

**South African Consumer Conference**

**24 June 2009**

**Constraints facing the South African  
consumer in the recovery phase**

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- Current realities
- A risk of a second round of distress
- Green shoots
- What should happen next?

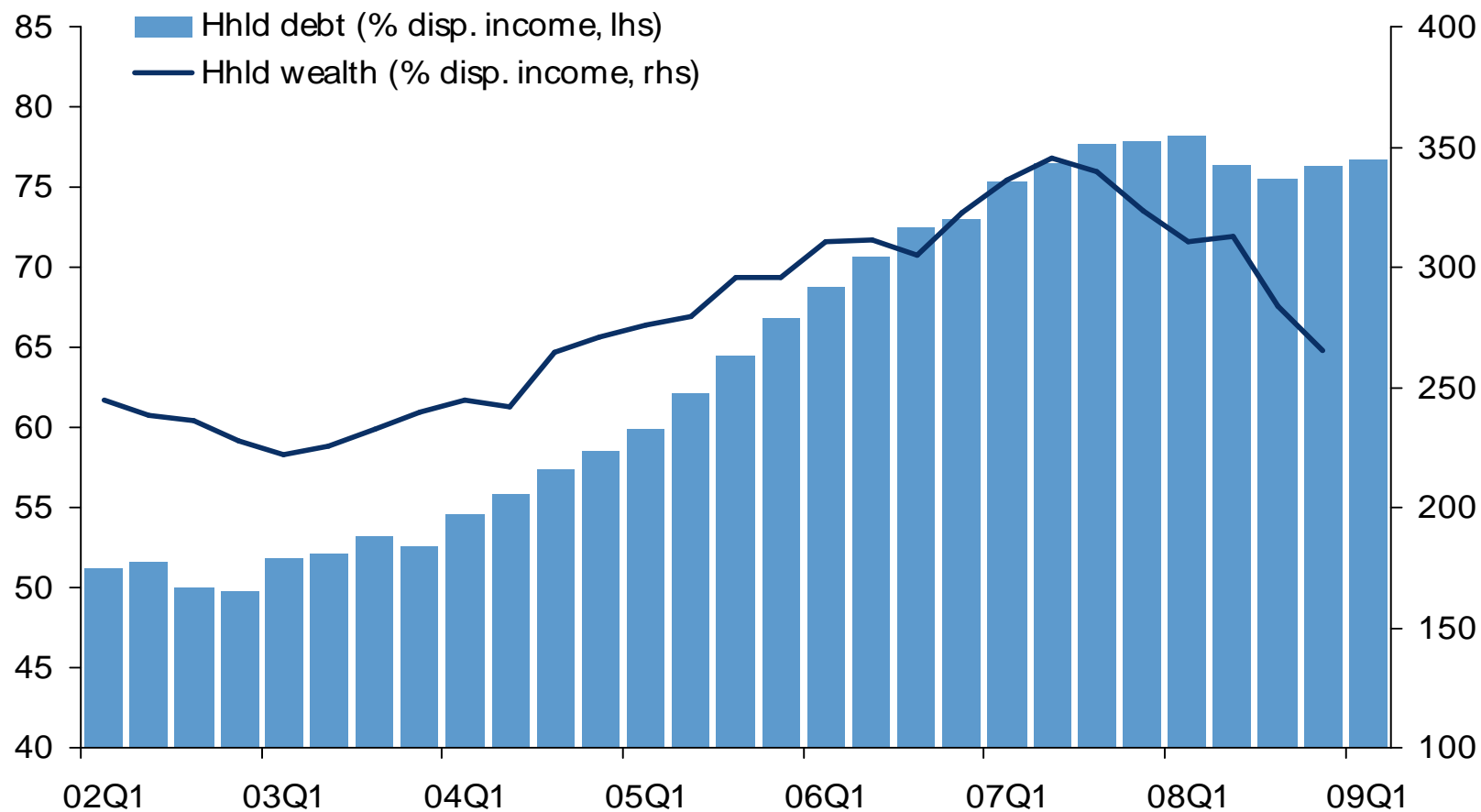
# QUESTIONS ASKED OF THE BANKS

- How does this cycle compare to previous cycles?
- When will banks start lending again?
- When do we see the turn in the cycle?

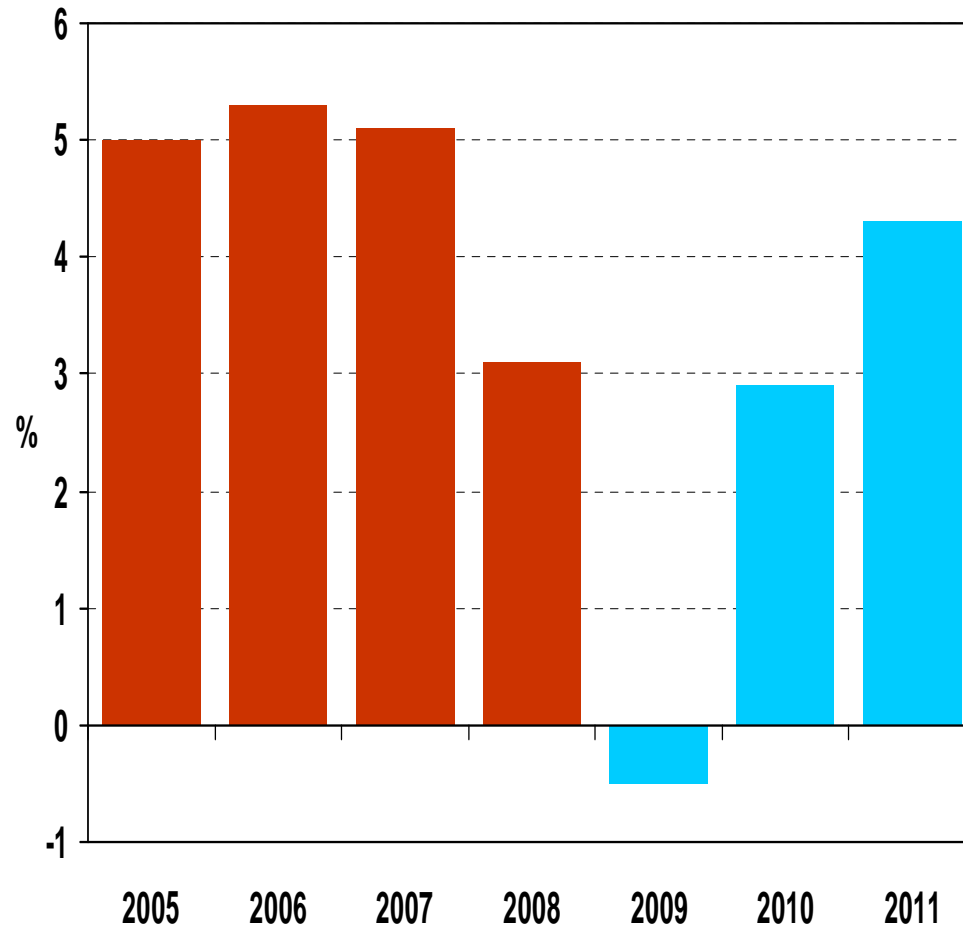
**It is important to look at certain realities**

