experian

Business Debt Index

Quarterly Summary - Q4 2021

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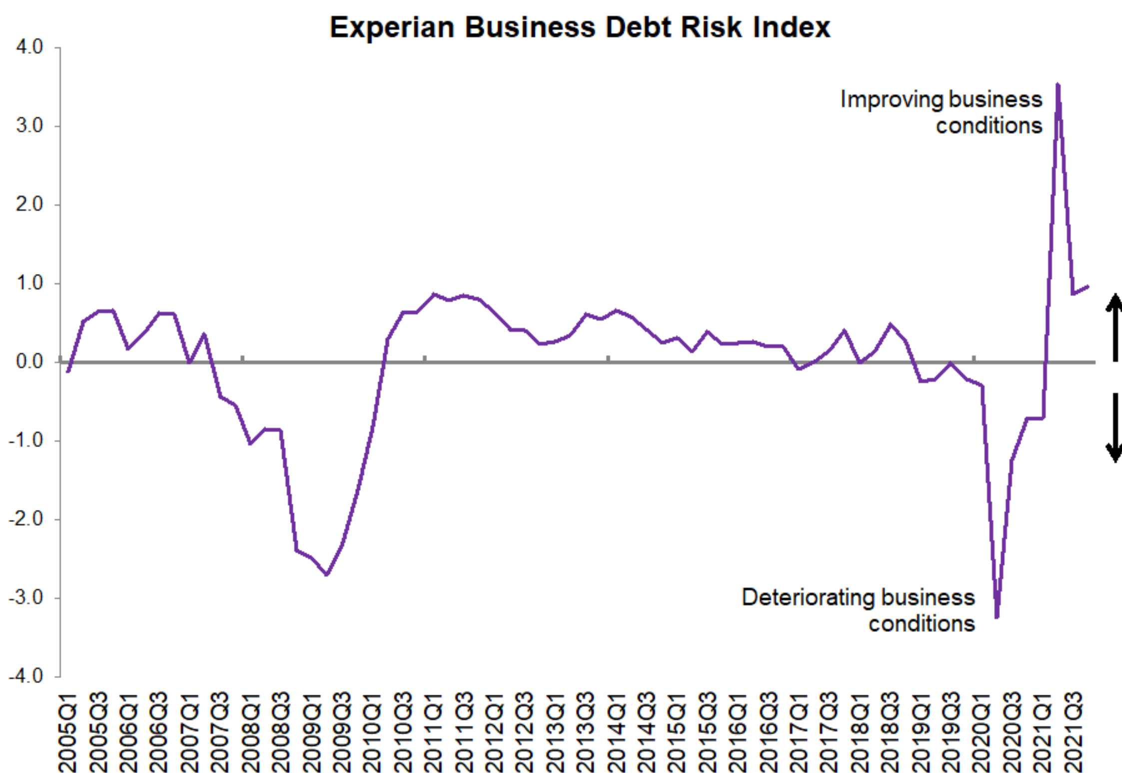
EXPERIAN BUSINESS DEBT INDEX (BDI) RESULTS FOR Q4 2021

Improvement in Q4 BDI in line with the recovery in q/q economic growth

The Experian Business Debt Index (BDI) unexpectedly rose in Q4 2021, to a reading of 0.966, from 0.863 in Q3 and 3.534 in Q2. The latter two figures were themselves revised upwards from 0.808 and 3.476 respectively.



	Q4 2020*	Q1 2021*	Q2 2021*	Q3 2021*	Q4 2021*
Index >0= Improving business conditions <0 = Deteriorating business conditions	-0.720	-0.694	3.534	0.863	0.966

** Revised*

Business debt metrics in Q4 2021

One had expected the BDI to decline slightly in Q4 on account of the lagged effects of the looting spree and social unrest experienced in Q3 (July specifically) on the financial position of companies.

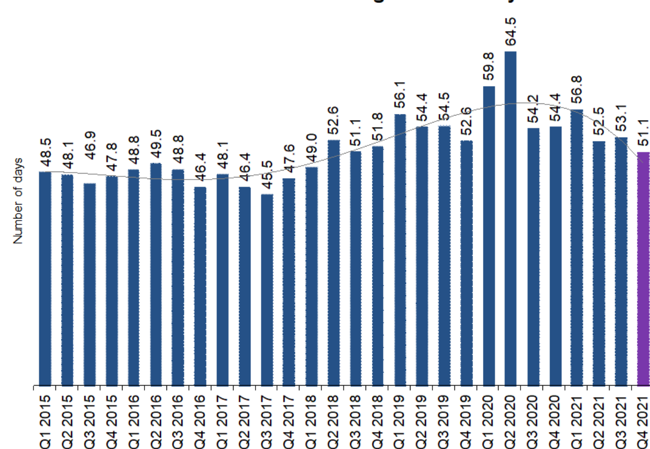
Instead, based on the Experian outstanding debtors' days figures, there was an unexpectedly modest improvement rather than deterioration in Q4.

