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# in the moment


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## Consumer pulse: Sentiment lifts but financial stress endures

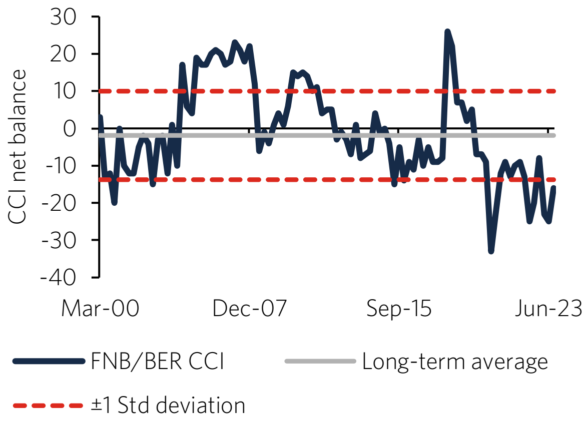
### Highlights

- According to the First National Bank (FNB)/Bureau for Economic Research (BER) Consumer Confidence Index (CCI), consumer sentiment rose from negative 25 points to negative 16 in the third quarter of 2023.
- Less negative sentiment stemmed from improved perceptions of the economic outlook (negative 22 points from negative 37 points) and high-income households (negative 17 points from a record low of negative 40 points).
- Quarterly Labour Force Survey (QLFS) data published by Statistics South Africa (Stats SA) reported a slight drop in the second quarter unemployment rate to 32.6% from 32.9% in the first quarter. Most of the job gains were recorded in the construction industry.
- Expected employment growth remains negative across most of the industries covered by the BER's quarterly surveys (manufacturing, retail, wholesale and construction) which means that these industries are unlikely to ramp up jobs significantly in the near term. The services industry, bolstered by tourism, seems to be the exception.
- Real wage growth in the second quarter of 2023 contracted by 1.2%, marking the fifth consecutive quarter of negative growth. This implies that consumers are worse off than before in terms of their purchasing power. The South African Reserve Bank (SARB) expects nominal average salaries to rise by 6.6% in 2023 and 6.1% in 2024 which translates to real wage growth of 0.6% this year and 1.1% in 2024. This will likely improve consumer demand but we do not expect an inflationary impact to result from this.
- There is increasing evidence pointing to consumers feeling the pinch of elevated interest rates.
- Nominal private sector credit extension (PSCE) to households softened for the sixth consecutive month to 6.1% y/y in July which suggests a reduction in the rate of credit take-up. Data from the National Credit Regular (NCR) showed that lending conditions remained stringent but the appetite for credit decreased in the first quarter.
- The ratio of debt-service cost to disposable income edged higher to 8.4% in the first quarter of 2023. This is still relatively contained compared to levels reached during the pandemic and the global financial crisis (GFC) but we expect the ratio to tick up further in light of elevated interest rates and negative real wage growth.
- The deterioration in Experian's Consumer Default Index (CDI) across the various credit products is an indication of consumers' increasing inability to finance their debt.
- Signs of consumer stress are becoming apparent given a deterioration in credit metrics which are reflecting the lagged effect of higher inflation on consumers' disposable incomes and their purchasing power. However, the uptick in consumer sentiment to less negative levels bodes well for a mild improvement in household expenditure next year from an expected 0.8% this year to a projected 1.3%. We expect this to be largely based on an improvement in real incomes as lower anticipated inflation in 2024 should drive a recovery in real household income.

## High-income households lift overall CCI

Consumer confidence recovered markedly in the third quarter of 2023 with the FNB/BER CCI picking up to negative 16 points from the second-lowest confidence reading of negative 25 points since the inception of the index. Even with this uptick, confidence levels remain significantly weak as witnessed by the overall reading remaining below the long-term average of negative 1.9 since 1982 as seen in chart 1.

