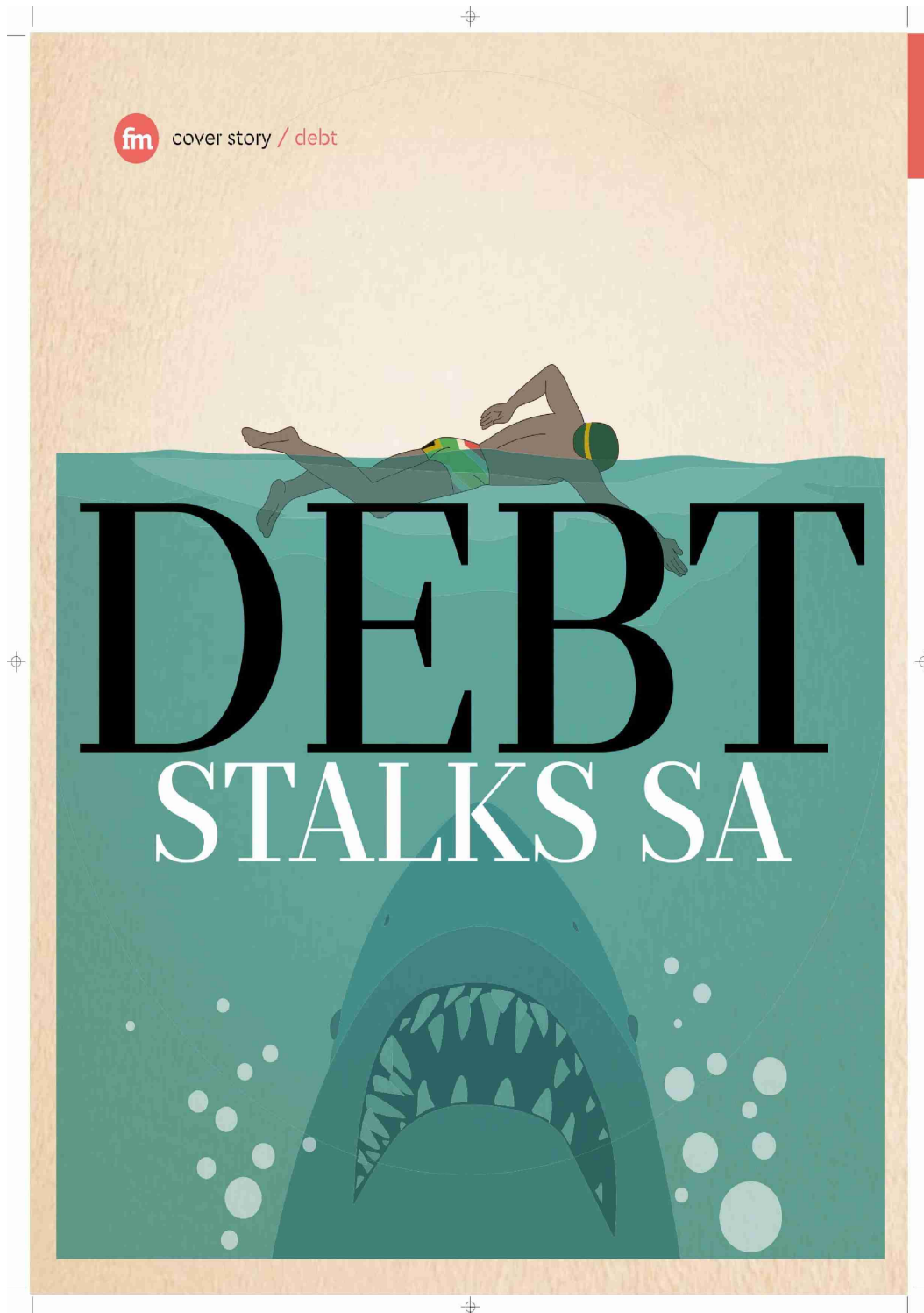
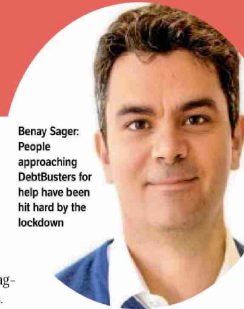