# Falling household wealth and high debt levels present a challenge for households...

Declining household wealth and high debt levels are not conducive to a near term recovery in consumption spending

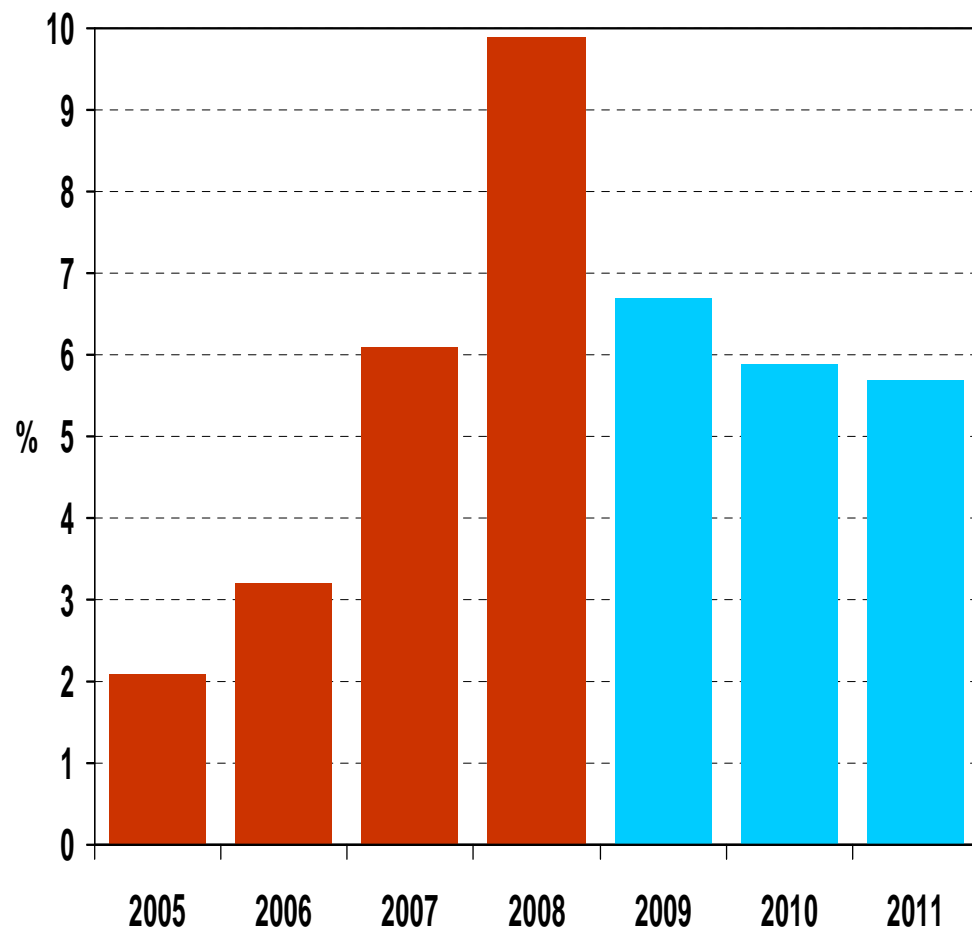


# Real economic growth



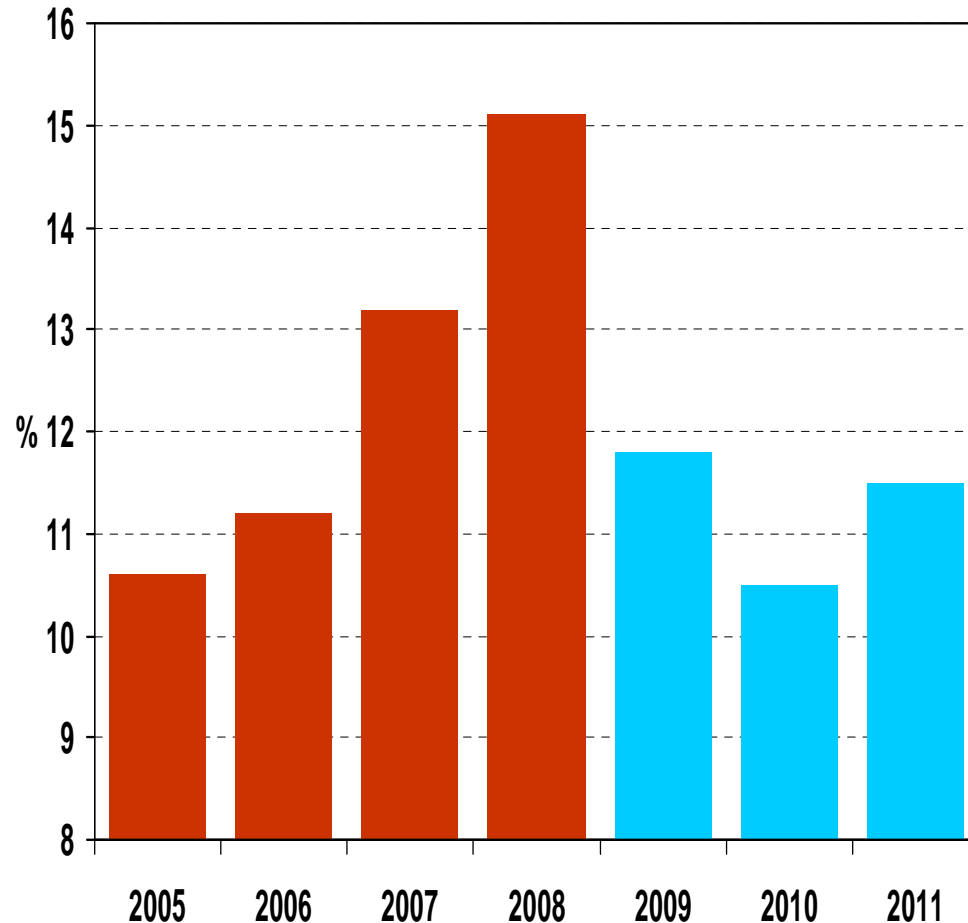
- Economy in recession in 2009 (impact of global trends and domestic demand).
- Bottoming out in second half of 2008.
- Conditions improve in late 2009 on the back of a recovery in the world economy.
- Recovery from 2010, but economic growth not expected to reach the level of 6%.

