experian

The Impact of COVID-19 on Business

The State of Business Credit in South Africa

20 / 01 / 2021

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Update on credit appetite metrics

Credit Activity Trends – January 2021

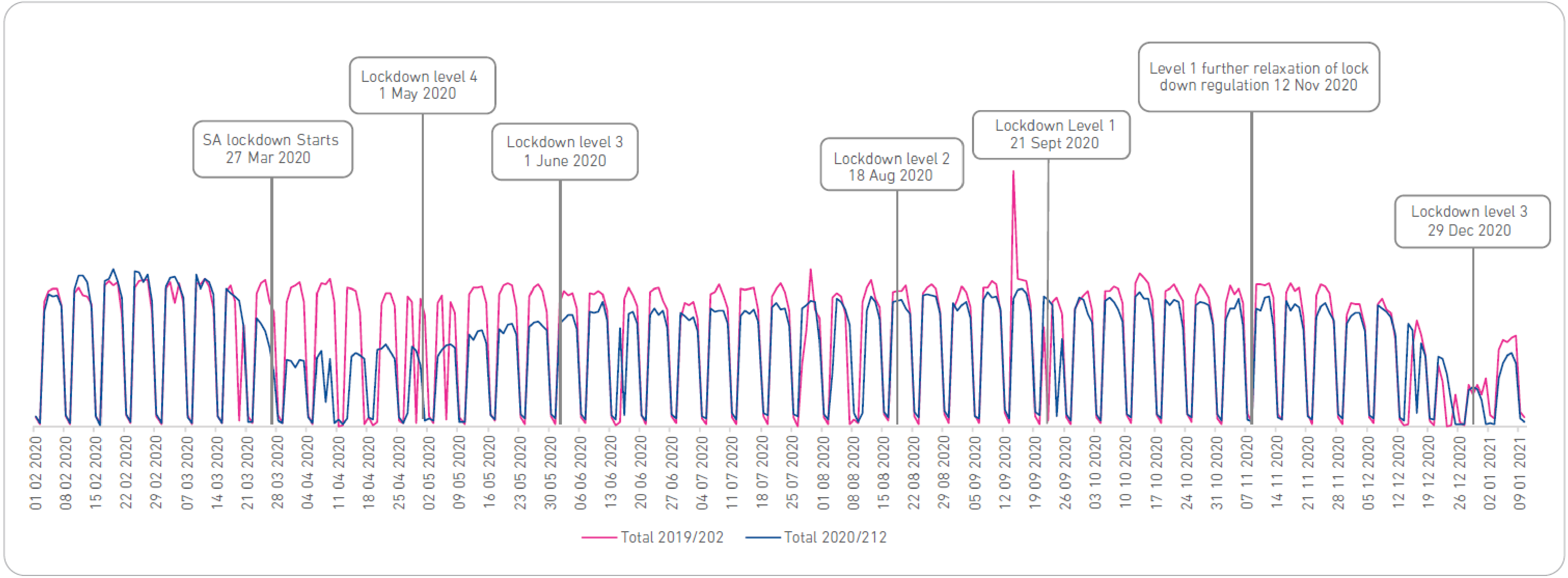
Overall Consumer Enquiry activity recovers to previous levels.

We observed that enquiry volumes have recovered to pre-lockdown levels – even slightly exceeding the levels observed over the same period in the preceding year. This highlights the increased demand for credit.

Credit Activity Trends – January 2021

Overall Business Enquiry activity still recovering to previous levels.

We observed enquiry volumes that have increased but not quite yet recovered to pre-lockdown levels. This suggests that, although credit appetite in business has improved since the relaxation of the lockdown measures, business activity is still dampened, relative to the same period last year.