Even though the repo rate was increased by 0.25% in November, representing the first such interest rate increase in seven years, the fact was that the prime overdraft rate was still 2.75% lower than it had been prior to the onset of the COVID-19 pandemic.

As such, businesses and consumers continued to benefit from sharply lower debt servicing costs. In addition, consumers' savings had benefited for two years from them working from home rather than spending money travelling to the office. Increased savings had also been accumulated over the preceding 18 months by consumers as a result of a reluctance to spend on restaurants and leisure activities and going on holiday for fear of contracting the COVID-19 virus.

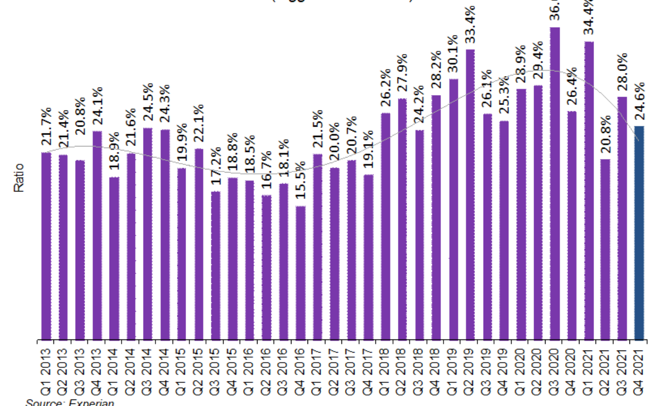
From a business perspective, insurance payouts by SASRIA to compensate them for damage inflicted on them in the social unrest and looting in July 2021 had amounted to R17.1bn by mid-February 2022, and the intention is for SASRIA to have issued R27bn in compensation by the end of March. Together with the R5bn relief issued to small businesses as well as the compensation paid to employees of such businesses through the Temporary Employee Relief Scheme, it would appear that businesses received significant assistance to help them cope financially with the ravages of both the COVID-19 lockdown and the July looting episode.

In the event, the average number of outstanding debtors' days decreased to 51.1 in Q4, from 53.1 in Q3 and a peak of 64.5 in Q2 2020. The 51.1 average for outstanding debtors' days in Q4 2021 was, in fact, the lowest such figure since Q1 2018.

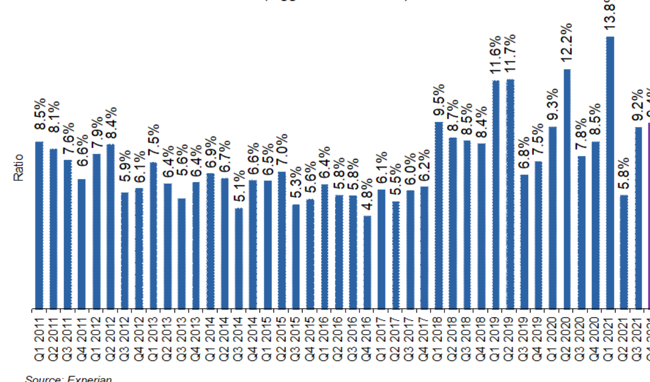


It would appear that the better-than-expected outcome for the Experian outstanding debtors' days figures in Q4, played an important role in the BDI coming in stronger than expected in Q4.

More specifically in the measurement methodology of the BDI was the fact that **30 to 60 days ratio**[1], declined quite sharply to 24.6% in Q4, from 28.0% in Q3.



Even in the case of the **60 to 90 ratio**[2], there was only a marginal increase from 9.2% in Q3, to 9.4% in Q4.