# Consumer price inflation



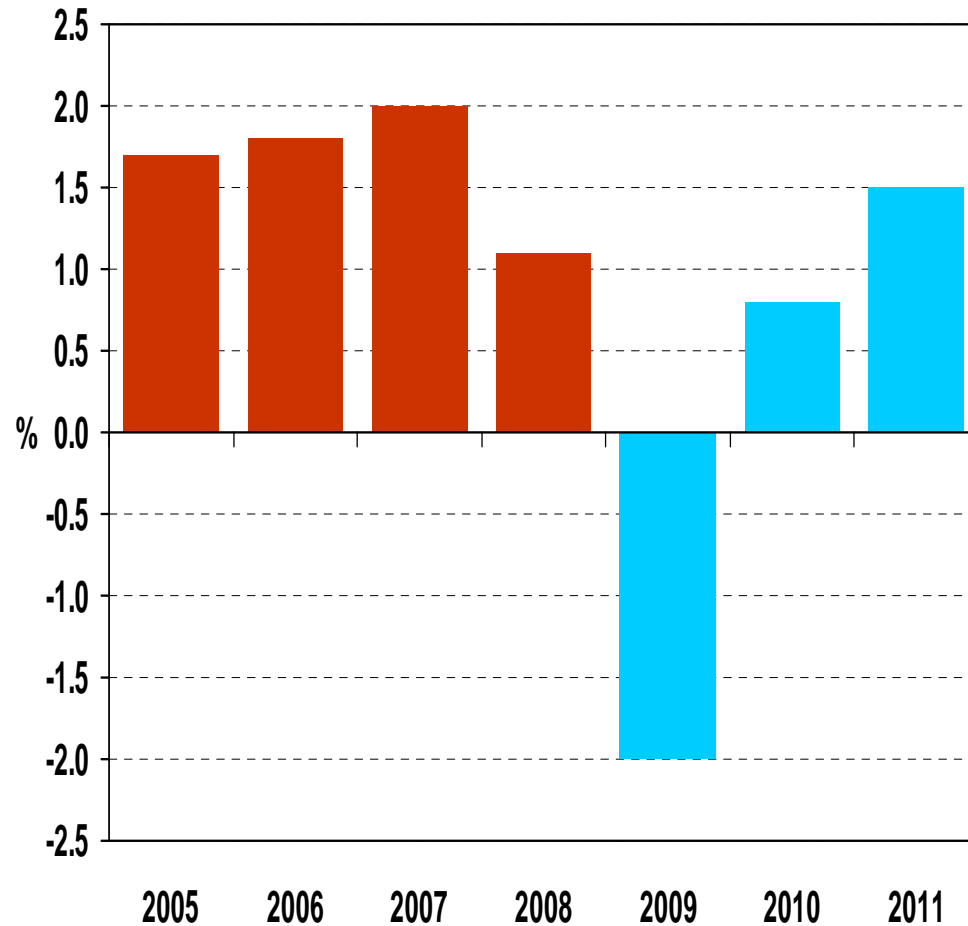
- Assumption: Inflation target to remain in place with target range 3%-6%.
- CPI inflation on a declining trend since late 2009 on the back of lower international oil prices and somewhat lower food price inflation.
- Inflation factors such as oil prices and rand exchange rate movements, impacting domestic fuel prices, as well as food price trends will determine inflation trends.
- Inflation declining to just below 6%, with a depreciating rand and rising oil price causing upward pressure.
- Eskom potential tariff increase will cause some upward pressure on inflation.

# Prime interest rate



- In view of inflation targeting, interest rates will be the policy instrument to contain inflation.
- Lending rates to decline to 2006 levels on the back of lower inflation and a poorly performing economy.
- With upward pressure on inflation as a result of exchange rate and oil price movements, interest rates are hiked by 1% in the second half of 2010.
- Rates remain unchanged in 2011 with inflation at just under 6%.
- Policy changes at the SARB. Will Tito remain after his term ends in October 2009.

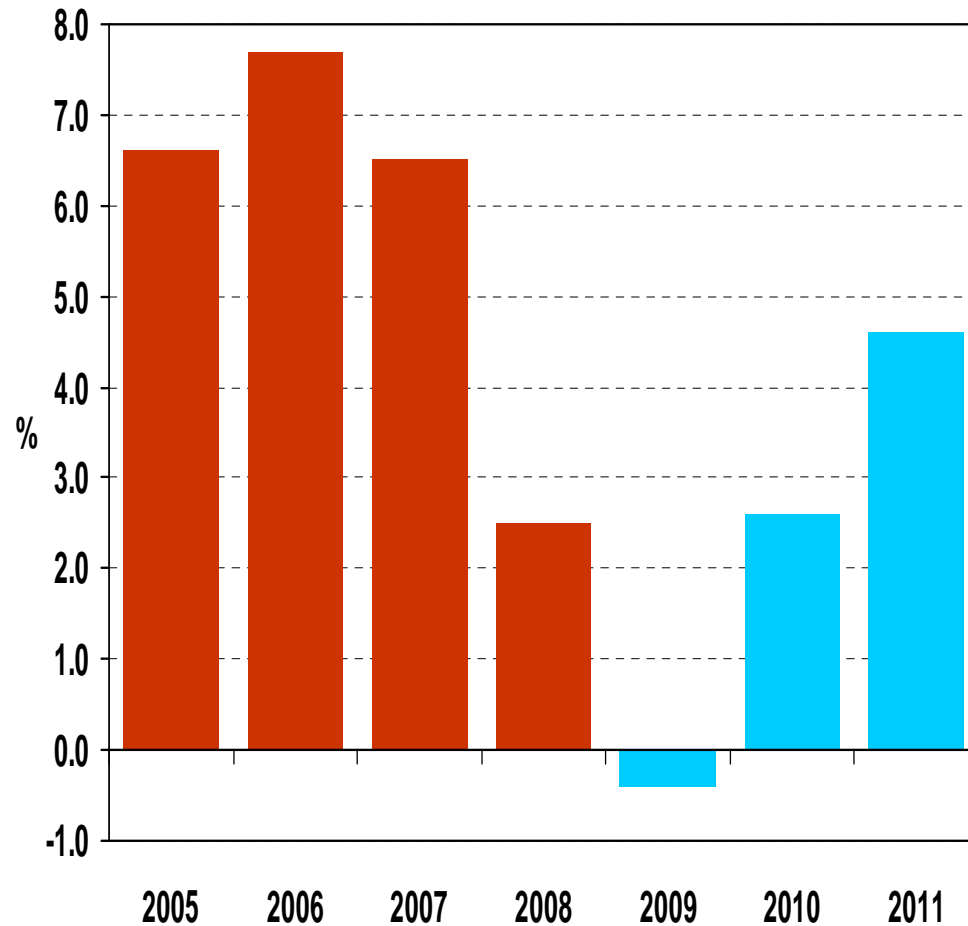
# Employment growth



- Employment under pressure as a result of declining economic activity in most sectors of the economy.
- In the first quarter of 2009, employment dropped by 208 000, or 1,5%, compared with the fourth quarter of 2008.
- A gradual recovery is expected from 2010 on the back of improving economic activity and positive real GDP growth.