Chart 1: CCI improves but remains weak




*Source: BER, Momentum Investments*

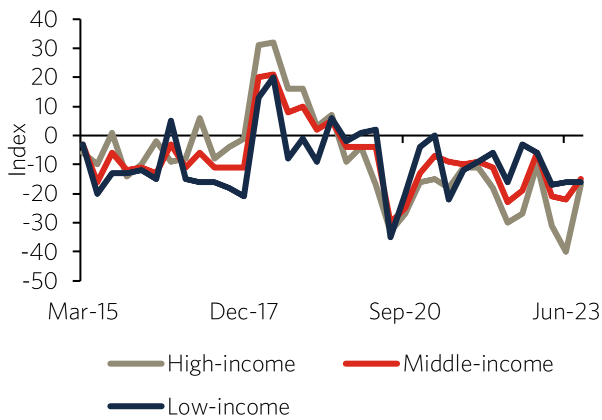
Confidence gains in the third quarter were largely driven by high-income households (earning more than R20 000 per month) and the improvement in the expectation of economic performance. The sub-index measuring expected economic performance ticked up by 15 points to negative 22 points in the third quarter of 2023. This could be attributable to better-than-anticipated economic growth in the first half of this year. While the survey was concluded before the release of the second quarter gross domestic product (GDP) figure, the high frequency data of industrial production was pointing toward positive growth in the second quarter.

The sub-index relating to the appropriate time to buy durable goods also improved from negative 35 points to negative 26 points. This could be on the back of the upcoming festive season and Black Friday sales where consumers historically indulged in the purchase of big-ticket items. However, this sub-index is still very weak which indicates that we may not see a big uptake of durable purchases yet.

Expected household finances increased marginally by one point to negative one. The data shows that consumers are still more concerned about the state of the economy than their personal finances relative to the historic gap between the two indices.

Shifting the focus to income bands shows that much of the improvement in sentiment was expressed by high income households whose confidence levels soared by 23 points to negative 17. This comes after intense pessimism that saw high-income households' confidence levels dip to a historical low of negative 40 points in the second quarter of 2023. The BER indicates that this segment's pessimism in the second quarter was on the back of loadshedding concerns, rand weakness, interest rate hikes and rising geopolitical concerns. While loadshedding remains a recurring feature, SA dodged the worst-case scenario of stage 8 during winter. Furthermore, the SARB adopted a wait-and-see approach by pausing interest rates at the July meeting and geopolitical concerns have subsided following the finding that no arms were loaded onto Lady R (Russian vessel). These developments support the retraction of pessimism from high-income households.

Chart 2: CCI among income groups has merged




*Source: BER, Momentum Investments*

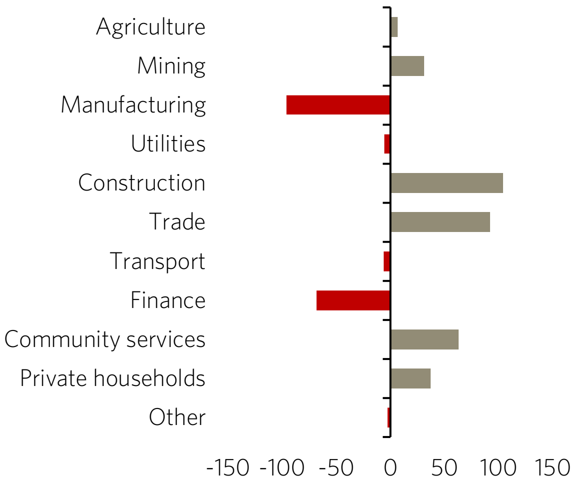
Confidence levels of middle-income households (earning between R5 000 and R20 000 per month) improved to negative 15 points in the third quarter (previously negative 22 points) and sentiment from low-income households (earning less than R5 000 per month) remained unchanged at negative 16. This brought the confidence levels of the different income groups to around the same level as depicted in chart 2.

## Services likely to record employment gains in the near term thanks to tourism revival

The official unemployment rate, reported by Stats SA, decreased slightly from 32.9% in the first quarter of 2023 to 32.6% in the second quarter. Over this period, the increase in employed persons (153 914) outpaced the increase in the labour force (142 539).

Employment opportunities in the second quarter were created in six of the 10 industries, with the biggest gains recorded in construction (103 800), trade (91 700), community services (62 800) and private households (37 200). Industries that shed the most jobs were manufacturing (96 300) and finance (68 100) as seen in chart 3.