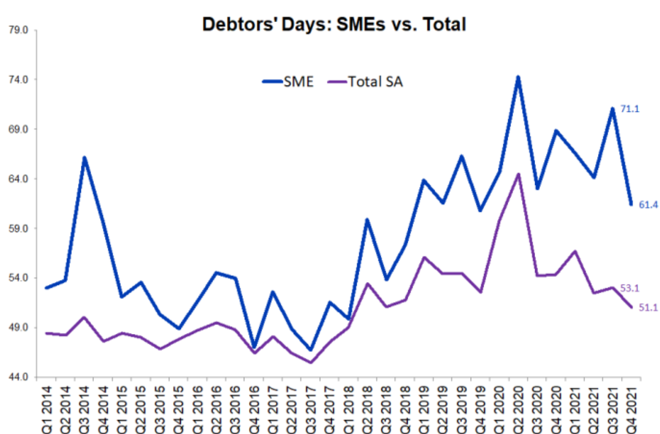


[1] *The ratio of outstanding debt owed of 30 to 60 days relative to that owed of less than 30 days lagged by one month*

[2] *Outstanding debt owed of 60 to 90 days relative to debt owed of less than 30 days lagged by two months*

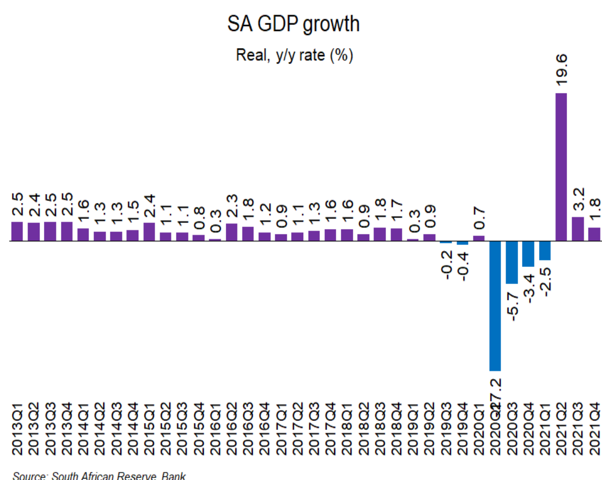
BDI by company size

Specifically, in the case of small businesses, there was a fairly dramatic decline in outstanding debtors' days, from 71.1 in Q3 to 61.4 in Q4. As a result, the SME stress ratio, which divides the number of outstanding longer-term debts by the number of shorter-term debts outstanding, plummeted from 33.7% in Q3 to 22.3% in Q4, the lowest level in five quarters.



Macroeconomic factors influencing Q4 2021

Nonetheless, macroeconomic factors also contributed to a relatively positive outcome. This was notwithstanding the fact that the domestic GDP growth rate on a y/y basis declined in Q4, to 1.8%, from 3.2% in Q3. The decline in the y/y growth rate was, however, to be expected, being largely statistical in nature. GDP had grown strongly in Q4 2020 in the wake of the lifting of lockdown restrictions that had been imposed earlier in the year to fight COVID-19.



Source: South African Reserve Bank

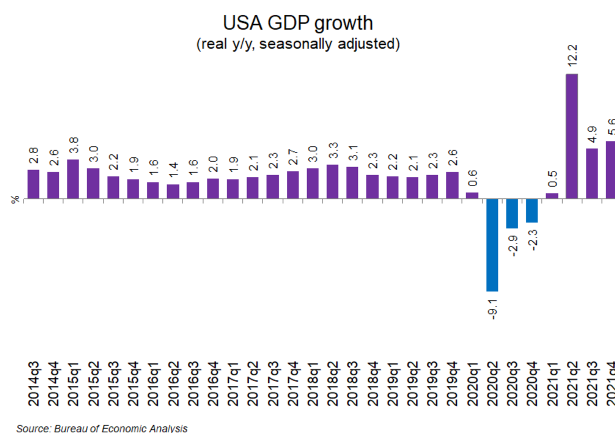
Consequently, on a comparative basis, one was comparing against a very strong base for a year earlier even though on a q/q basis, GDP growth actually improved quite significantly in Q4 2021 compared with Q3 2021 (to a positive 1.2% from a negative -1.7% respectively), reflecting some recovery from the damaging effects of the looting spree in July last year.

The fact is that the relative improvement in recovery from the looting in the latter part of 2021 was not as great in magnitude as that which emanated from an economy recovering over the same period of 2020 from a situation where virtually half the economy had been put out of action by hard lockdown earlier in the year.