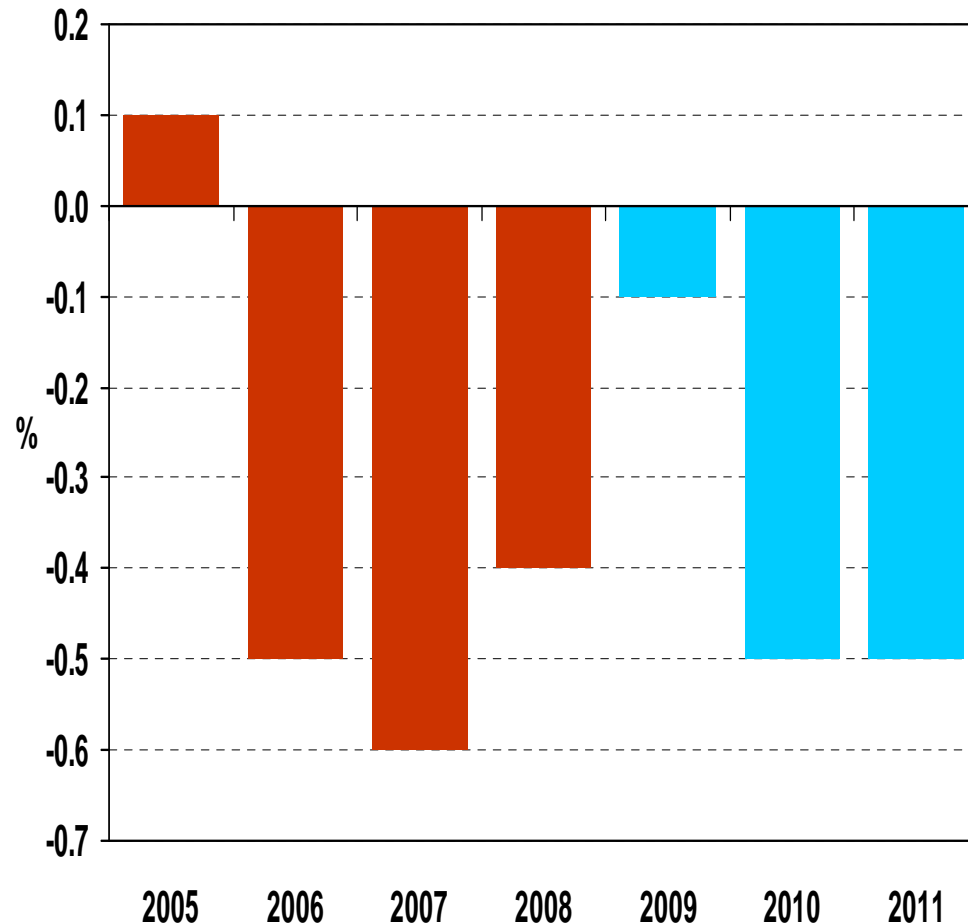


# Real household disposable income growth



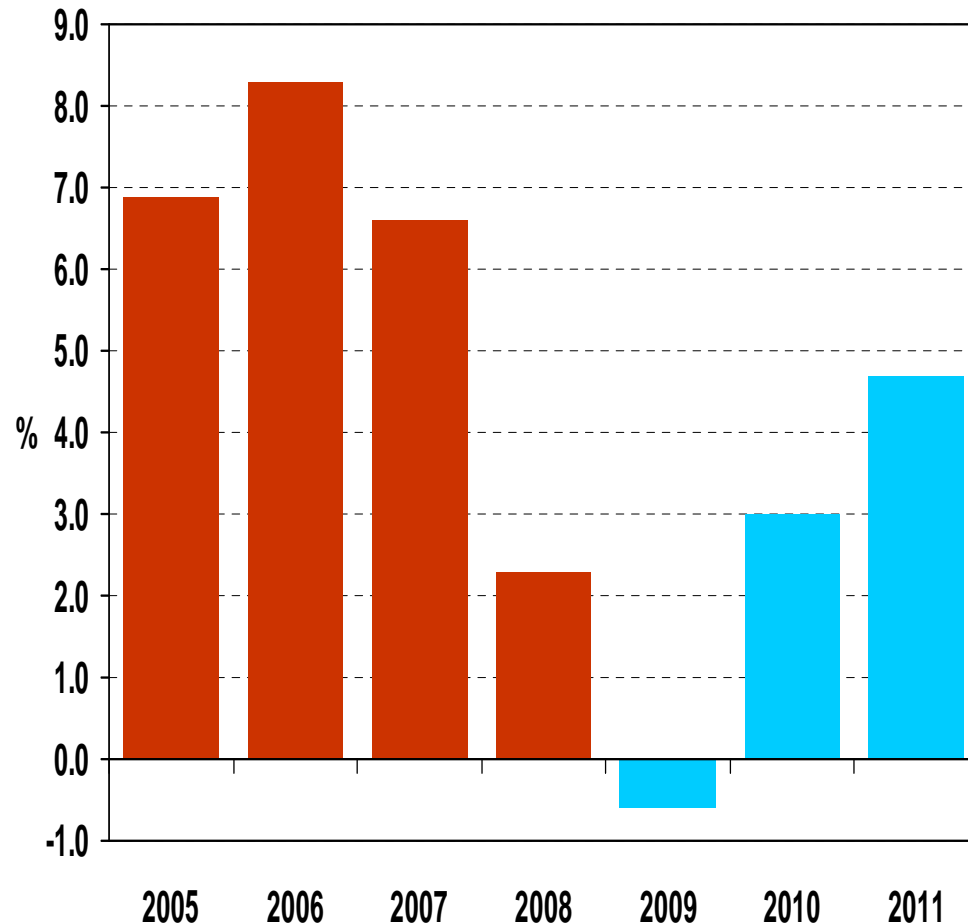
- Real household disposable income dropped by 1,9% quarter-on-quarter in the fourth quarter of 2009.
- Economic conditions and employment trends set to put further pressure on income growth in 2009.
- Low growth in 2010 on the back of a gradually recovering economy and improving employment.