Chart 3: Construction had the largest employment increase in 2Q 2023 (q/q)

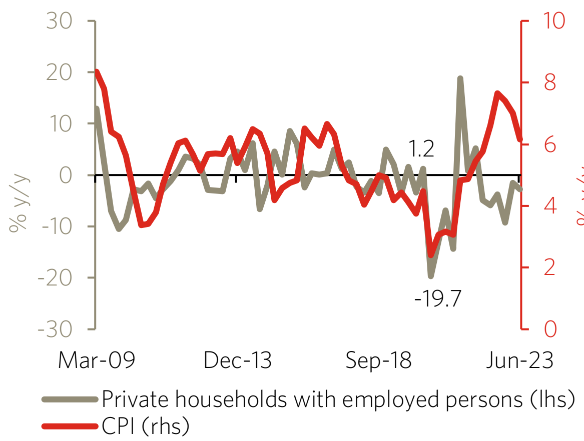



*Source: Global Insight, Stats SA, Momentum Investments*
*Utilities refer to electricity, gas and water supply*
*Trade refers to wholesale and retail trade; repair of motor vehicles, motorcycles and personal and household goods; hotels and restaurants.*
*Finance refers to financial intermediation, insurance, real estate and business services.*
*Red illustrates job losses and gold illustrates job gains*

We also observe growth in employment on a year-on-year basis (second quarter of 2023 compared to the second quarter of 2022) of 784 334 jobs. These job gains are spread across nine of the 10 industries and the most jobs came from trade (197 700), community services (143 700) and construction (127 600). Only private households recorded job losses of 30 500.

The category 'private households' typically refers to employment of paid domestic work (cleaning, cooking and gardening). As illustrated in chart 4, the rate of job creation in this industry plummeted from 1.2% y/y to negative 19.7% y/y between the first and second quarters of 2020 when lockdown restrictions were implemented. Employment growth subsequently recovered to a peak of 18.8% y/y in the second quarter of 2021 but has since been on a downward trend. The decline since the second quarter of 2021 can partly be explained by the surge in inflation which, together with the rise in interest rates, significantly reduced consumers' disposable income. As a result, households likely laid off or reduced demand for paid domestic work as a measure to deal with the cost-of-living crisis. Another factor that could explain this downward trend is the new normal of working from home which results in a lower demand for paid domestic work.

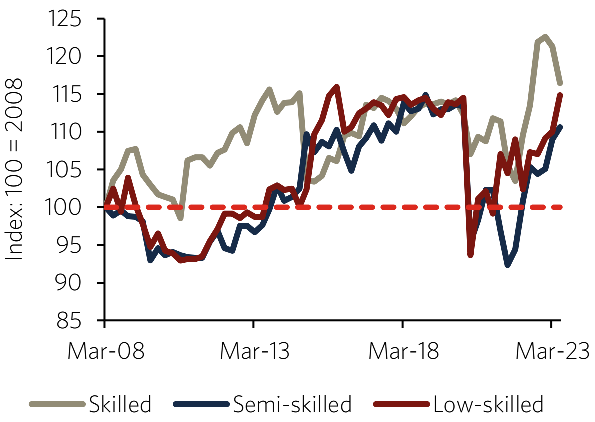
Chart 4: Surge in inflation partly explains the decrease in private household jobs




*Source: Global Insight, Stats SA, Momentum Investments*

Employment of skilled workers recovered to well above pre-pandemic levels. However, chart 5 illustrates that more people are losing jobs in these occupations. The sharp decline is largely due to managers where the number of employed managers decreased from the peak of 1.5 million in December 2022 to 1 2 million in the second quarter of 2023. Skilled individuals are known to enjoy job security but the recent statistics suggest creeping vulnerability likely due to unfavourable business conditions.

