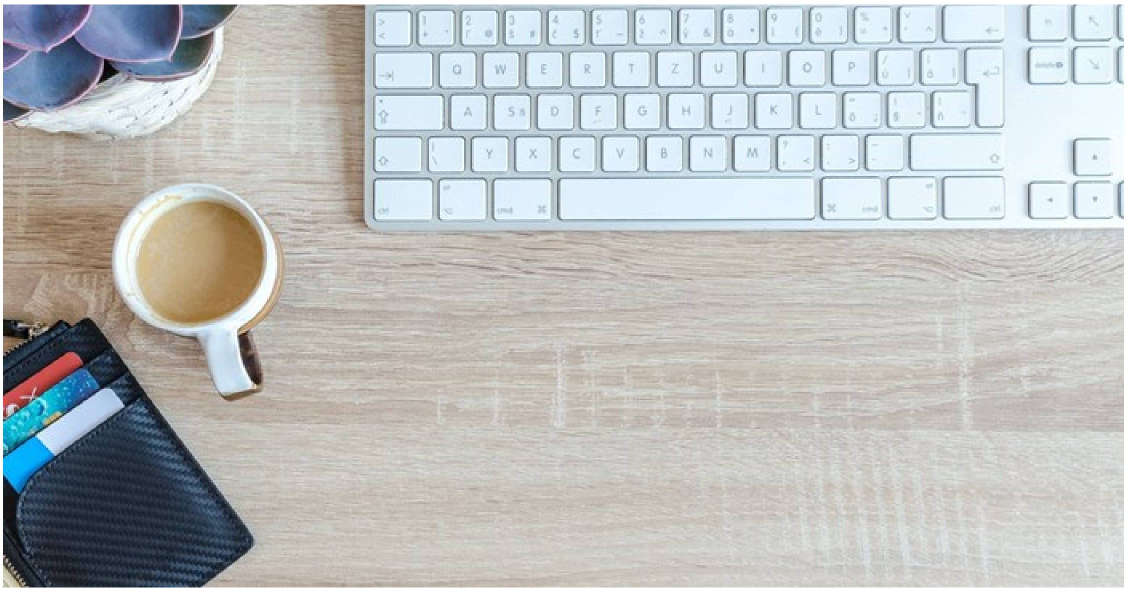
Consumer credit market sees modest improvements in Q3 2023

The statistics of Eighty20's Q3 2023 *Credit Stress Report* have been released.



Source: Pexels

It is early days, but the economic and credit indicators from quarter three highlighted a shift in outlook for the first time in over a year.

Here are the top five indicators:

- Inflation eased further to 5.0% from 6.2% in the previous quarter.
- The unemployment rate dropped below 32% (31.9%), with the number of employed persons up by nearly 400,000.
- Consumer confidence and the leading indicator of the economy has moved upward.
- In the credit space, the percentage of loans in arrears has come down to 37.5%.

The rate of new defaults is coming down

The rate of new defaults (RND) (the proportion of outstanding loan balances that went into default during the quarter across all loan products), which has been steadily increasing since 2022 Q1, trended down this quarter with the exception of vehicle asset finance (VAF).

This is a welcome reprieve from the double-digit year-on-year growth in the RND witnessed over the last three quarters. The RND is at 2.51%, up 25% from 2.01% a year ago. Although the annual change in the rate of new defaults (CRND) remains high, it is down 1.3% on last quarter.

The CRND is an early warning sign for the state of credit in the country. All loan products except VAF saw a drop in the rate of new defaults QoQ, with new retail defaults down nearly 6%.

From an Eighty20 National Segmentation (ENS) perspective, it was only the Middle Class Workers who still experienced an increase in overall RND from last quarter, but only by 0.2%.

Unpacking movements in data is complex and there are a few possible explanations – not all of them are necessarily good:

- **Hypothesis 1:** Things are getting better - people are managing their finances, cutting back on spending and making payments on debt.
- **Hypothesis 2:** Things literally couldn't get any worse - anyone who was going to default has already gone into default.
- **Hypothesis 3:** Credit providers have become significantly more risk averse in their lending and are therefore giving loans to people less likely to default.

The reality is probably a combination of all three factors.

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"The hypothesis that people have become more responsible about their debt is reflected in the credit-card numbers. While balances are still growing across all segments albeit at a slower rate, new defaults are down QoQ by 2.1%.

"The four wealthier ENS segments have been relying on their credit cards to make it to the end of the month. As a result, overall credit balances are up more than 30% since Covid - by comparison, overall loan balances are up 20%, with retail- and unsecured loans up barely one percent," says Andrew Fulton, director at Eighty20.

Year on year, total credit-card debt is up 9.5% but this is significantly lower than the double-digit growth experienced over the past two years – peaking at almost 15% in 2022 Q2. This drop in the rate of growth was seen across all ENS segments this quarter, with the Middle Class at 6.5% YoY growth and the Mass Credit Market at nearly 12% YoY growth.

Deeper dive into credit dynamics

Despite this slowing growth, the average credit-card loan balances for these segments are still twice their average monthly income. The average instalment to income ratio is the percentage of a person's income that goes towards payments on all their loan products.

This ratio has continued to rise, but, as with credit-card debt, not as rapidly this quarter. However, we do still see the Middle Class with nearly three quarters of their income going to instalments, Heavy Hitters at 60% and the Mass Credit Market approaching 40%.

The small improvement in the RND and slowing growth in credit balances may also support the hypothesis that we have reached the bottom, with most credit-stressed South Africans already in default.

Furthermore, credit balances for Heavy Hitters and Comfortable Retirees have seen reasonable growth, while the Mass

Market and Middle Class Workers have seen no growth in the value or volume of total loans over the past year.

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- Of the R166bn growth in credit balances over the past year, 95% came from just two segments, the Heavy Hitters and Comfortable Retirees, with nearly two-thirds of the value coming from home-loan balances.

- Home-loan balances (up 9.1% on last year) are unlike other loan products in that nearly 99% of home-loan balances are held by only three segments: the Heavy Hitters (75%), Middle Class Workers (17%) and Comfortable Retirees (7%).

- The Heavy Hitter segment accounted for R90bn (10.8%) YoY growth in home-loan balances while Middle Class Workers' balances remained flat, bringing the overall increase to R102.7bn.

- Nearly 750,000 people have entered the credit market this quarter for the first time, which is a return to pre-Covid levels. These individuals were responsible for nearly R8bn of the R29bn in new loans' value this quarter.

Credit providers tightening their belts

In August, there was quite a lot of press regarding a slowdown in bank lending. It reflected that bank-lending growth decelerated in June to its most sluggish rate in the past year, reflecting financial institutions' apprehension regarding stagnant economic growth and rising consumer debt.

This might account for the lack of credit growth we have been seeing in the lower-income segments. In their most recent trading updates, all the major banks have been speaking to elevated levels of credit impairments related to consumer banking. Banks pulling back on lending would also concentrate new debt in less riskier segments, resulting in the drop in QoQ new defaults.

“Regardless of the cause, for the first time in many months we have seen credit- and economic indicators move in a different direction. Given the year we’ve had, some joy towards the end is welcome,” concludes Fulton.