# Net household saving to disposable income



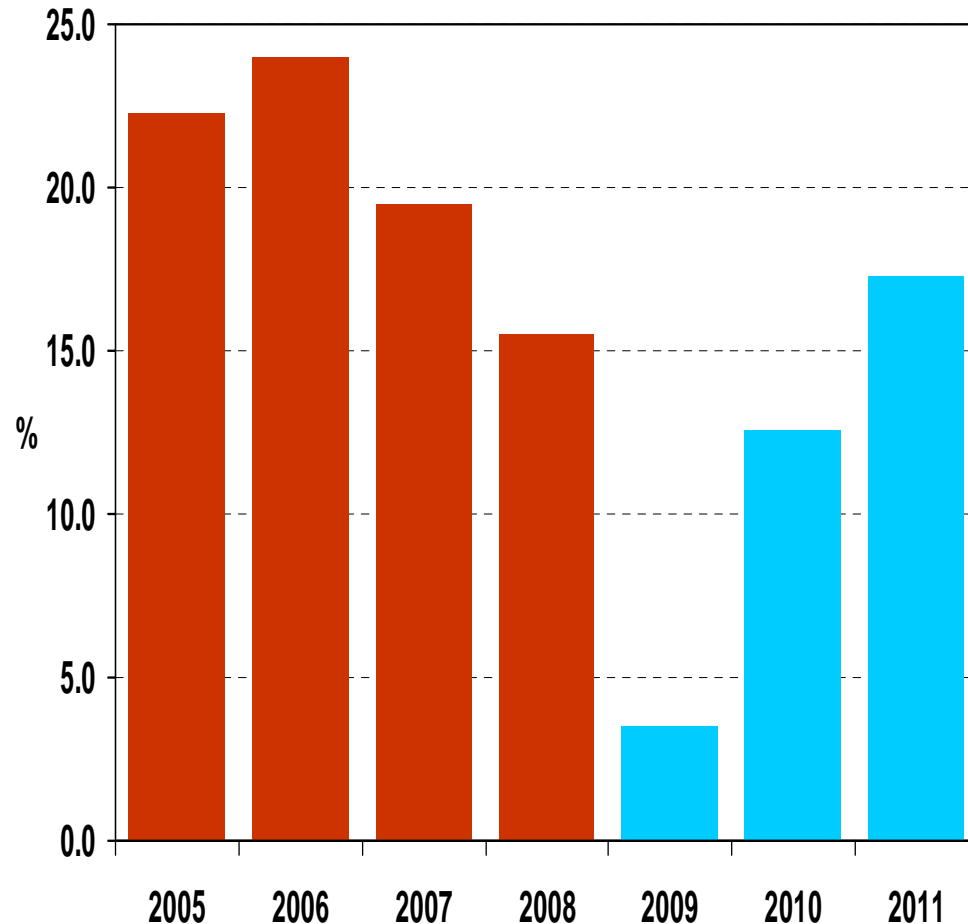
- Negative household saving (net of depreciation on assets) as a percentage of household disposable income an indication of a household sector not saving.
- Levels of indebtedness and sharply rising living costs caused a depletion of savings in an attempt to keep up living standards.
- Other factors impacting household savings: low real deposit rates, offering no real incentive to save; low level of interest income exemption from tax.

# Growth in real household consumption expenditure



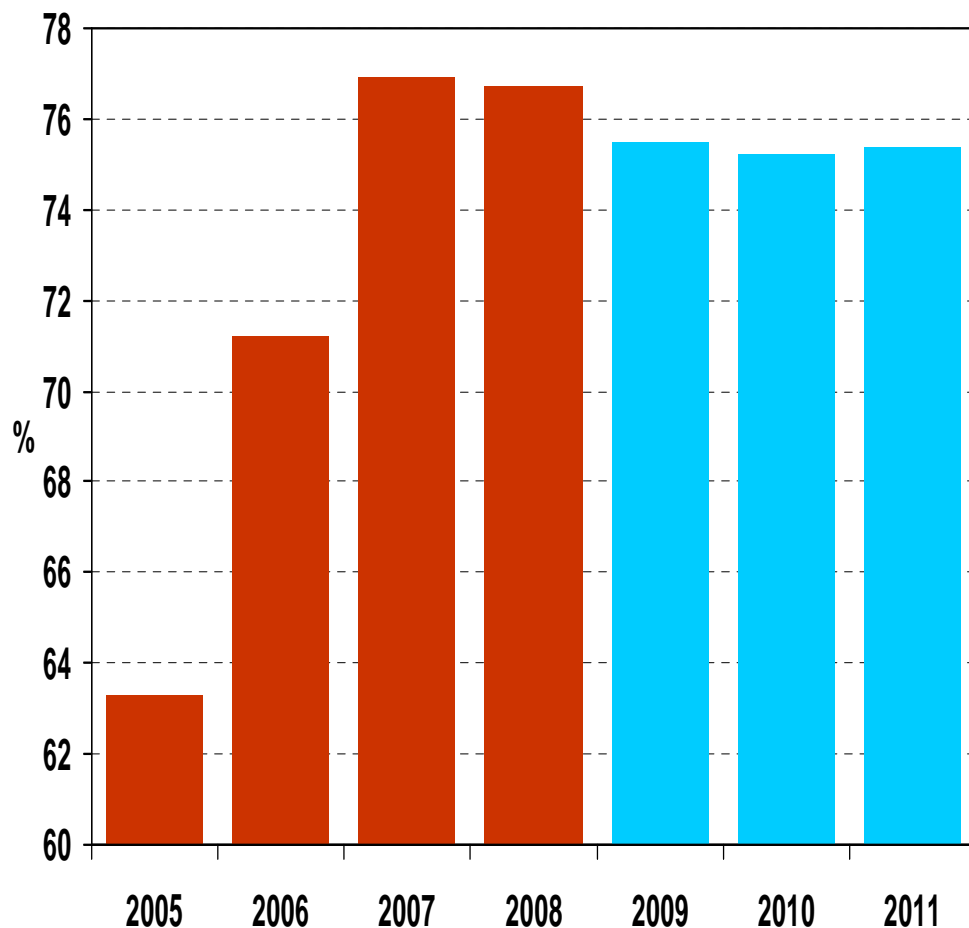
- Growth in real household consumption expenditure slowed down on the back of rising inflation and interest rates in 2006-2008, which eroded consumers' spending power.
- The ratio of household wealth (all fixed and financial assets) to disposable income dropped from 346% in the 2<sup>nd</sup> quarter of 2007 to 265% in the 4<sup>th</sup> quarter of 2008, mainly as a result of slowing property prices and declining share prices.
- This change in households' wealth negatively affected their consumption.
- Growth in consumption is expected to improve along with better employment conditions and growing household income.

# Growth in household credit



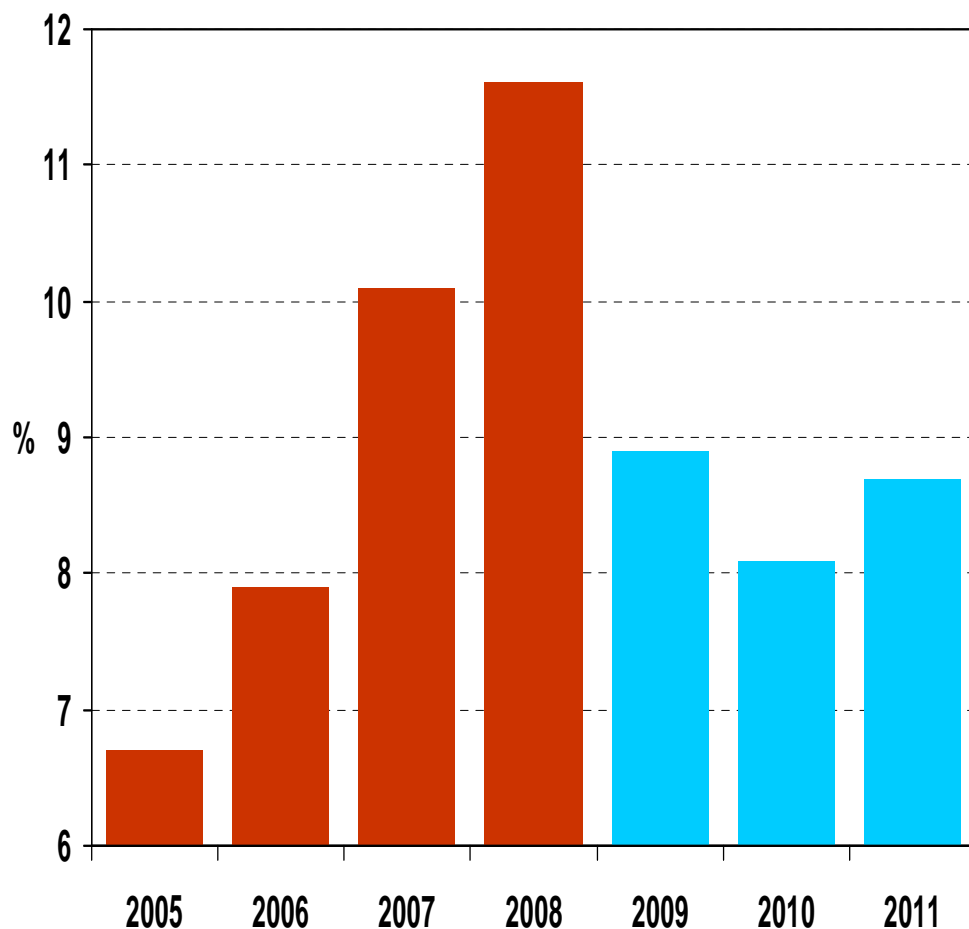
- Growth in credit extension tapered off on the back of rising interest rates in 2006-2008.
- In view of a slowing economy, declining employment and tight lending criteria, growth in household credit extension is forecasts to slow down into single digits by the end of 2009.
- Based on a better economic performance from late 2009, together with the lagged effect of lower interest rates, household credit growth is expected to improve from early 2010.