Benay Sager:
People approaching DebtBusters for help have been hit hard by the lockdown

In spite of the huge number of Covid-related job losses and resulting failure of thousands of South Africans to keep up with their credit payments, the big banks are looking remarkably steady. One concern is that civil servants may start to fall victim to retrenchments as the government seeks to cut costs, resulting in many more people (and their banks) feeling the crunch

Stephen Cranston & Rob Rose

Are SA's banks facing a bad-debt crunch, with customers who've been retrenched during Covid-19 defaulting on what they owe?

Given that 26.9 million South Africans owe R196-trillion, it's a question that has bankers on edge, as experts believe only half of the 2.2-million people who lost their jobs in recent months will regain them.

"Unemployment is the single biggest challenge facing SA, and the economic impact of Covid-19 has only made matters worse," says Absa CEO Daniel Mminele.

Few would argue with that.

This month, the National Credit Regulator (NCR) revealed that in the three months to June, millions of South Africans fell behind in their repayments for home loans, vehicle loans and other credit.

In those months, 780,000 accounts were "impaired", as customers fell behind in their payments. And the number of customers "in good standing" fell 3%, to 16.9 million.

It means that, right now, 37.1% of the South Africans who have credit are either behind in their repayments, or have some adverse listing, like a judgment, against them.

Banks are clearly jittery about this, and have been rejecting a large number of loan applications. The result: new consumer loans more than halved during those three months, from R113bn to R47bn.

It's an indication of how fragile the economy is right now.

A research note from Absa on October 6 warns that even as people get back on their feet, "arrears are unlikely to reverse quickly".

"The data shows rising arrears on mortgages, which account for more than half of all consumer lending, and other forms of secured lending, mostly vehicle financing,

What it means:
Economic growth and more employment are desperately needed if SA is to clamber out of the pandemic hole

BY THE NUMBERS

SA consumers at a glance



26.9-million SA consumers have credit and are listed at the credit bureaus

37.1% are either behind in their payments, or have judgments against them

In all, consumers owe R196-trillion in credit

In the three months to June, the amount of new credit granted fell 56% to R54.6bn

In those three months, finance houses rejected 67% of 5.78-million credit applications

In those three months, the value of new mortgages granted fell 66.6%

There were 5.78-million applications for credit in the three months to June – a quarterly decrease of 44.65%

Credit facilities – mainly of credit cards, store cards and bank overdrafts – were down 50.53% quarter on quarter, to R9.51bn

which we view as a troubling sign, since arrears tend to be a lagging indicator," it says.

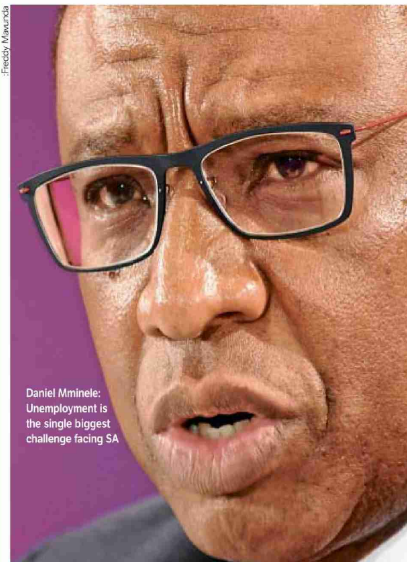
Research by DebtBusters, which is part of SA's largest debt management company, the IDM Group, shows just how badly customers have struggled in recent months.

DebtBusters COO Benay Sager says the people approaching the company for help in recent months have been hit hard by the lockdown.

"The debt exposure of these consumers was the highest in the past several years, led by an increase in unsecured debt levels," he says.