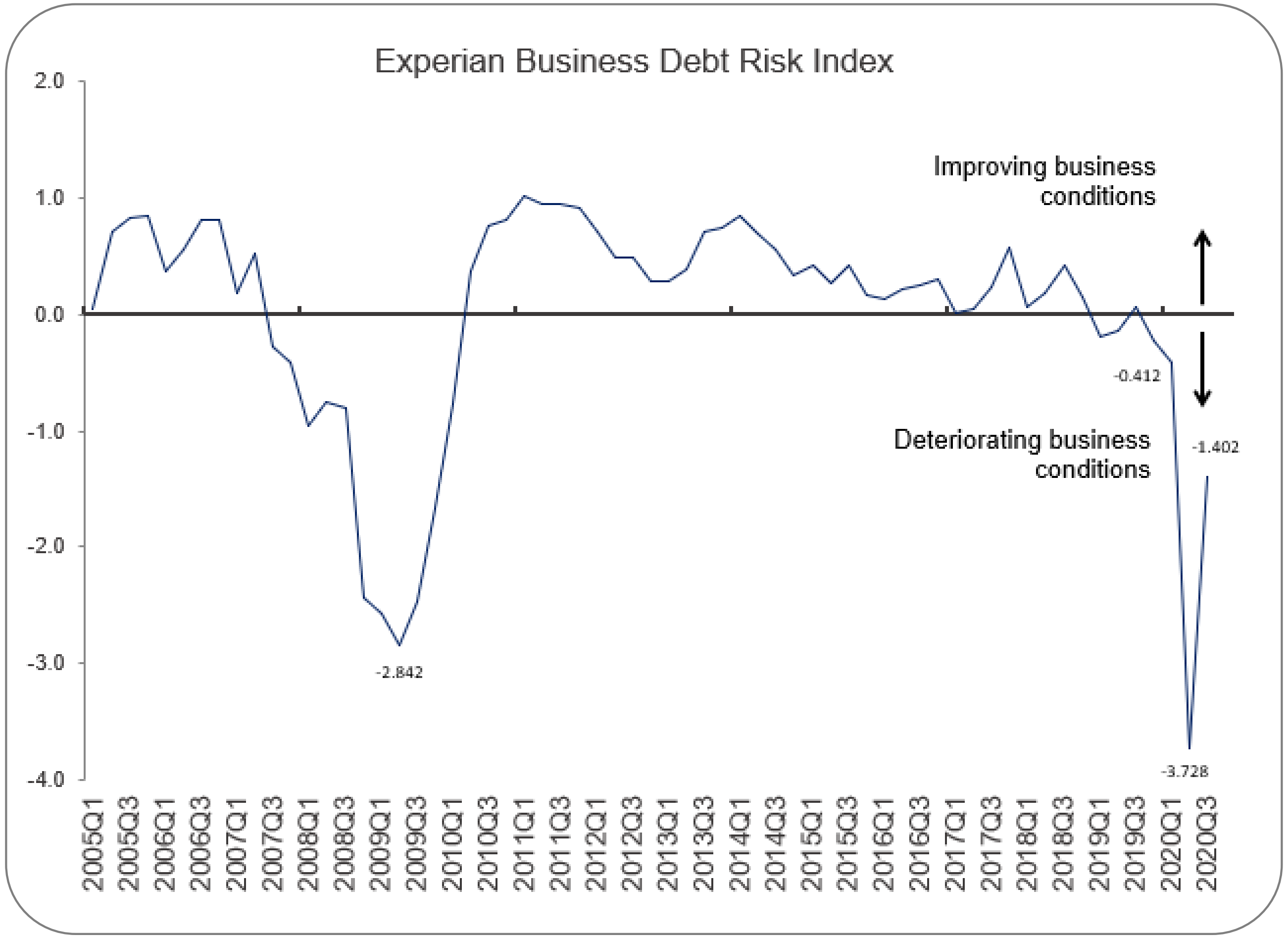


How easy has it been for businesses to meet their debt commitments?

Experian Business Debt Index (BDI) Results and Insights provided by **Econometrix**

Business Debt Index

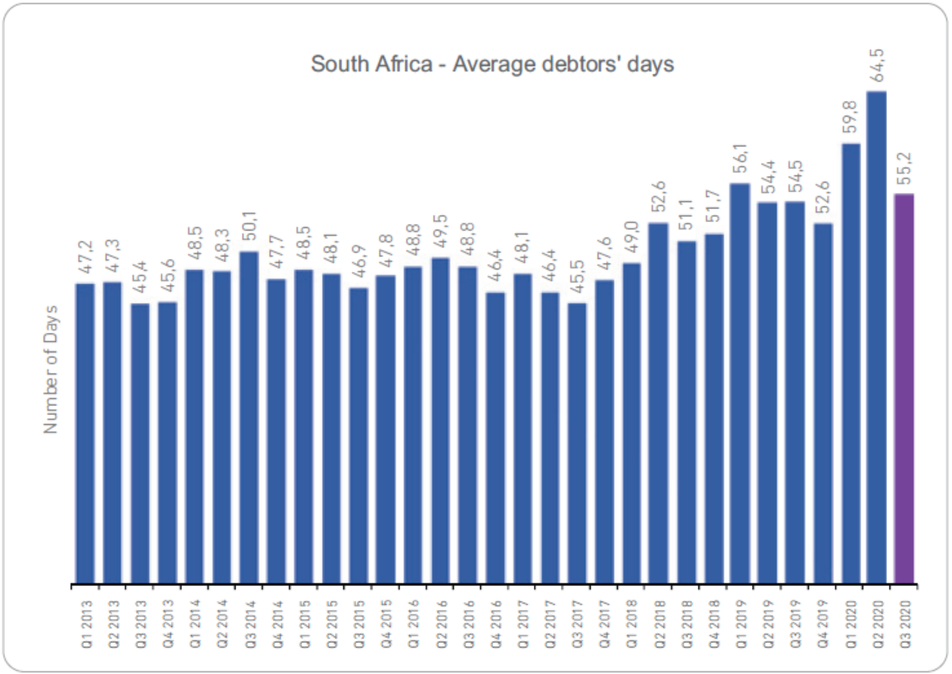
The BDI is improving drastically from the all-time low in Q2 2020. Still, South African business is not in a healthy state.

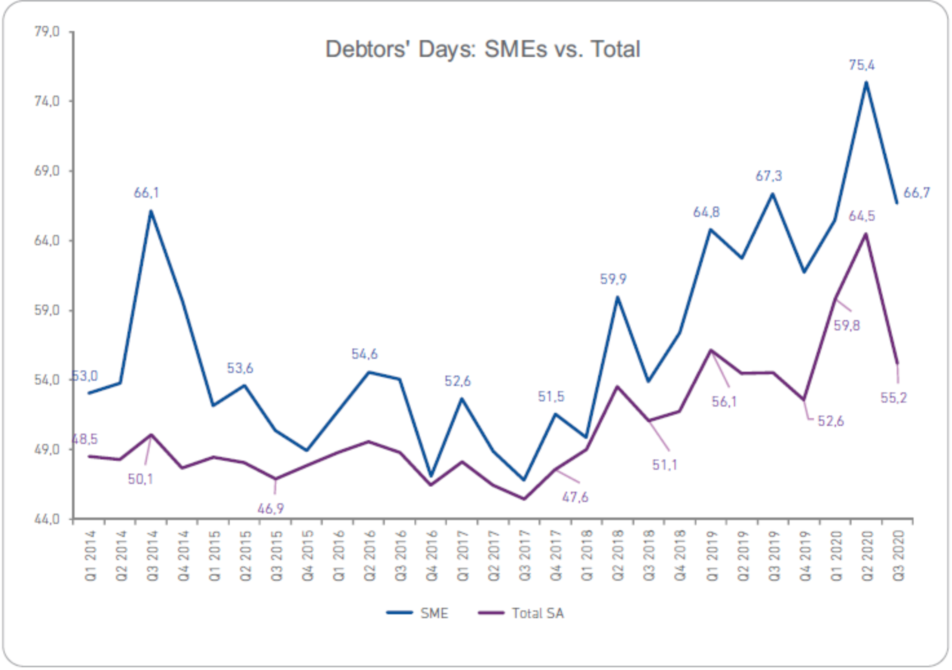


The BDI is a reflection of the overall health of businesses and the position of debt settlement between businesses in the economy. As expected, the BDI improved sharply in Q3, increasing from the historical low of -3.87 in Q2 to -1.402 in Q3 2020. This increase is on the back of the **re-opening of the South African economy**, following the stringent lockdown criteria imposed since the end of March 2020. This resulted in drastic improvement in GDP (in South Africa, but also other major world economies).

Stimulus packages introduced by the South African government also helped to stimulate economic activity.

In spite of the improvement, the **BDI is not yet recovered** to pre-COVID-19 levels as it still remains at a very negative level. This is due to the **9-month pre-lockdown recession** that the country experienced. The BDI is expected to remain negative well into 2021.