# Household debt to disposable income



- The ratio of household debt to disposable income increased sharply to a level of 78,2% in the 1<sup>st</sup> quarter of 2008, largely as a result of markedly lower interest rates up to 2006, a strongly growing economy and property market, leading to significant growth mortgage finance.
- Household indebtedness is forecast to remain relatively high compared with previous years on the back of an increasing number of households obtaining access to finance.
- Household debt ratio expected to increase gradually on the back of improving economic and household income conditions.

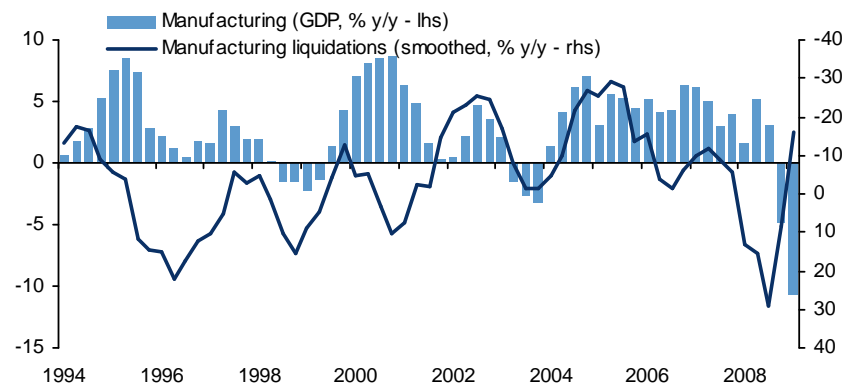
# Household debt servicing cost to disposable income



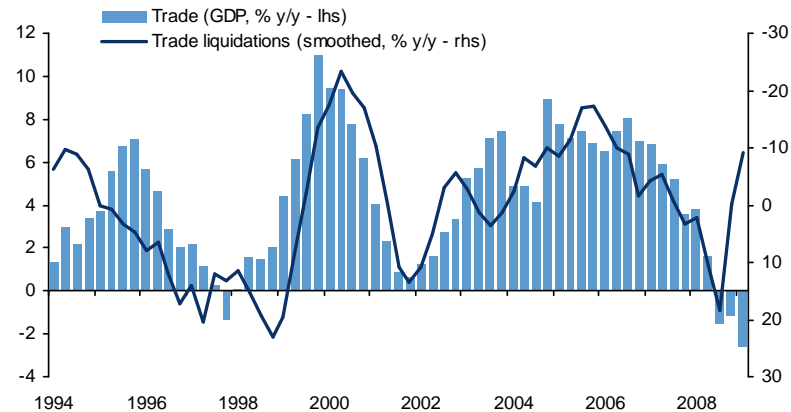
- The ratio of the cost of servicing household debt to disposable income increased sharply to a level of 11,7% in the second half of 2008 on the back of rising debt levels and interest rates in 2006-2008.
- Lower levels of household debt and declining interest rates will see the debt servicing ratio declining to about 8% in 2010.
- The debt servicing ratio is not expected to decline to the 2005 level of below 7%, mainly as a result of the debt ratio remaining above 75% of disposable income and the prime rate forecast to rise again in the second half of 2010.

# Data on liquidations show that different sectors are at different points in their credit quality cycle

Liquidations in manufacturing sector easing



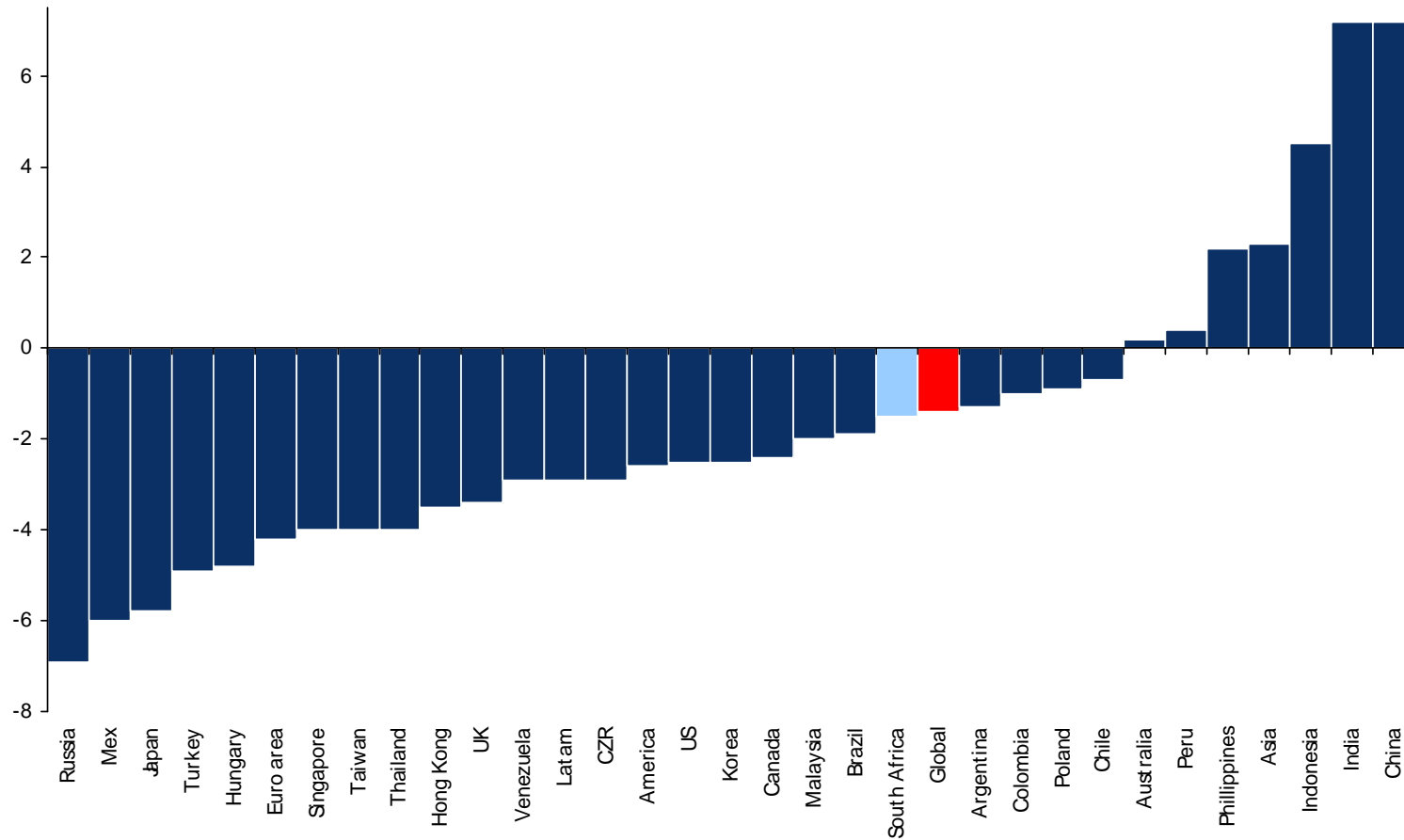
Liquidations in trade sector still rising