The group's Debtometer, which tracks how South Africans are handling debt, shows that the people who came to the company for help in recent months are using a huge 62% of their monthly income just to pay debt.

And within that group, those who earned more than R20,000 a month had debt equal to 138% of their annual income.



Daniel Mminele:
Unemployment is the single biggest challenge facing SA

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As Sager points out with some understatement, this is "not sustainable".

Neil Roets, CEO of Debt Rescue, a debt counselling company, warns that it's only going to get worse.

"A lot of people were under the impression that they would lose their job only during the lockdown. But I think what's going to happen over the next year or two is that companies will close down, so this issue will be with us for a long time," he tells the FM.

A Debt Rescue survey, released this month, found that an alarming 96% of 1,040 respondents "were stressed about their health, their finances, or both". No wonder – 55% of those who answered said they needed credit, but couldn't get it.

Says Roets: "I believe 2021 will be worse. Until now, companies tapped into their reserves, but those are running out."

"The problem for consumers and businesses is that the credit providers will begin collecting their money, which we haven't seen until now."

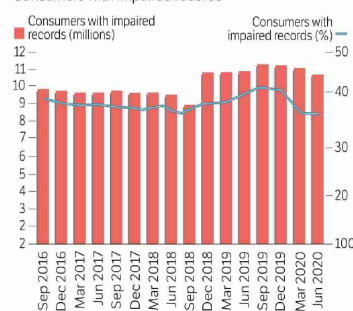
Irrecoverable change

Denker Capital's Kokkie Kooyman is a veteran banks analyst who has seen more market crashes than most. He believes that when everything shakes out in the end, SA consumers will end up with far more debt than they had before the lockdown.

"In the US and UK, the government aid in cases exceeded debt payments, and in SA the government has given little direct relief. But the bottom line is that those SA con-

A MATTER OF RECORD

Consumers with impaired records



Source: Credit Bureau Monitor, Second Quarter 2020, National Credit Regulator

sumers financially affected by the lockdown – those who lost jobs or had diminished income – will have higher debt levels," he says.

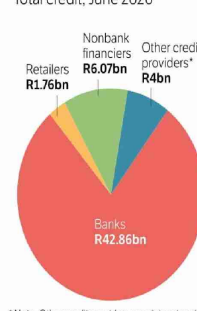
The banks, says Kooyman, are likely to become stricter in granting credit, looking far more closely at whether a customer can repay. "And those clients in a poor financial state will drift towards microlenders," he says.

The recent National Income Dynamics: Coronavirus Rapid Mobile Survey, compiled by more than 40 academics, spells out how tough it has become in the wider economy.

It reveals that Covid-19 struck hardest at the bottom end of the pyramid, among low-skilled or informal workers. For example, almost 50% of the 2.2 million jobs lost have been in the informal sector or in those doing

SHARED LOAD

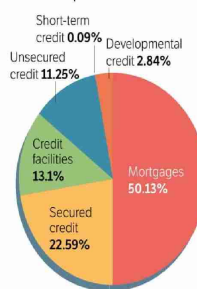
Total credit, June 2020



* Note: Other credit providers consists primarily of pension-backed, developmental, micro-loan and agricultural lenders, insurers, nonbank mortgage lenders and securitised debt
Source: Consumer Credit Market Report, Second Quarter 2020, National Credit Regulator

MARKET SNAPSHOT

How the credit market is made up



Source: Consumer Credit Market Report, Second Quarter 2020, National Credit Regulator



Haroon Bhorat: Many of the jobs lost during lockdown will probably return

domestic work.

Haroon Bhorat, professor of development economics at the University of Cape Town (UCT), who worked on the survey, says many of these jobs will probably return.

"This evidence would suggest that if informal sector and domestic worker jobs bounce back, as I expect them to, then we are looking at a scale of job losses similar to the great recession of 2008, when we lost about 1-million jobs," says Bhorat.