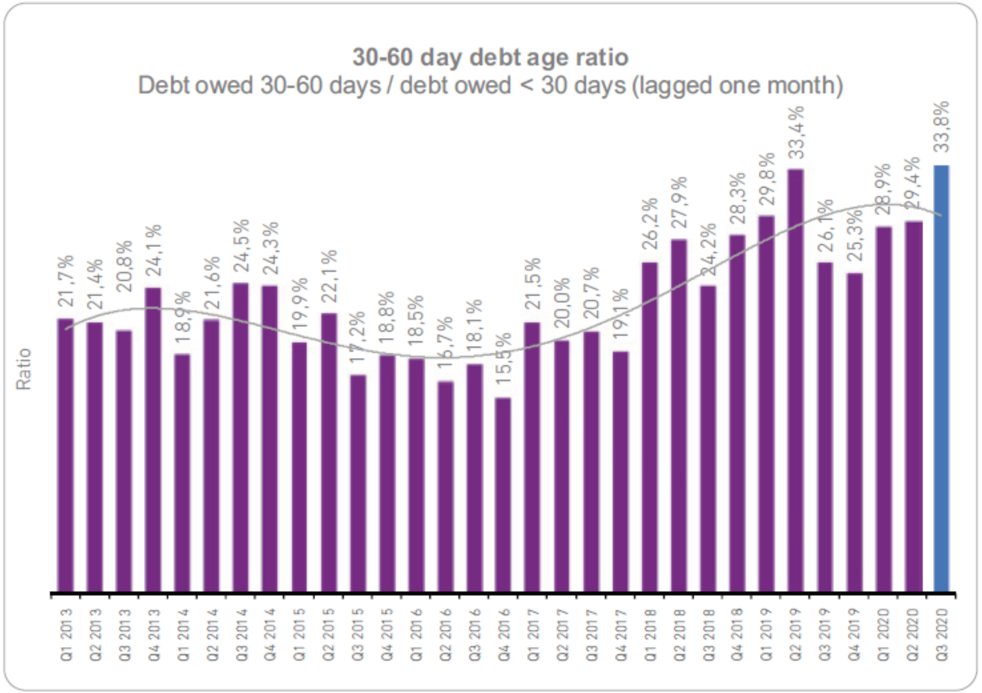
Debtors Age

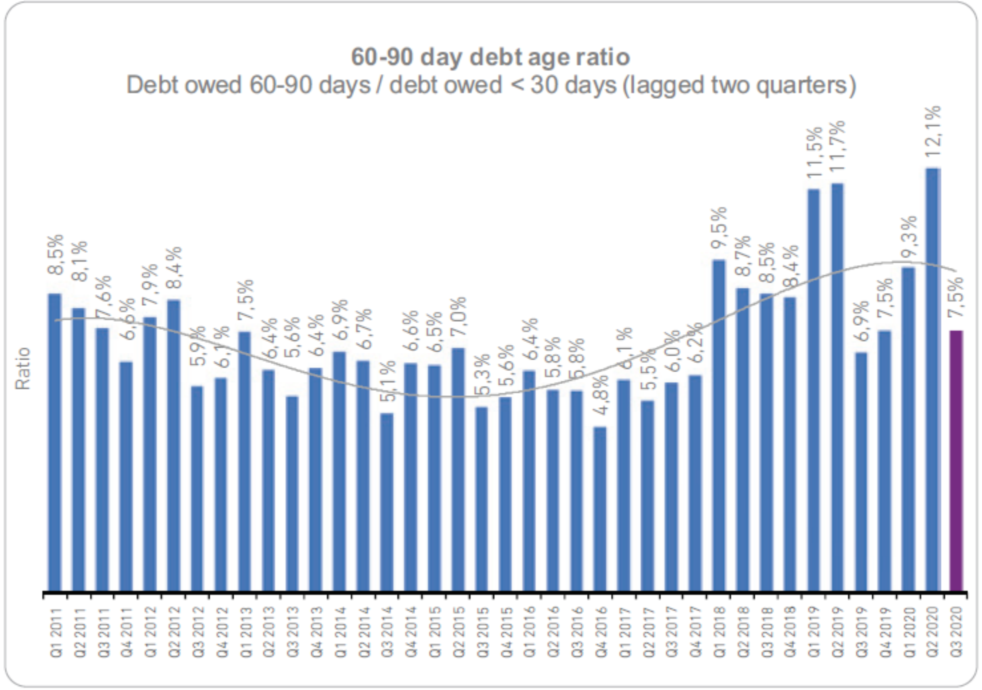
Debtors overdue age has improved for business in general as well as for SMEs in particular.

The average number of days that business debtors are overdue on agreed payment terms dropped in Q3 from the Q2 all-time record high of 64.5 days to 55.2 days.

The **drastic improvement** shows an overall return to, and even an improvement on the overdue days observed pre-COVID-19 lockdown in Q1 of 2020. Note, however, that this by no means signifies a recovered environment for business in which to operate. Rather, it shows that business' ability to honour debt commitments is similar to what we have seen in the 9-month recession period preceding the COVID-19 lockdown, which started at the end of March 2020.

This improvement in average overdue days, however, is **less pronounced for SMEs**, where we saw an improvement from 75.4 days in Q2 of 2020 to 66.7 days in Q3 of 2020. This has still not returned to the levels we saw in Q1 of 2020 or even Q4 of 2019, thus suggesting that SMEs tend to still hold back on paying off debtors even longer than what was observed in Q1 2020.





Debtors Age Ratio

60-90 days debtors ratio has improved significantly, but the 30-60 days ratio has deteriorated.