Chart 5: Skilled employment losing momentum

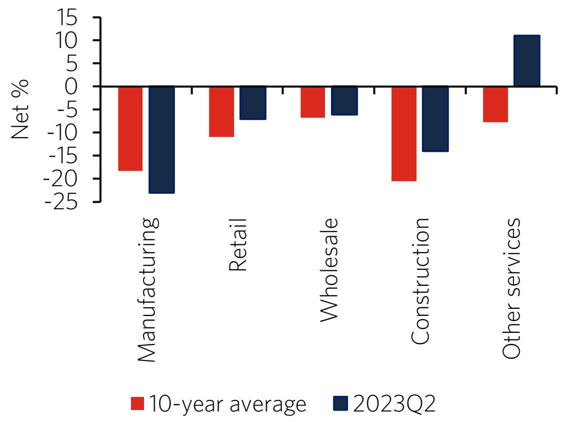



*Source: Global Insight, Stats SA, Momentum Investments*
*Skilled refers to managers, professionals and technicians*
*Semi-skilled refers to clerks; sales and services; skilled agriculture; craft and related trade; and plant and machine operator*
*Low-skilled refers to elementary jobs and domestic work*

On the other hand, there is an increase in semi-skilled and low-skilled employment jobs. These two categories will be partly supported by the 'Nasi iSpan' initiative (a Gauteng-based recruitment drive 'aimed at addressing unemployment and promoting access to job opportunities available within the Provincial Government'). According to the Gauteng provincial government, the programme has attracted more than 1.3 million applications for 8 000 posts and the process of filling these vacancies is underway.

Collating information about expected employment across the various BER surveys indicates weak employment perceptions across the industries, apart from other services as seen in chart 6. Manufacturers were more pessimistic about expected employment than the other industries in the second quarter (negative 23 points) and the reading was worse than the 10-year average. The perception of retailers, wholesalers and construction in the second quarter was better than their respective 10-year averages but remained negative. These trends are not encouraging for significant job creation prospects. Services was the only industry with positive employment perceptions in the second quarter and this is likely linked to the current recovery in tourism which is boosting activity in the services sector.

Chart 6: Employment perceptions are generally weak



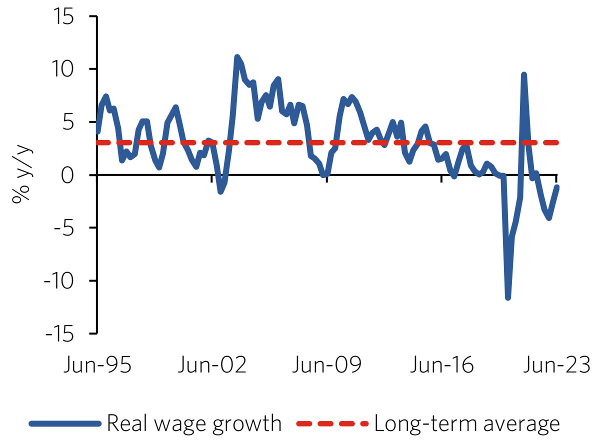

*Source: BER, Standard Bank, Momentum Investments*

## Wages have not kept up with inflation

Employed persons have been consistently confronted with negative real wage growth for the past few quarters (see chart 7) which means consumers' financial position has been worsening. Since December 2022, the direction has changed toward an upward trajectory. In the second quarter of 2023, real wage growth was negative 1.2% y/y which was an improvement from negative 2.6% y/y in the previous quarter. This improvement was due to an increase in nominal wage growth and a decrease in the average inflation rate during the quarter. Nevertheless, real wage growth is still negative and below the long-term average growth of 3%.

In the July Monetary Policy Committee (MPC) meeting, the SARB revised expected nominal average salaries down for 2023 (from 6.8% in the May meeting to 6.6%) and for 2024 (from 6.5% to 6.1%). The estimate for 2025 was revised up from 4.9% to 5.2%. Taking into account the SARB's headline inflation forecast, real average salaries are expected to be positive in the medium term and grow by 0.6% in 2023, improve to 1.1% in 2024 before moderating to 0.7% in 2025. While these estimates are likely to put consumers in a slightly better position, we do not expect the impact to be inflationary because these real wage rates are still relatively low and below the long-term average. Moreover, consumers have endured prolonged periods of financial strain and a slight increase in real incomes may be allocated toward expenditure items that were sacrificed to afford necessities. Finally, extra income may go toward repaying debt accumulated to deal with the cost-of-living crisis.