But this means that banks with a disproportionately large share of clients in semi-skilled or low-skilled formal sector jobs – some of which have vanished permanently



Alan Pullinger: Activity levels remain muted

– may end up with large amounts of unpaid debt on their books.

Of course, it's not as if consumers were in great shape before Covid.

Last year, investment company Differential Capital published a controversial report that said unsecured lending "has consumers sliding towards financial ruin".

It said 7.8-million South Africans owed R228bn in unsecured debt, paying as much as 225% in interest in some cases.

"Perhaps the debt trap that consumers almost invariably find themselves in after taking out an unsecured loan would be more palatable if its proceeds were used for constructive purposes ... [but] 74% is for consumption purposes or borrowing to pay off other loans," the report noted.

If, as Kooyman suggests, more consumers drift towards microlenders – while salaries remain low and jobs vanish – the picture isn't pretty.

So what could change this trajectory? Pretty much only an economic recovery.

Even after the economy begins growing again, Mminele says SA's experience during the 2008 global financial crisis shows that job losses may continue for some time.

"The probability of a national debt crisis will keep rising in the absence of drastic measures, which require difficult decisions about structural reforms, and necessary trade-offs," he says.

Last week, President Cyril Ramaphosa launched his economic reconstruction & recovery plan. While some of the measures look unfeasible – the energy targets, for example – this wasn't the main problem.

Rather, it is that the government has launched so many plans, and implemented so few, that not many people believe this one will be any different.

Mminele says the plan has "a few new initiatives – but a relentless focus on implementation and tangible evidence of [that is needed] to shore up confidence [and] break some of the negative feedback loops".

Banks lose value fast

But if SA's consumers are on a hiding to nothing, what does this mean for the banks that lend to them?

All of them have taken a beating on the JSE this year, reflecting the possibility that bad debts from consumers would eat deeply into their profits.

Nedbank's shares have lost the most this year, shedding 54%. But everyone felt the pain: Absa is down 39.2%, FirstRand 37.5%,



Standard Bank 34.5% and Capitec 24.2%.

To mitigate the loss, all the banks have hiked their credit-loss ratios – the amount of money they set aside to cover bad debts – from about 0.4% of their total loans to about 2% today.

In FirstRand's annual report for the year to June, CEO Alan Pullinger says that while things are improving after the lockdown, "activity levels remain muted".

In truth, things are so bad that FirstRand reported a return on



Jacques Celliers: We are seeing greater acceptance of new ways of banking

fm cover story / debt

equity lower than its cost of equity for the first time since the 2008 financial crisis.

If anything, its peers have done worse. With record low interest rates, banks can no longer expect a healthy income stream just from the interest earned off their own capital. And yet, despite this, some bankers are still quite positive.

Jacques Celliers, the dynamic CEO of FNB, FirstRand's retail unit, tells the FM that at least crises are a good way of wiping away old practices.

"We are seeing greater acceptance of new ways of banking, principally online from people who, pre-Covid 19, were still drawing money at counters or using advisers to buy simple credit life insurance," he says.

Does he think the hard times are over?

No, he says. "The pebble is in the water, but many ripples are still going to be felt."

But there are, at least, green shoots.

For one thing, for most banks, their most profitable cohorts of customers have bounced back fastest.

From April to June 2020, the proportion of people aged over 50 now working increased from 45% to 52%. By December, this may exceed the 56% level of February.

And banks, including FNB, are readjusting their lending criteria to be more flexible.

Says Celliers: "A hairdresser and a coffee shop might have similar financial needs and a similar staff complement, but we need to treat every small business differently to ensure we lend to the survivors."

Luckily for the banks, Covid-19 arrived at a time when they had already been making sure they weren't heavily exposed to credit losses.

This is partly why none of the banks seems near to any sort of collapse.