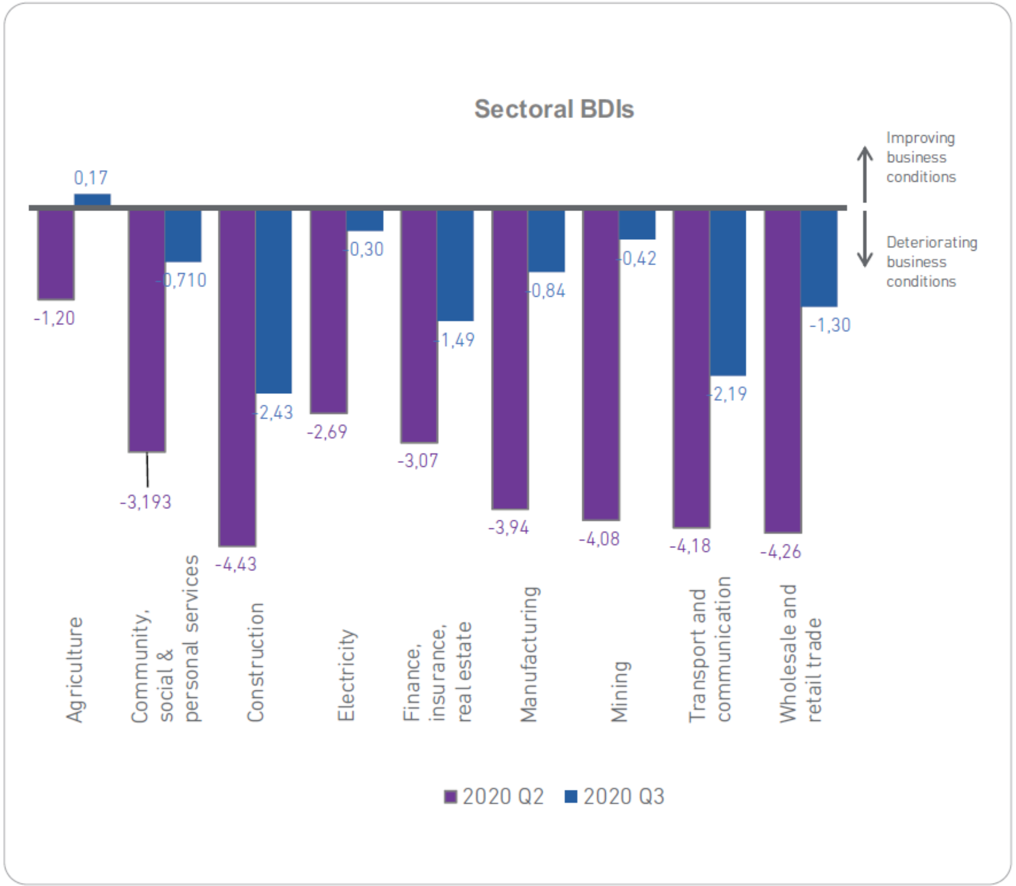
Q3 of 2020 saw the **60-90 days debt age ratio improving** significantly from 12.1% observed in Q2 of 2020 to 7.5% in Q3 of 2020. This is mostly due to mutually extended relief measures from suppliers, which masks the actual reality of cash flow pressure. In addition, the relaxation of the lockdown criteria has had a positive impact on the longer overdue agreed terms payment rate.

As for the **30-60 days ratio, we observed a deterioration** from 29.4% to 33.8%. This is a more realistic view of debtors still facing cash flow pressure and struggling to meet the short-term cash-flow obligations. This increase suggests that although Q3 of 2020 saw businesses improving in the context of longer overdue terms, businesses still experienced increasing pressure to close the gap in the shorter debtor age context.

Overall, the drastic improvement in 60-90 day debt age ratio contributed to the improvement of the BDI.

Impact on Sectoral BDI

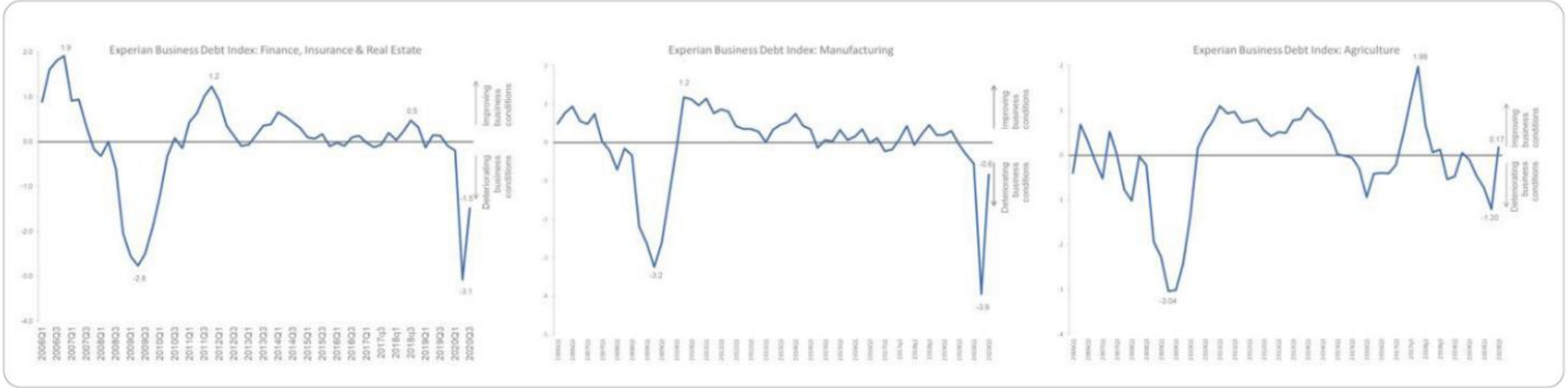
All sectors in the South African Economy have recorded a dramatic improvement in BDI, but this does not yet signal full recovery.



All sectors in the South African economy showed a significant **improvement** in BDI in Q3 of 2020, with some sectors showing improvement to pre-pandemic levels.

One such sector was **Manufacturing**, which showed an improvement from -3.94 in Q2 of 2020 to -0.84 in Q3 of 2020. Conversely, the **Financial** sector, in spite of its relative resilience, has shown a less spectacular improvement in Q3 of 2020, improving from -3.07 to -1.49 only. The latter is related to decreased credit extensions in Q3 of 2020, in both Business and Consumer credit.

Agriculture, the only sector in positive BDI territory, is benefiting from three consecutive quarters of double-digit growth in agricultural output, following excellent harvests as a result of good rainfall in the 2019/2020 summer rainfall season.



