News release

Solid improvement in SA business debt conditions in Q1 – Experian data

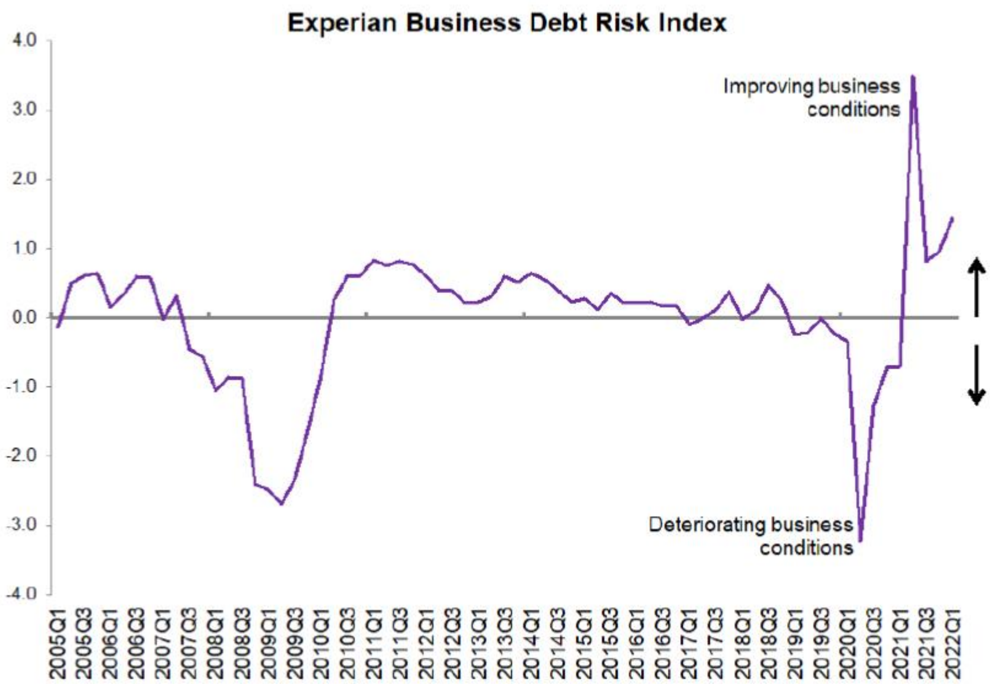
- *Outstanding debtors' days of SMEs drops to lowest level in three years*

Johannesburg, 16 August 2022 – There has been a strong improvement in business debt conditions in Q1 but this trajectory is likely to decline in the coming quarters, according to new insight from Experian South Africa.

The Experian Business Debt Index (BDI) increased in Q1 from Q4 2021, rising to 1.435 from an upwardly revised 0.970.

The principal contributors to the improvement in the Q1 BDI were a pickup in domestic and US economic growth during that quarter. Domestically, the adverse effects of the looting and unrest experienced in Q3 of 2021 continued to fade during Q1 of 2022.

Jaco van Jaarsveldt, Head of Commercial Strategy and Innovation at Experian Africa said: "A combination of stronger than expected local and international economic growth along with the continued stabilisation of supply chains post the Q3 looting, contributed to the improved BDI reading in Q1. Whilst positive overall, one should be cautious not to read too much into these numbers with the impact of the April floods in KwaZulu Natal, the significant increase in electricity disruptions and the ongoing war in Ukraine expected to reverse the improving trend in coming quarters."