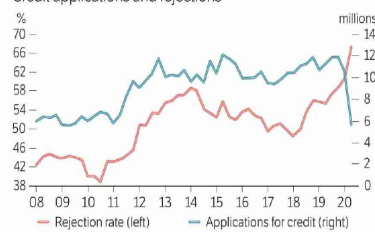
Chris Steward, head of financials at investment company Ninety One, says the four big banks all have solid capital buffers.

"It would take an impairment charge equivalent to more than three times the reported annualised 2020 bad debts at FirstRand or Standard Bank before their capital 'buffer' was eroded," he says.

At Absa and Nedbank, he says, this buffer would be eroded if bad debts were to double. While that's not impossible, it seems unlikely at this point.

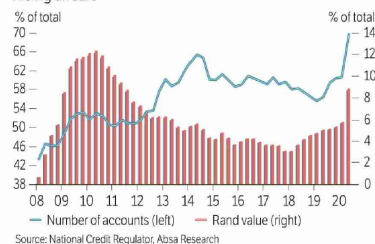
FEELING THE COVID CRUNCH

Credit applications and rejections



FALLING BEHIND

Rising arrears



For investors, says Steward, the two safest banking bets are FirstRand and Capitec.

Capitec is an interesting case. It is, perhaps, the bank most exposed to the lower end of the market, where there's been a bloodletting of jobs. But the bank has shifted dramatically in recent years, from being a microlender to taking deposits.

HOLDING THE LINE

Credit standing of consumers, June 2020

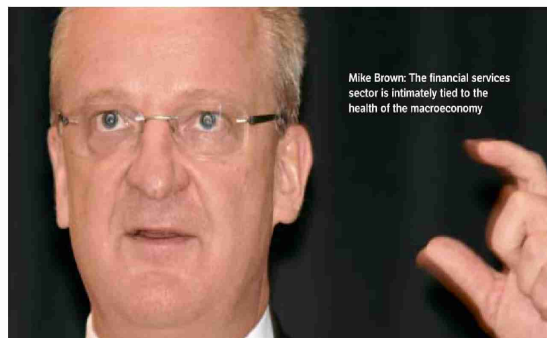


Kooyman argues that Capitec also imposed far stricter credit criteria before Covid-19, which led to it rejecting many applications. And today, it's largely eschewing loans to clients earning less than R7,000 a month.

Capitec also has set aside far more than its rivals to cover bad debts – its debt-loss ratio is now 8%, up from 6% last year – but that's probably right, considering it makes riskier, unsecured loans.

Bhorat says that if Capitec has a large number of informal-sector clients who can bounce back quickly into economic activity, it'll be better placed than banks with a large share of formal-sector workers in, say, the tourism or restaurant industries.

Of course, making a call on where bad

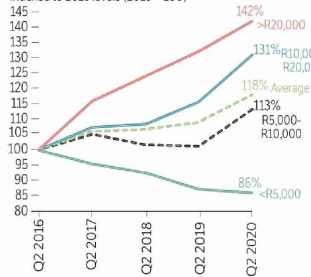


Mike Brown: The financial services sector is intimately tied to the health of the macroeconomy

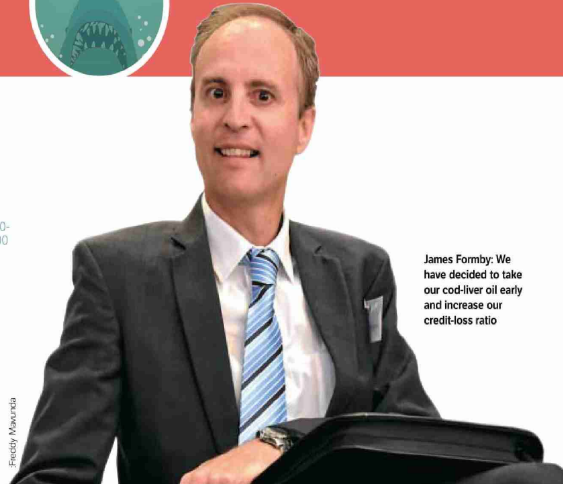
GROWING RISK

Unsecured loan growth

Change in unsecured debt levels per income band, indexed to 2016 levels (2016 = 100)



Note: Data for DebtBusters clients signed up in the quarter
Source: Debtometer, Quarter 2 2020, DebtBusters



James Formby: We have decided to take our cod-liver oil early and increase our credit-loss ratio

debts will end up almost seems like throwing a dart against a wall right now.