The risk of a second consumer distress cycle

## ... that said, 2009 remains a strong (relative) performance

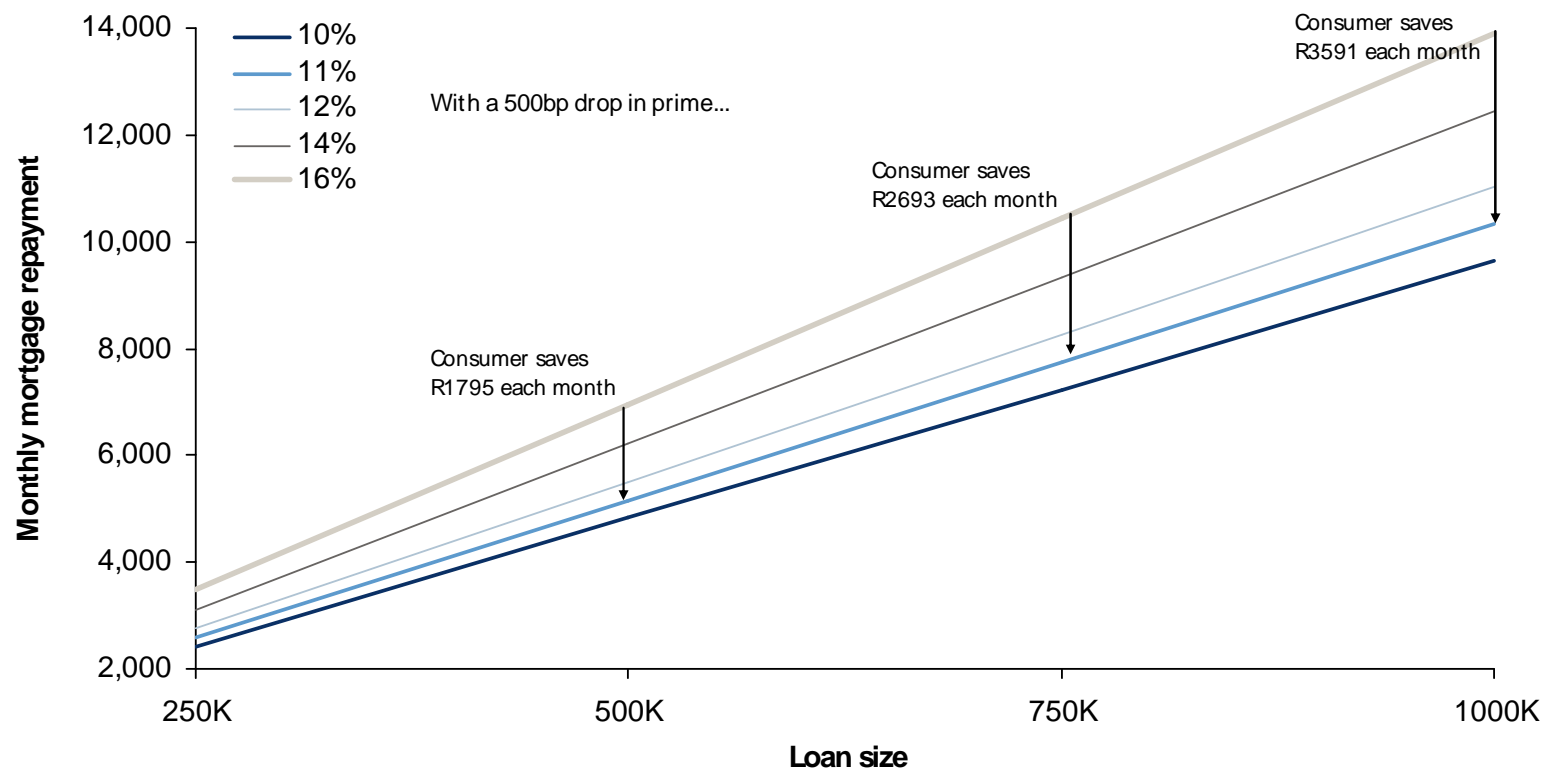
- Of the 50-odd countries that Absa/Barclays forecasts in detail, SA ranks 12<sup>th</sup> in terms of relative growth performance!





# Putting rands back in the pockets of consumers

- Petrol averaged R7.34 in the last 3 months, against R10.16 in Q3 08, saving consumers around R7bn in fuel cost in the last 3 months...
- MPC's rate cuts are worth about R7bn for every 100bp cut....



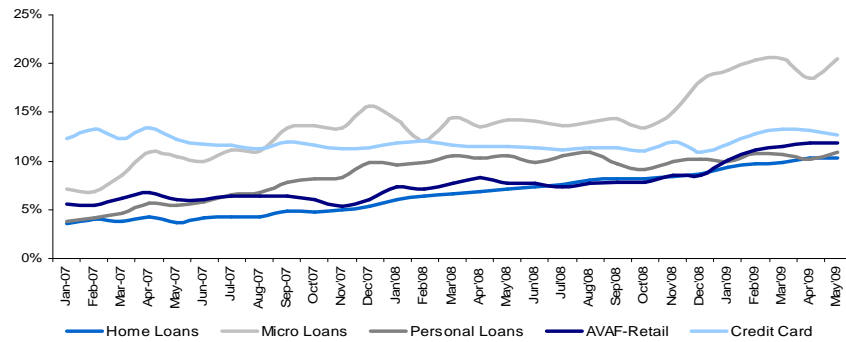
# Green shoots for SA?