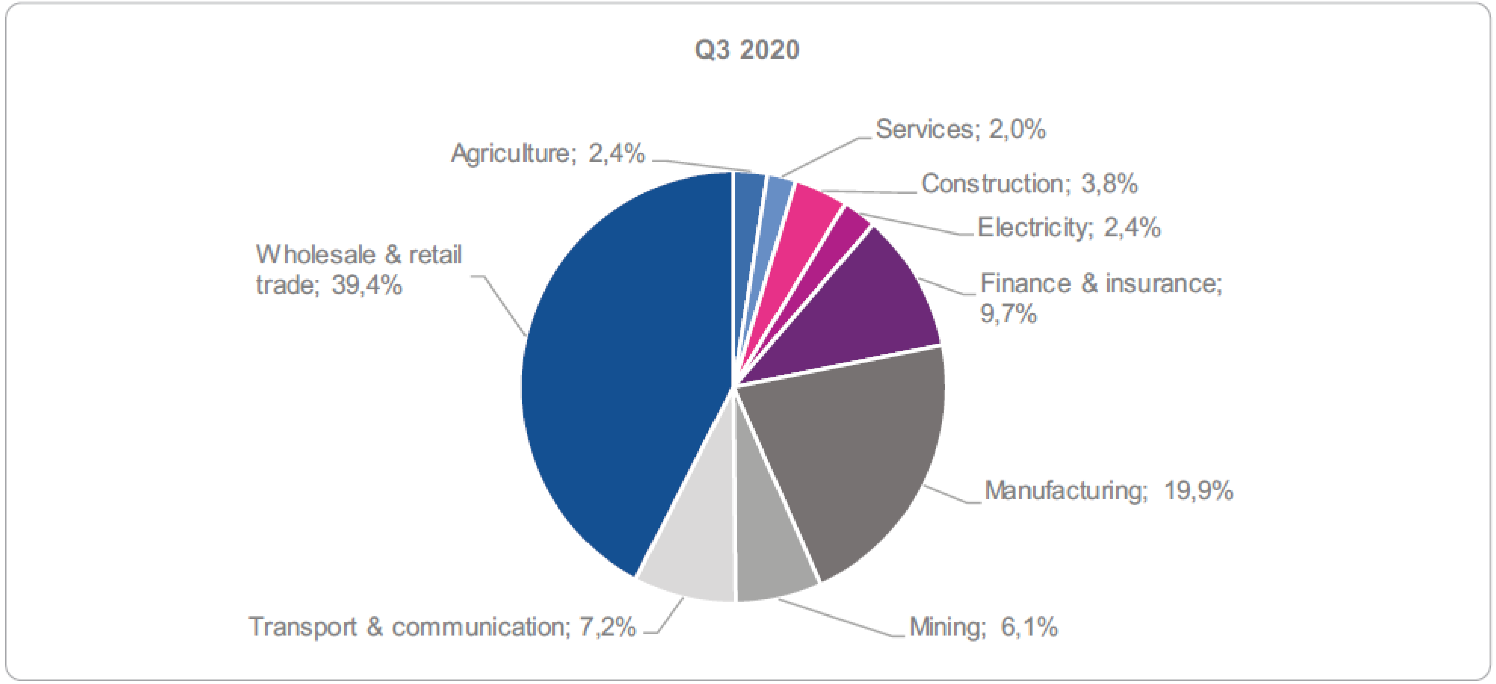
Sectoral Credit Risk Benchmark

All sectors in the South African Economy has recorded a dramatic improvement in BDI, but this does not yet signal full recovery.

The biggest share of business debt is owed by the trade and motor vehicle repair sector.

On the back of the low base observed in Q2 of 2020, the latest Business Debt overview identifies all other industries except Agriculture, to be in **Neutral territory** in terms of credit risk benchmarking. This benchmark is derived from a combination of BDI, average debtors days and the number of judgments and liquidations in a sector.

Agriculture is deemed to be a Good credit risk, as a result of good summer crops having been harvested and a promising outlook for the winter crops.



INDUSTRY	BDI Movement	30-60 Debt Age Ratio	Debtors Days	GDP Movement	Judg & Liquid	Credit Risk Benchmark
Agriculture	↑	↓	↓	↑	↑	GOOD
Services	↑	↓	↓	↑	↑	Neutral
Construction	↑	↓	↓	↑	↑	Neutral
Electricity	↑	↓	↓	↑	↑	Neutral
Finance & insurance	↑	↓	↓	↑	↑	Neutral
Manufacturing	↑	↓	↓	↑	↑	Neutral
Mining	↑	↓	↓	↑	↑	Neutral
Transport & communication	↑	↑	↑	↑	↑	Neutral
Wholesale & retail trade	↑	↓	↓	↑	↑	Neutral

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Experian Africa

Specialises in SME market insight and best practice

Highlights from *Enterprise Agility and Smart Routes to Digital Transformation* - a commissioned study conducted by Forrester Consulting on behalf of Experian across EMEA.

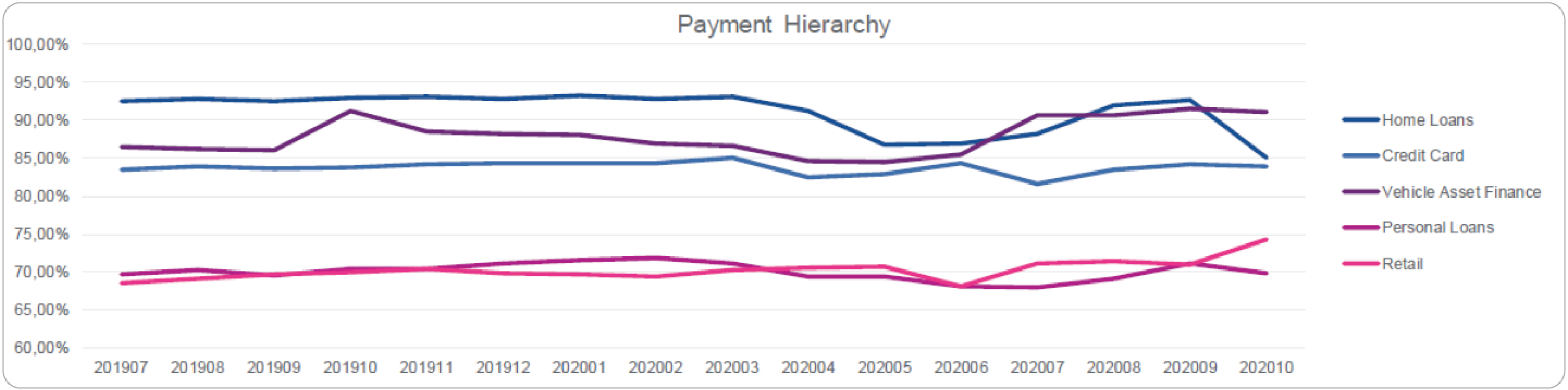
- 80% of firms expect to be trading again at pre-COVID-19 levels within 18 months.
- *80% of firms have increased budgets for advanced analytics and customer insight.*
- 60% of firms have increased their budget for fraud.
- *43% of firms said they are struggling to get a complete picture of indebtedness or identify "at risk clients".*
- 74% of firms are making improved customer experience a priority (digital war across life cycle).
- 26% of firms say that lack of automation in their tools (life cycle) is the biggest barrier to commercial success.
- 35% of South African firms say they do not have a collections system to cater for the pandemic (Major collections focus and change of operational landscape).