Gustav Raubenheimer, finance director of African Bank, tells the FM it would be "irresponsible" to rely on historical data to make this call.

"We have mostly seen, in our credit life numbers, an increase in unpaid leave and shortened weeks, but not the increase in retrenchments you might expect," he says.

The concern for African Bank, however, is that a third of its loans have been made to the public sector – including civil servants.

Raubenheimer says this group has "been immune so far". But finance minister Tito Mboweni has to find a way to slash government spending – and cutting the civil service is the obvious route.

The economic helix

Nedbank CEO Mike Brown says: "It is hard to find another sector that is so intimately

tied to the health of the macroeconomy" as the financial services sector.

For this reason, he thinks banks will have a hard time over the next two years. Consumers are clearly struggling, even if the three percentage point fall in interest rates this year has dulled the pain to an extent.

In Nedbank's case, customers appear to have been surprisingly resilient. Brown says, for example, that just 20% of the bank's retail customers asked for a payment holiday when Covid-19 struck.

"Of these, 80% resumed payment quite effortlessly after three months, just 10% requested an extension and a further 10% missed their first payment," he says.

Brown expects the 80% of clients who didn't ask for payment relief to become financially stronger in the months ahead, in part because of the interest rate cuts.

But individual customers are one thing; what happens when large companies fall over? Already this year a number have tipped into business rescue – including Edcon and Comair. Could banks face a potential crisis from this quarter?

James Formby, CEO of Rand Merchant Bank, says corporate clients have not proven to be as vulnerable – for now.

"But we have decided to take our cod-liver oil early and [increase] our credit-loss ratio from 0.12% to 0.94%," he says.

"This is much wider than current bad debts and includes forecast nonpaying loans

which we believe will emerge in the June 2021 financial year and beyond."

Large companies also, obviously, have more options available to them – such as issuing new shares rather than taking out loans.

Formby reveals that corporate deposits are growing much faster than loans – at about 12% until February, compared with 4% loan growth. If anything, it's a reflection that companies don't yet have the confidence to invest in the SA economy, and would rather sit on their cash.

Of course, all expectations could fly out the window if something big were to happen in the economy – like the government defaulting on its debt.

But Bhorat doesn't see that as likely.

"I don't see that as a risk and certainly, with a cabinet and president mindful of the dangers of an excessive fiscal deficit, the huge interest burden we already face and the need for a growth plan, I think a sovereign default is going to be avoided at all costs."

The other big unknown is what happens with Covid-19, and whether any resurgence in infections prompts the government to reimpose a stricter lockdown.

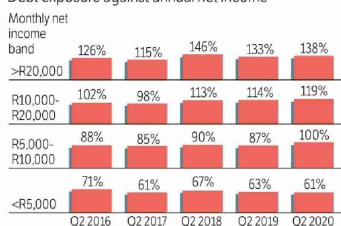
Says Steward: "I only hope we are not going to return to a full lockdown, which [will make] a recovery much harder."

But even if SA doesn't go back to a stricter lockdown, and a vaccine arrives, the country isn't going back to business as usual. A much weaker consumer has changed the game for SA's banks.

And as much as the ANC might be tempted to shift the deck chairs, the only long-term solution is economic growth and jobs. x

OVERINDEBTED

Debt exposure against annual net income



Note: Debt exposure against net income ratio when clients sign up with DebtBusters
Source: Debtometer, Quarter 2 2020, DebtBusters