longer than one year. If the land is not held under a separate title deed at the point of entering into the contract the period of repayment in terms of the contract, may not exceed five years.

Ownership of the title deed of the particular asset only transfers from the owner of the property to the purchaser once the loan granted has been settled and covered in full. Another similarity to conventional bond finance is that the buyer has the same benefits and responsibilities as with mortgage bond finance.

5.2 Main research problem

The main question this study aimed to answer was whether an *Instalment Sale Agreement* could be considered a viable property financing alternative for both the purchaser as well as the credit provider. The study focussed especially on properties sold in the market at a value above any government subsidy programmes but at the same time below R500 000 in the Gauteng province of South Africa.

5.3 Sub questions

In order to answer the main research question a couple of sub questions had to be answered.

5.3.1 First sub question

The first sub question that this study aimed to answer was whether developers found it feasible to develop and sell these properties on the basis of an *Instalment Sale Agreements* for the specific target market.

5.3.1.1 Research findings

There is currently a large backlog for housing in South Africa. The government has however got strategies in place to counter this backlog and provide for more houses or opportunities to own a residential property for those in the country that do not have the privilege of owning a house.

While the government provides a comprehensive housing subsidy programmes, its capacity to meet the growing demand and backlog is seriously challenged, especially given reduced GDP growth rates and rising unemployment and the ever rising population figure.

It is therefore very imperative for housing to be developed and provided right across the country for all income groups.

The *Instalment Sale Agreement* concept is still a fairly unfamiliar funding option in South African housing market, but if it is introduced more and more in the market the property developer and prospective residential property owner will become more accustom to it and will therefore be more than willing to accept it in the market place.

Thus, the *Instalment Sale Agreement* is considered to be a viable option for the developer. It provides the developers with more demand in the market to develop for, and more viable developments effectively imply a better income and profit stream for the developers.

5.3.2 Second sub question

The second sub question that this study aimed to answer was whether prospective clients will be willing to purchase residential property on the *Instalment Sale Agreement* model and at the same time accept this as a viable alternative financing method compared to the conventional method of purchasing a property in South Africa.

5.3.2.1 Research findings

The research conducted and common knowledge both dictates that people across all income groups wants to own a house in which they and their family can live, feel secure in and prosper.

For the majority of people, the purchase and ownership of a residential property constitutes their most expensive financial investment ever. Thus, a prospective home buyer will seek out the most secure but affordable and financially convenient method to purchase a home.

The *Instalment Sale Agreement* does offer an option whereby more prospective home buyers could qualify to purchase a property due to the structuring of the financial responsibilities in such agreement.

The research findings in chapter 4, clearly supports the above statement.

The research findings show that there will be an interest in alternative funding methods if it provides the buyer with a possibility and opportunity to successfully apply and qualify to purchase a property.

The research findings indicate that only a small portion of people do not believe that *Instalment Sale Agreement* option could be successfully implemented in the residential property market. The majority believes that it would be possible to successfully introduce and employ it in the market. However, adequate attention should be given to the education of the consumer on all aspects and benefits of the *Instalment Sale Agreement* concept as a crucial element to ensure success. In addition, research findings also indicated that the general prospective buyer needs to be educated thoroughly on safe and secure alternative financing methods available to purchase property. By educating the prospective home buyers they will become more accustom to alternative financing options and it might be that a financing option like the *Instalment Sale Agreement* just might become the most sought after financing option when property is purchased.

5.4 Recommendations for future studies

The study indicated that:

- Developers and credit providers should consider making the understanding of housing finance and concepts easier to understand for the average person.
- Tenant/buyer education regarding housing finance should be a bigger priority for credit providers. More people would consider applying for this form of housing finance if they understand the relevant concepts better.

The study revealed and highlighted further areas of research, which may be investigated.

The following questions in a South African context were identified:

- Why have the *Instalment Sale Agreement* concept not yet taken over a certain section of the property market in South Africa?
- Has the *Instalment Sale Agreement* concept made a difference in home financing in other countries?

- Which property market segment is most appropriate for the *Instalment Sale Agreement*?

5.5 Conclusion

The Alienation of Land Act, 1981 defines an *Instalment Sale Agreement* as, an agreement of sale of land used or intended to be used mainly for residential purposes and in terms of a contract as defined in terms of the Alienation of Land Act, 1981 in terms of which the purchase price is paid to the seller by way of more than two instalments over a period of longer than one year.

The *Instalment Sale Agreement* concept does offer an option whereby more prospective home buyers can qualify to purchase a property due to the structuring of the financial responsibilities of such an agreement.

Instalment Sale Agreements offers the developers with the possibility of more demand in the market to develop for and therefore provide them with more opportunity of financially viable developments. This in turn will effectively culminate in better income and profit stream and margins for the developers.

With improved advertising and education on the *Instalment Sale Agreement* concept and its place in the property market, *Instalment Sale Agreements* will be seen as a viable property financing alternative for both the purchaser and the credit provider in the residential property market for properties positioned at a value above government subsidy programmes but at the same time beneath the R500 000 mark in the Gauteng province of South Africa.

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- Conventional penalties act ACT

- ALA - ACT

7. ANNEXURES

7.1 ANNEXURE A - Questionnaire to Credit Providers and Developers

7.2 ANNEXURE B - Survey to possible home buyers