How has the COVID-19 crisis impacted consumer credit profiles?

All Credit-Active Consumers – Payment Hierarchy

Do consumers prioritise paying certain trades before others?

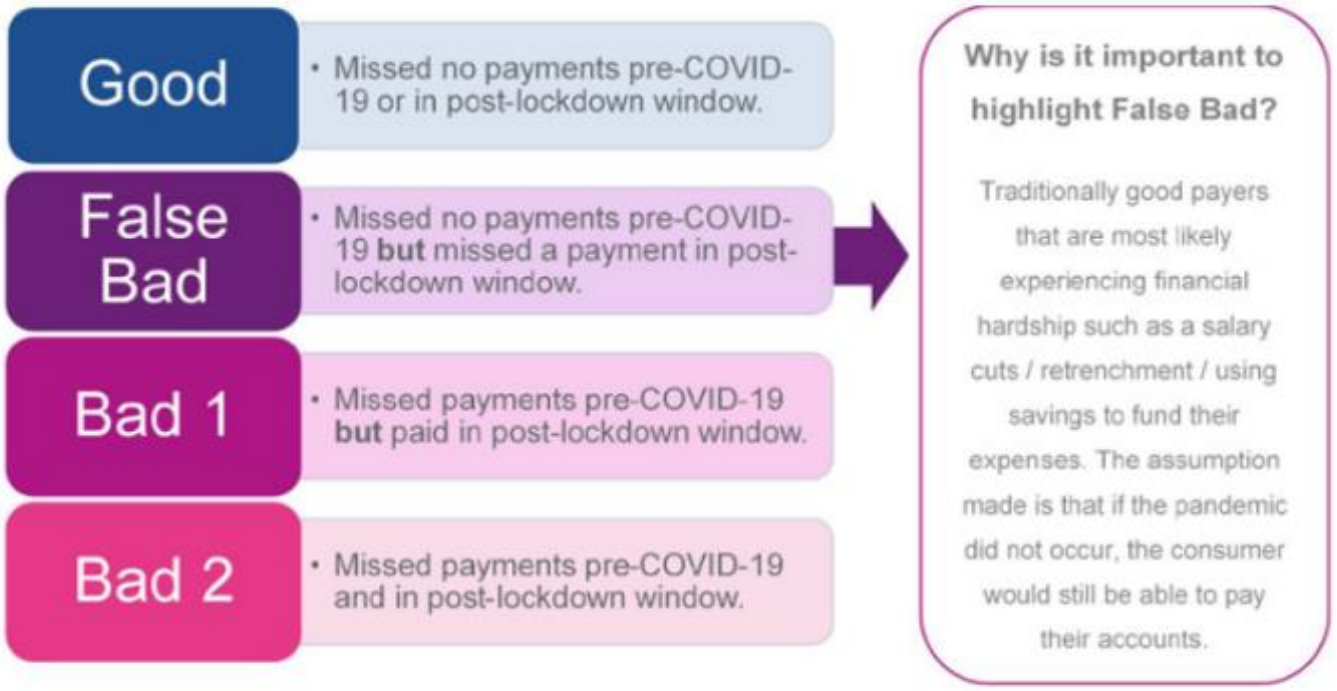
Prior to the COVID-19 pandemic, consumers prioritised their secured payments over unsecured payments; however, a change is evident after April 2020, where consumers start missing payments on their secured products and start to repay their unsecured products. This could be a factor of consumers being able to repay smaller credit commitments and not larger commitments such as their Home Loans or Vehicle Asset Finance products. Consumers start to prioritise secured lending again after July 2020. Payment Holidays granted to consumers have also influenced these trends.



All Credit-Active Consumers – COVID-19 Indicators

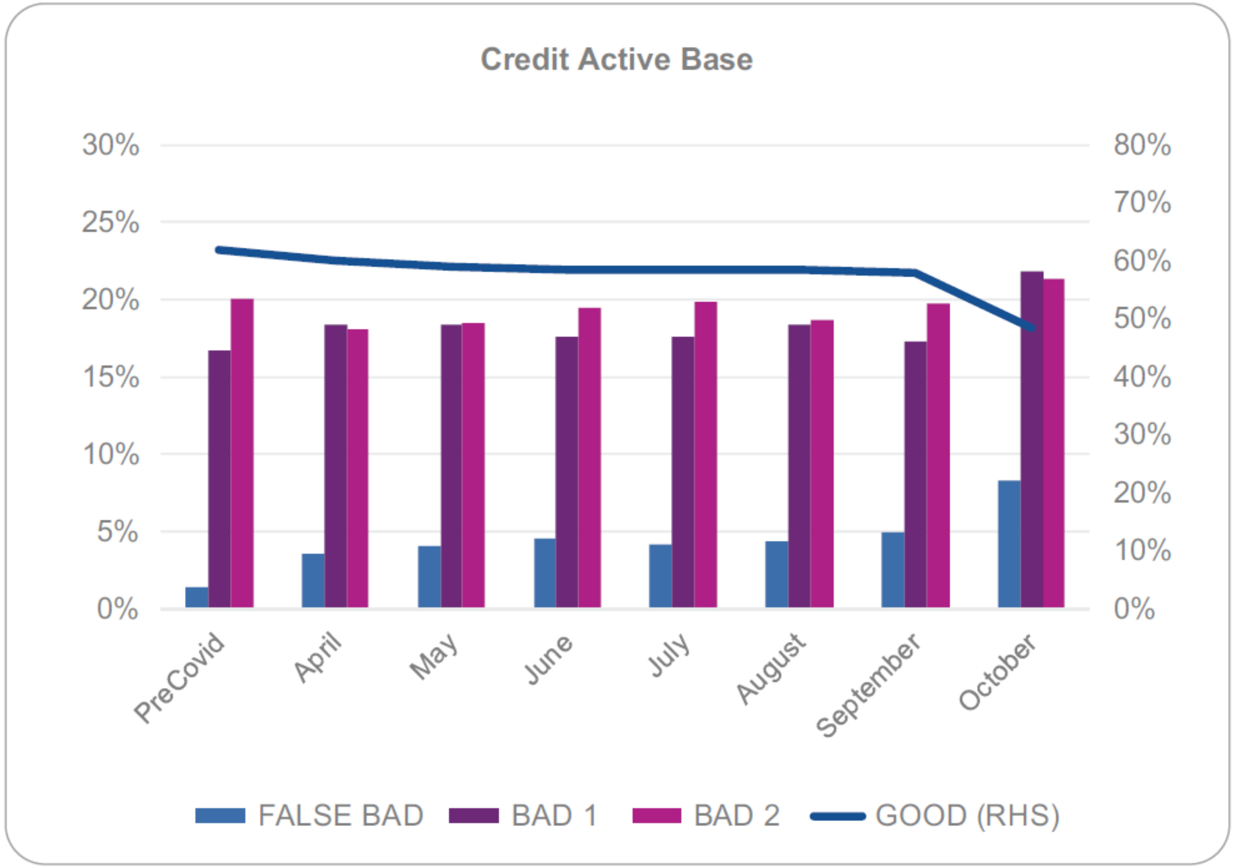
We have created COVID-19 Indicators as a unique tool to segment consumers into four categories to measure the risk of consumers post lockdown.