Macroeconomic factors influencing Q1 2022

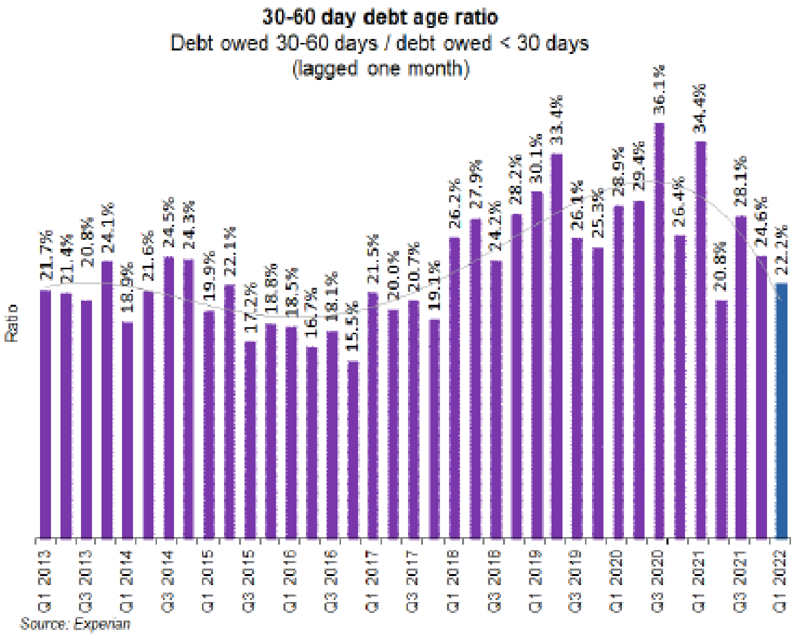
Macroeconomics factors that contributed to the improvement in the Q1 BDI were a pickup in domestic and US economic growth during that quarter. In addition, commodity prices remained elevated in Q1 this year, supported by supply-side shortages globally caused by disruptions to supply chains emanating from lockdowns introduced to fight off the omicron variant of COVID-19.

During that time, the Russian invasion of Ukraine exacerbated such shortages. Furthermore, the reintroduction of hard lockdowns in several Chinese cities extended supply disruptions, especially concerning fossil fuels and food commodities. Domestic interest rates continued at levels well below those that prevailed before the onset of COVID-19; this gave support to retail sales, as did the increased health of personal balance sheets.

Business debt metrics in Q1 2022

The improvement in the BDI in Q1 2022 was not, however, confined to domestic macroeconomic factors alone. Experian data on debt age ratios also had a significantly positive impact – both in the case of the 30-60 day and the 60-90 day debt age ratios.

The 30-60 day debt age ratio improved from 24.6% to 22.2% in Q1. The improvement in the 60-90 day debt age ratio was even more significant from 9.5% down to 6.3%.

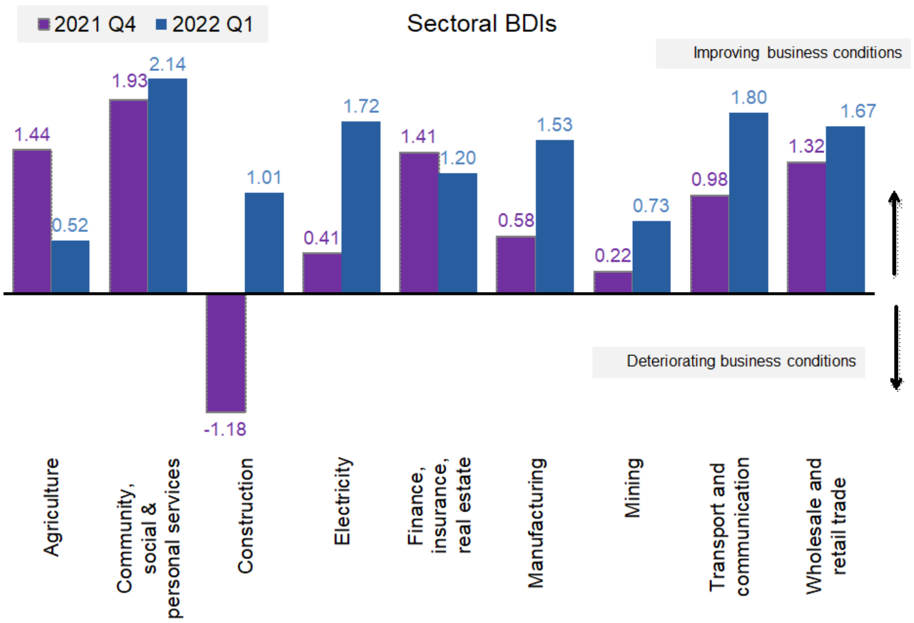


In the 30-60 day debt age ratio, the improving trend has been quite sharp, following the all-time highs observed in Q2 of 2020 of 36.1%.