Chart 7: Purchasing power dented




*Source: Global Insight, Iress, Stats SA, Momentum Investments*

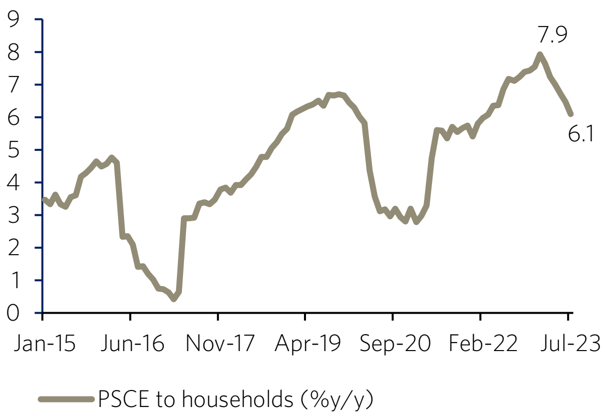
## High interest rates biting consumers

Since the start of the interest rate hiking cycle in November 2021, which was aimed at arresting the surge in inflation, the SARB has raised rates by a cumulative 475 basis points. At the July 2023 interest rate setting meeting, the SARB kept rates constant at 8.25% after increasing consistently over the previous 10 meetings. The decision to pause rates was welcomed by consumers but it does not provide immediate relief because some of the previous interest rate hikes are still working their way into the economy.

There is increasing evidence of consumers feeling the pinch from past interest rate hikes.

One of the tell-tale signs of the previous interest rates working into the economy is the moderating credit growth. Credit has been one of the tools that consumers used to supplement their income in order to meet their monthly obligations. As seen in chart 8, nominal PSCE to households moderated for the sixth consecutive month from the peak of 7.9% recorded in January 2023 to 6.1% in July. This moderation could be related to debt becoming more expensive to service. On the other hand, real PSCE is ticking up but this is due to the deceleration in inflation witnessed over the past few months.

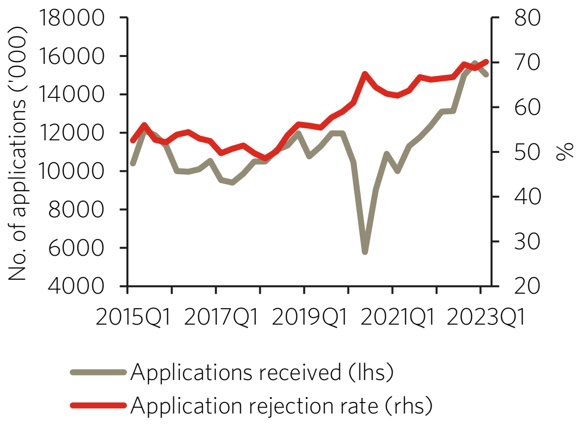
Chart 8: Deceleration in PSCE growth to households




*Source: Global Insight, SARB, Momentum Investments*

According to the NCR, the number of credit applications received decreased from 15.61 million in the fourth quarter of 2022 to 15.02 million in the first quarter of 2023. This marks the first decrease in applications since the first quarter of 2021. On the other hand, the rejection rate increased to 70.1% from 68.7% over the same period (see chart 9).

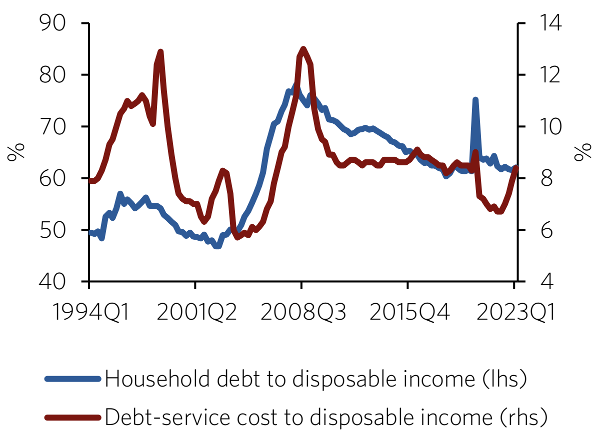
Chart 9: Credit appetite lower in 2023Q




*Source: NCR, Momentum Investments*

The second tell-tale sign is the increasingly stretched debt-service cost-to-disposable income ratio illustrated in chart 10. The ratio of debt-service cost to disposable income has gone up in higher increments from 7.4% in the third quarter of 2022 to 7.9% in the fourth quarter and then to 8.4% in the first quarter of 2023. We note that the debt-service cost to disposable income ratio is still relatively contained compared to levels reached during the COVID pandemic in 2020 and the GFC in 2008. However, we expect the debt-service cost-to-disposable income ratio to increase further in light of elevated interest rates and negative real wage growth. This points to financial pressure on consumers in the coming months as debt obligations increase, which will likely lead to less savings (for those who save) and less spending as budgets get re-adjusted.