Q4 2021 was also impacted somewhat negatively by the renewed onset of load-shedding, as well as by concerns relating to the onset of the Omicron variant of COVID-19 in early November. Fortunately, in respect of the spread of the new variant, the impact did not turn out to be as severe as one might have feared. Consequently, there was no need for the government to reimpose severe lockdown restrictions over the Christmas holiday season, as had been the case a year earlier.

The important fact is that notwithstanding the decline in y/y domestic growth in Q4, the other components of the macroeconomic data making up the BDI tended to play a positive role in supporting the index.

Global growth in Q4 did not slow as much as one might have anticipated in the wake of the termination of relief measures in the US and elsewhere. The benefits of those relief measures continue to manifest themselves with the lag. The US economic growth rate, in fact, accelerated to 5.6% y/y in Q4, from 4.9% in Q3.

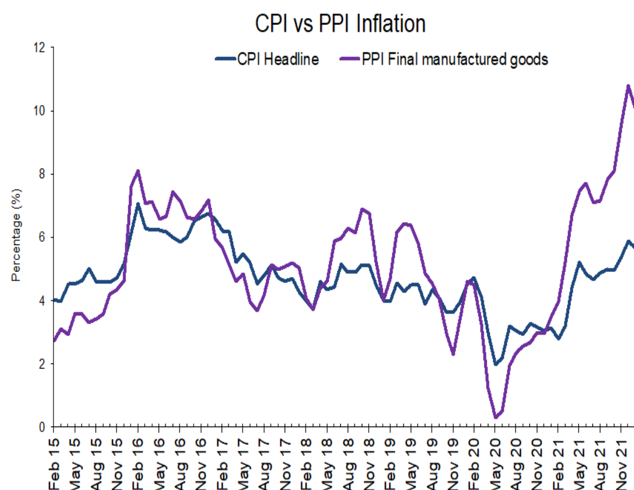


Source: Bureau of Economic Analysis

Concerns about higher US interest rates and a tapering off of quantitative easing were in evidence more in

contemplating their future rather than in terms of their immediate impact.

From a macroeconomic perspective, the BDI also benefited from an increase in the difference between the PPI and CPI inflation rates. Both increased significantly over the course of the quarter, but the former rose more sharply, interpreted as a proxy for expanding profit margins.



Source: StatsSA

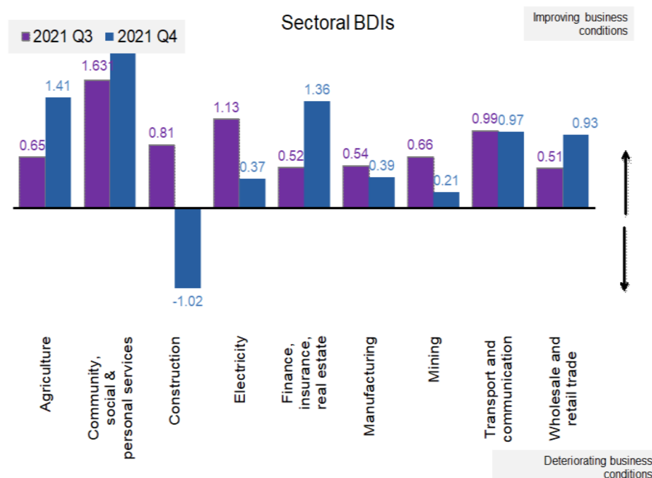
In addition, interest rate movements domestically also had a positive role to play in boosting the BDI. Longer-term interest rates domestically rose relative to short-term interest rates, traditionally interpreted as a harbinger for an improvement in growth prospects for the local economy. There was a small increase in the differential between short-term interest rates in South Africa and those in the US, which is a proxy for international borrowing costs. Fortunately, its impact was not material.

Nonetheless, on reflection, it was the positive impact of the relative improvement in the financial position of consumers and businesses, which had been underestimated three months ago which played an important role in enabling the BDI to rise slightly in Q4 when a decline had been anticipated. This relative improvement was reflected subsequently also in the continuing strong overrun of growth in government revenue and healthy trade surplus arising out of commodity prices remaining relatively high in the wake of the improvement in global economic growth.

Finally, there was a very strong surge in agricultural output, specifically in Q4, following excellent rainfall in the summer crop-growing regions.