- They were designed to measure the repayment behaviour of South African consumers with active credit products such as Home Loans, Personal Loans, Credit Cards and Retail Loan Accounts.
- Looking at consumers' payment behaviour on individual accounts, we can create segments based on their pre- and post-lockdown observed risk.
- These risk definitions can be assigned on an account level as well as at a consumer level using an instalment-weighted approach.
- The indicators are calculated for each month after the start of lockdown (end of March 2020).



COVID-19 Indicators

Comparing the COVID-19 Indicators distribution across time for the credit-active base.



- Pre-COVID-19, the **False Bad** percentage was **less than 1.5%** on the credit-active base.
- The False Bads continued to grow over time, whereas Bad 1 and Bad 2 stayed stable.
- In **October 2020, 8% of the population was classified as False Bad.** This is a significant increase compared to September 2020 as well as Pre-COVID-19.
- During 2020, there were multiple levels of lockdown and the economy opened slowly towards year-end. Credit activity increased as stores opened, and consumers were able to buy non-essential goods and move more freely within as well as in/out of the country. This allowed many more businesses to open their doors and trade again. Unfortunately, from the False Bad and Bad 2 population, it is evident that many consumers are still facing financial hardship and most likely lost their job or still have a lower income compared to Pre-COVID-19 times.

All Credit-Active Consumers – Payment Holiday

With more consumers moving into a distressed financial state, more payment relief measures were taken up in April-June 2020. These have, for the most part, been decreasing since July.

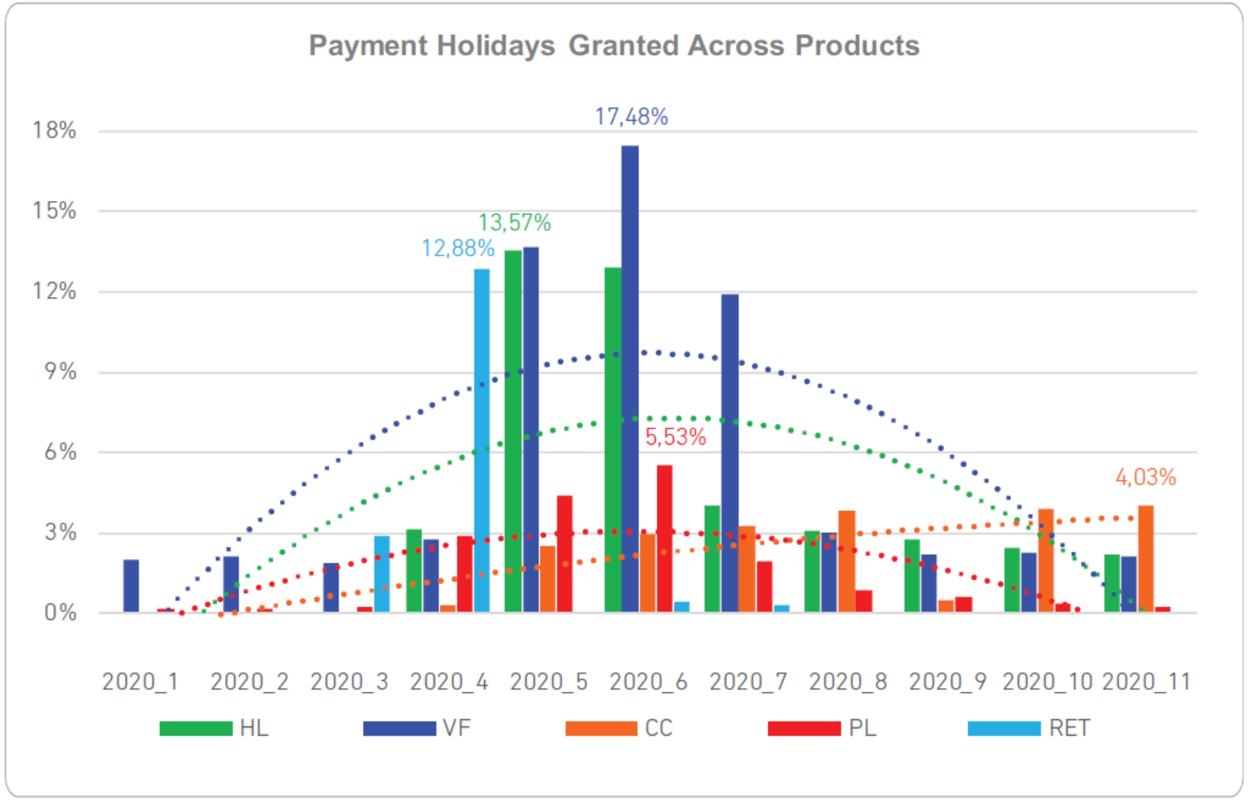
Credit service providers assisted consumers who were negatively impacted by the pandemic by offering:

- Term extensions – Extending the remaining term on fixed-term agreements in order to reduce the monthly instalment to cope with reduced income and/or increased expenditure due to COVID-19.
- Deferred payments/payment holidays – Deferring repayment of debt for a period of 1 or more months in order to provide immediate relief to consumers dealing with retrenchments, reduced income and/or increased expenditure due to COVID-19.

Limitations:

- Payment relief measures are normally extended to lower-risk consumers and might not provide relief for all consumers who are willing to take it up.