## The levels versus direction argument...

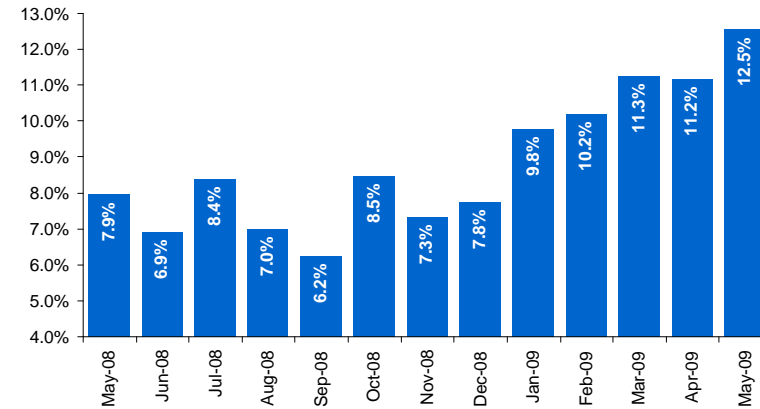
	Latest print	Green shoots?	Period
PMI	<b>37.3</b>	√	May
Business activity	<b>35.1</b>	√√	May
New orders	<b>35.7</b>	√√	May
Expectations	<b>51.3</b>	√√	May
Manufacturing % y/ y	<b>-21.6</b>	<b>X</b>	Apr
Retail sales % y/ y	<b>-6.7</b>	<b>XX</b>	Apr
Passenger car sales % y/ y	<b>-26.9</b>	√	May
Medium comm vehicle sales % y/ y	<b>-41.4</b>	√√	May
Consumer confidence	<b>1</b>	√	Q1
Business confidence	<b>26</b>	<b>XX</b>	Q2
House prices % y/ y	<b>-3.6</b>	<b>XX</b>	May
Building plans passed % y/ y	<b>-28.0</b>	<b>X</b>	Mar
Private credit growth % q/ q	<b>0.8</b>	√	Apr
Households % q/ q	<b>1.0</b>	<b>X</b>	Apr
Corporate credit growth (excl inv and bills) % q/ q	<b>-0.9</b>	√	Apr
Electricity consumed % y/ y	<b>-1.4</b>	√√	Apr
SA leading indicator	<b>105.4</b>	<b>X</b>	Mar

# However, to lend with confidence you need more stability in arrears

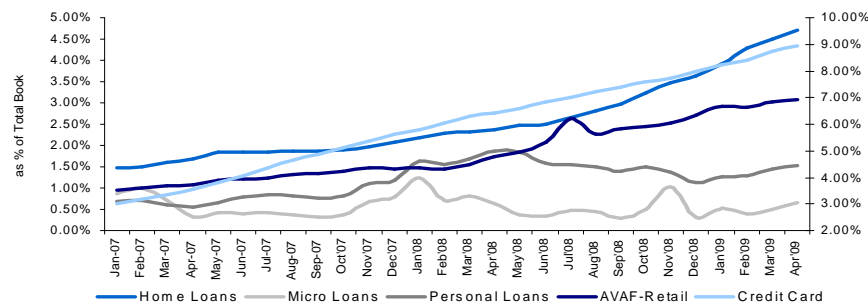
Total arrears (excl Legal) construct of key Portfolios



EWL as % of Loans & Advances



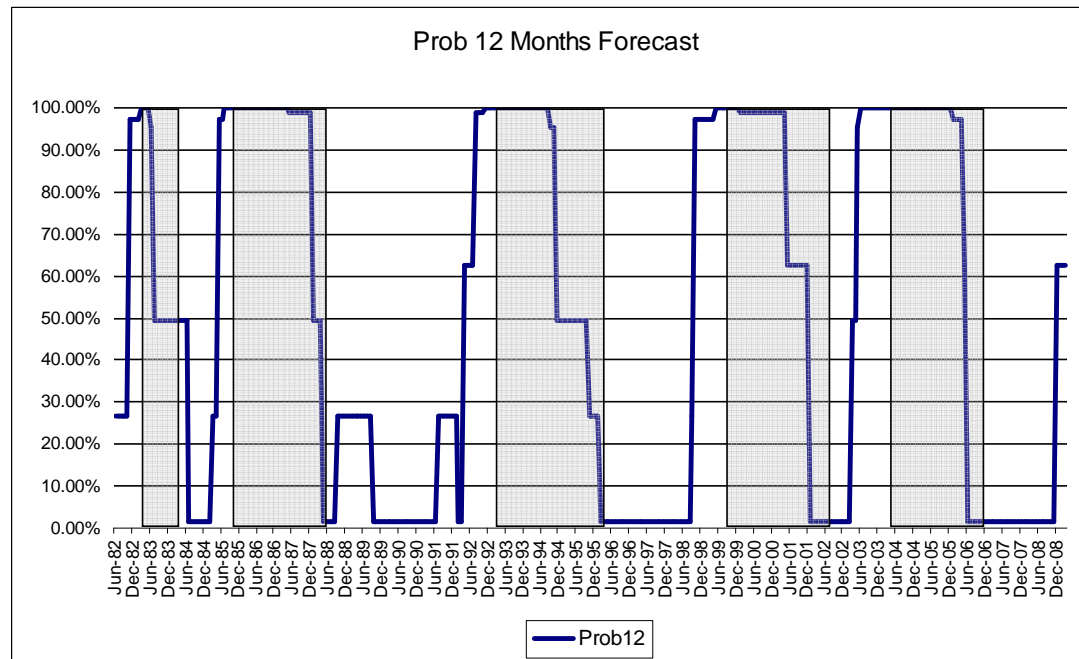
Legal by value



# Constraints facing the consumer in the recovery phase

- **Poor economic performance; slow recovery; low economic growth.**
- **Inflation declining to levels only just below 6%.**
- **Interest rates declining on the back of a poorly performing economy and lower inflation; rates hiked somewhat to keep inflation in check.**
- **Declining employment; low employment growth.**
- **Declining real household disposable income; improving gradually; relatively low growth.**
- **Net household saving to disposable income negative; remaining negative.**
- **Real household consumption expenditure declining; improving gradually on the back of higher growth in disposable income.**
- **Household credit growth in single digits; picking up as a result of lower interest rates and faster growth in disposable income.**
- **Household debt to income declining slightly; picking up gradually during recovery.**
- **Ratio of household debt servicing cost to disposable income declining; rising gradually on the back of slightly higher interest rates and a rising debt ratio.**
- **Lending criteria (National Credit Act and banks' credit criteria).**
- **Many households' credit records were impacted, having implications for future credit extension.**
- **Low and declining property prices having wealth implications in the recovery phase.**

# Economic cycle turning points



- Shaded areas are economic booms in history i.e. up-cycles
- Blue line shows the probability that we will be in a boom period in 12 months time
- In Dec 2008 the probability of being in an upswing in 12 months time was 63%
- We therefore should see the cycle turning around beginning 2010