“The ability of borrowers to benefit from the reduced debt-servicing costs following the 30% reduction in domestic interest rates in the first half of 2020 certainly contributed to this improvement,” said van Jaarsveldt.

BDI by sector

The improvement in the Q1 BDI was transmitted through most sectors of the economy. Every one of the nine sectors recorded a positive BDI in Q1 of 2022, reflecting improved financial health.



The one sector that had seen business debt conditions deteriorating in Q4 of 2021, construction, saw positive business debt conditions returning in Q1 this year. Only in the case of agriculture and financial services did the BDI reading deteriorate from extremely strong to modestly strong in Q1 of this year. This, in turn, was a function of a comparison against a strong base for the previous quarter.

There were particularly impressive increases in the BDI in respect of manufacturing and, associated with this, electricity. These improvements reflect a return to normal conditions following the devastation of industrial activity caused in KwaZulu-Natal in Q3 2021 by the social and political unrest at the time.

BDI by company size – SME ratio

Outstanding average debtors' days of SMEs declined to 61.4 in Q1 of 2022, from 64.3 in Q4 of 2021 and 72.4 in Q3 of 2021 at the height of the looting spree.

SMEs are still under a lot more strain than larger companies if you compare this to the 50.5 days outstanding for the whole sample of companies for which Experian has data. Yet, the number of outstanding debtors' days of SMEs has fallen to its lowest level in three years.

Similarly, the SME stress ratio (the number of SMEs with outstanding debts of less than 60 days relative to those with debts outstanding of more than 90 days) fell to 22.3% in Q1 of 2022, from 35.4 and 25.2 outstanding debtors' days respectively for Q3 and Q4 of 2021. This ratio is the lowest since Q4 of 2019.

Declines in BDI expected

Unfortunately, the improvement in business debt conditions identified in Q1 of 2022 is likely to be reversed in Q2 and probably in subsequent quarters as well.

Domestically, data on mining and manufacturing activity for April reflects a significant decline compared with earlier months this year. An intensification of electricity load-shedding and strike activity in both sectors appear to have impacted negatively on output.

The heavy rains and flooding that occurred in KwaZulu-Natal during April are likely to have inflicted damage on several businesses in the region, especially those involved in manufacturing, sugarcane farming and importing or exporting through the Durban harbour, which was severely damaged.

Q2 is likely to witness the adverse impact of the 0.75% cumulative increase in the repo rate between November and March and the additional 0.75% rate hike in May. It is also likely that interest rates will increase further over the remainder of the year in the wake of rising inflation, especially in food and fuel prices.

Van Jaarsveldt concludes: “The adverse impact on business debt conditions is unlikely to be confined to domestic factors alone. Internationally, the continuation of the Ukrainian war without any apparent signs of an end threatens to sustain shortages of vital industrial materials and food commodities. The continued global price pressure is set to drive leading central banks worldwide to continue raising interest rates more steeply than had been imagined.

“The South African consumer will also feel the pain of the negative global sentiment. The latest consumer inflation (7.4% in June 2022) is the highest it’s been since May 2009 and is expected to remain high for some time. The impact of the continuous cost of living increase and increasing debt servicing costs is expected to negatively impact consumer spending and thus negatively affect the BDI further. It is thus recommended that businesses take a prudent approach to their debtor management strategies to minimise their own credit risk.”

[1093 words]

*****ENDS*****

Notes to the editor:

* Debtors' days is a metric of time measuring the average outstanding period (in days) that businesses take to repay their debt. A higher debtors' day value points to an environment where firms are taking longer to repay their outstanding debt obligations.

The Experian Business Debt Index is an indicator of the overall health of businesses, as well as the South African economy. It 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.

How to interpret the index: 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. 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.

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 the business stress is the primary factor influencing the co-movement and by extracting the principal components, it is possible to build and index with a useful economic interpretation.

For a more detailed analysis of business debt stress, Experian releases a Business Debt Overview report. The Business Debt Overview report constitutes of three main sections: The Business Debt Stress Index, a macro-economic overview and a sectoral debt analysis.

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