For the majority of the products, payment holidays were extended predominantly during April, May and June. Most of these products showed a decline in the incidence of payment holiday extension from July 2020 onwards.



Financial Affluence Segmentation (FAS)

The Experian FAS model is segmented into six primary groups described below.

FAS Group 1: Luxury Living - Affluent individuals representing the upper crust of South African society with the financial freedom to afford expensive homes and cars.

FAS Group 2: Aspirational Achievers - Young and middle-aged professionals with the resources to afford a high level of living while furthering their careers, buying property and establishing families.

FAS Group 3: Stable Spenders - Young adults that rely on financial products to assist in making ends meet or to afford specific necessities such as clothing and school fees, or seasonal luxuries.

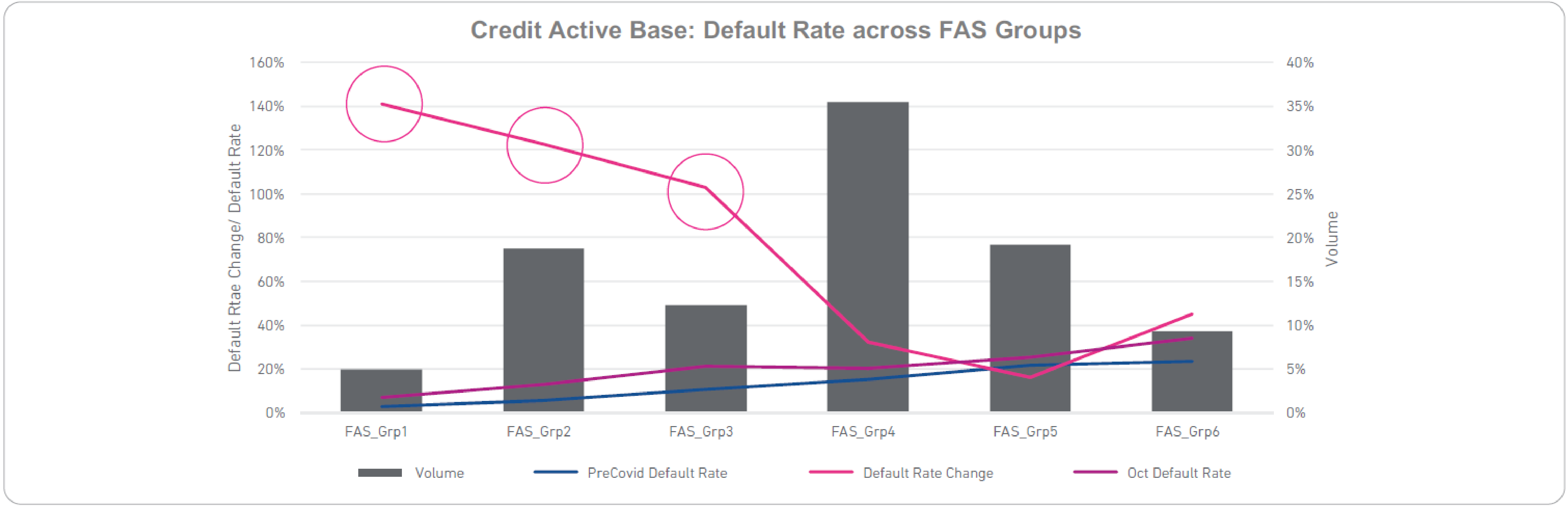
FAS Group 4: Money-Conscious Majority - Older citizens that are conscious of where and how they spend their money; often seeking out financial products to cover basic needs or for unforeseen expenses.

FAS Group 5: Laboured Living - Financially limited individuals as salaries are below national tax thresholds, they spend their money on basic living necessities such as food and shelter.

FAS Group 6: Yearning Youth - Very young citizens that are new to the workforce; this mix of labourers and possibly working students earn low salaries and are limited to spending on non-essential goods.

FAS Group

Default Rate on Credit Active Base across FAS Groups



The default rate is calculated using a 3+ definition across all products per consumer. FAS Group 1, 2 and 3 have the highest change in default rate when comparing pre-COVID-19 with October 2020 default rates. The default rate of FAS Group 1 could be attributed to the higher proportionate exposure to secured lending products as highlighted in Experian's Consumer Default Index (CDI). There was also a significant increase in FAS Group 2 and 3 default rates, which was expected as consumers across the income spectrum are experiencing financial strain. The volume of payment holidays extended across different products decreased in October and could also contribute to the high volume of consumers defaulting as some consumers may still experience financial difficulty. With the re-instated lockdown and alcohol ban in place, it is expected that default rates across all FAS groups will remain high and might increase in the following months.

Payment Quadrants

These quadrants illustrate how consumers with two or more product repay the products compared to how they repay other active credit products.

September 2020

		Repay Banking Products	
		No	Yes
Repay Retail	No	6.23%	11.16%
	Yes	20.85%	61.75%

October 2020

		Repay Banking Products	
		No	Yes
Repay Retail	No	8.80%	19.57%
	Yes	19.27%	52.36%

The payment quadrants illustrate how consumers repay their retail loans versus banking loans. The first grid shows the results of repayment as at the end of September 2020, whereas the second grid shows the results as at the end of October 2020. Amongst consumers with retail loans, a low percentage pay both retail and banking products and decreased to 52.36% in October 2020. A higher percentage of consumers do not pay either their retail loans or banking products in October 2020 (8.80%) as well as not paying their retail loans but paying their banking loans (19.57%). This is evident that **collection processes should continue to be a key focus** to avoid having consumers not repaying their retail accounts, as there is still income to repay other credit such as any banking product.

Thank you.

Questions?

The third quarter of 2020 has seen the South African economy gradually improving, following the steady re-opening relaxation of the lockdown criteria. As such, the BDI has **improved markedly in Q3**. However, the BDI **has not yet recovered** to pre-COVID-19 levels, and we don't expect it to do so in the short-term, as South African businesses now need to weather the re-instated level 3 lockdown measures while still still suffering from the impact of the **9-month recession preceding the lockdown**.

Analysis of COVID-19 metrics derived and monitored by Experian suggest that **consumers remained under severe stress** for the third quarter of 2020, with strain particularly on consumers that are dependent on credit for day-to-day survival.

Recovery to pre-COVID-19 status is not expected to be seen in 2021. With the re-instated lockdown rules and alcohol ban, businesses and consumers are still **expected to be under significant financial strain** for the remainder of the year.

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