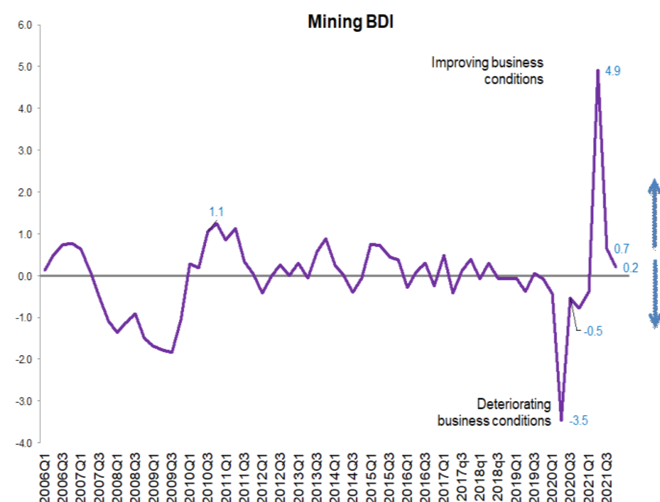
BDI by sector

Indeed, from a sectoral comparative perspective, the agricultural sector stands out as having recorded the best improvement in business debt conditions in Q4. There was also a solid improvement in debt conditions in the finance, insurance and real estate sector, presumably linked to the rollout of insurance payments by SASRIA.



The recovery in the financial position of consumers in Q4 was also reflected in a significant improvement in business debt conditions of the wholesale and retail trade sector.

However, there were also sectors that recorded a substantial relative deterioration in their business debt conditions. These included electricity and mining, largely one suspect because of the renewed onset of load shedding in Q4, which had been relatively absent in the previous quarter.



Nowhere was the deterioration in business debt conditions more severe, however, than in the construction sector. Yet again, this illustrated the manner

in which the absence of progress made in implementing infrastructural investment projects is impeding the delivery of services in the country.

The lag between growth in fixed capital formation on the one hand and more robust consumer spending, on the other hand, is likely to continue acting as a significant constraint on the economy's ability to grow more rapidly in the longer term.

Outlook

Unfortunately, many of the factors contributing towards the improvement in the BDI are likely to unravel somewhat in forthcoming quarters. This is mainly attributable to global factors.

The phasing out of COVID-19 relief measures in the world's advanced economies stands to weigh down on economic growth prospects.

In particular, a surge in global inflation arising out of a variety of supply shortages due to insufficient investment in new sources of supply, but also due to disruptions in logistics caused by COVID-19, is compelling leading central banks to contemplate tightening monetary policy reasonably aggressively.

The bond-buying programmes introduced by global central banks two years ago to add liquidity to the world economy as a relief measure is being phased out. This is also causing ructions on global financial markets, which have depended upon the abundance of liquidity over this period to thrive.

The prospect of higher interest rates around the world is no longer conducive to expectations of improved economic conditions. Rising long-term interest rates also pose a threat to governments' ability to introduce further fiscal stimulus to counteract economic slowdown because debt servicing costs are set to rise substantially given the high levels of public debt prevailing.

In light of the negative outlook for the world economy, it is not surprising to see that the BDI forecast for Q1 2022 sees the index falling back somewhat. The potential negative impact of load shedding on the domestic economy also needs to be taken into account.

Most recently, of course, is a new and potentially potent threat to the sustainability of solid economic growth from the Russian invasion of Ukraine.

Sanctions imposed by the West on Russia for its actions, has already contributed towards fears of insufficient supplies of commodities and a resultant sudden surge in commodity prices, especially in the price of oil.

Short-term inflationary pressures are therefore likely to be exacerbated and will contribute towards an erosion of disposable income of consumers around the world.

Such pressures could also be heightened further by the renewed surge of COVID-19 infections in China which has imposed new lockdown restrictions in many cities. Supply-side shortages potentially could worsen as a consequence, resulting in higher inflation remaining more entrenched globally than previously anticipated.

South Africa is fortunate in the short term in benefiting from the rise in the prices of many of the commodities that it produces in competition with Russian supplies.

The mining, agricultural and related sectors, therefore, stand to profit from a continuation of the improvement in revenues seen over the past 18 months.

These developments may support the BDI to remain in positive territory for a number of forthcoming quarters. However, one is concerned that in the longer term, we could see the BDI falling back into negative territory in line with the marked slowdown in global economic conditions as the full effects of the latest geopolitical tensions play out on the world economic stage.

Explanatory notes regarding the Experian Business Debt Index

What is the Experian Business Debt Index?

The Experian Business Debt Index (BDI) is an indicator of the overall health of businesses, as well as the South African economy. It measures the relative ability for business to pay its outstanding suppliers/creditors (i.e. amounts owed to other businesses) on time and tracks macro-economic indicators that can impact on the ability of companies to pay their creditors.

A number of debtors and macro-economic variables are combined into a single indicator of business debt stress.
In other words, the BDI is a reflection of the overall health of businesses and the position of debt settlement between businesses in the economy.

How to interpret the index

The Experian BDI, as an indicator of the overall health of businesses, measures the relative ability of businesses to pay their outstanding creditors on time. It also incorporates trends in macroeconomic indicators, insofar as these impact on the ability of companies to pay their creditors. The index is constructed around a mean value of zero.
Values above zero indicate less business debt stress and values below zero indicate business debt stress.
Given the underlying data of the index, relative higher levels of debt indicate a weakening in the ability to pay outstanding creditors. Higher interest rates result in higher borrowing costs and an increase in business stress. Relatively higher production costs vs consumer costs decrease operating margins of business, while higher domestic and international growth could result in a better trading environment for businesses.

Measured by using principle components

The Experian Business Debt Index (BDI) is constructed using principal components analysis. This is similar to the St. Louis Fed's Financial Stress Index (STLFSI) and the Kansas City Fed's FSI (KCFSI) in the USA. The principal components analysis is a statistical method that is used to extract factors responsible for the co-movement of a group of variables. As such, it is assumed that business stress is the primary factor influencing the co-movement and by extracting the principal components, it is possible to build an index with a useful economic interpretation.

Variables included

The Experian Business Debt Index is made up of Experian business debtors' data and public domain data. Variables include the following:

- 30 – 60 debtor days' ratio (debt compared to initial amount invoiced 30 days ago);
- 60 – 90 debtor days' ratio (debt compared to initial amount invoiced 60 days ago);
- South Africa consumer inflation and producer inflation spread;
- Interest rate spread (Repo vs US Federal Fund rates);
- Interest rate spread (R157 vs Repo);
- Real SA GDP (year-on-year percentage change);
- Real US GDP (year-on-year percentage change).

No provision is made for any leads or lags in any of the variables.

Methodology used to construct the index

The index is constructed by first demeaning the individual indices - subtracting the index value from the index average and dividing it by the sample standard deviation (SD). The indices can now be expressed in the same units. Next, the method of principal components is used to calculate the coefficients of the variables in the EBSI. These coefficients are scaled so that the standard deviation of the index is 1. Lastly, each of the indices is multiplied by its respective adjusted coefficient.

When the index is updated quarterly, the values of the Experian Business Debt Index can change. This can occur either through a change in the coefficients (an updated re-estimation) or because of a change in the actual values of the variables in the sample. Because the data are demeaned and standardised, the value of the original sample will change as the sample mean and sample standard deviation of the underlying variables change.

About Experian

We are the leading global information services company, providing data and analytical tools to our clients around the world. We help businesses to manage credit risk, prevent fraud, target marketing offers and automate decision making. We also help people to check their credit report and credit score and protect against identity theft. In 2016, for the third year running, we were named one of the "World's Most Innovative Companies" by Forbes magazine.

We employ approximately 17,000 people in 37 countries and our corporate headquarters are in Dublin, Ireland, with operational headquarters in Nottingham, UK; California, US; and São Paulo, Brazil.

Experian plc is listed on the London Stock Exchange (EXPN) and is a constituent of the FTSE 100 index. Total revenue for the year ended March 31, 2016, was US$4.6 billion.

To find out more about our company, please visit http://www.experianplc.com or watch our documentary, 'Inside Experian'.

About Econometrix

Econometrix is South Africa's largest independent macro-economic consultancy based in Johannesburg. We are privately owned and therefore totally independent of any official organisation or pressure groups. Econometrix – which has a successful track record of more than 38 years - is committed to on-going research and analysis of economic fundamentals thereby ensuring a sound basis for future business decisions. These services are provided through a range of complementary products to more than 150 South African and international organisations.

Our approach is to empower our clients with quality decision support intelligence and assistance regarding the economic and financial environment, and assist them in their strategic and financial planning processes. Our in-depth analysis of economic fundamentals aims to assist our clients in commanding the economic environment and in identifying opportunities and risks.

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Next release date for the BDI: June 2021

For more detailed analysis on the debt stress by sector, Experian publishes the *Business Debt Overview* report. Please contact Taryn Stanojevic at Experian for more information.