Chart 10: Higher debt-service cost ratio



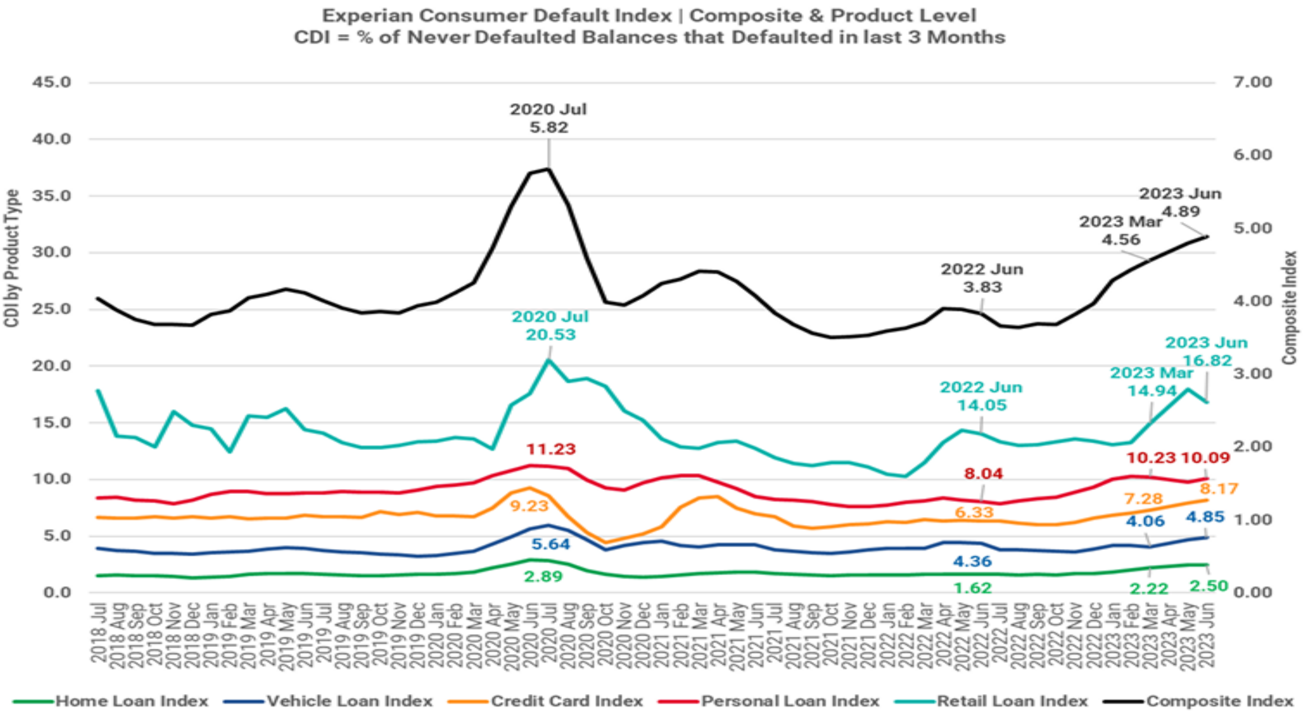

*Source: SARB, Momentum Investments*

The third indication of consumers feeling the burden of elevated interest rates is the rise in credit defaults. The Experian CDI ("an index measuring rolling default behaviour of SA consumers with home loan, vehicle loan, personal loan and credit account account") deteriorated to 4.89 in June 2023 (the worst level since the third quarter of 2020). As depicted in chart 11, the deterioration of the CDI has become steeper in recent months which indicates increasing consumer financial distress.

The deterioration in the CDI is evident across all the product types. Retail loans are recording the highest default behaviour followed by personal loans, while home loans have the least rolling defaults. This trend is an indication that lower income consumers are experiencing more financial strain than higher income earners. Debt Busters notes that consumers' top two priorities in their debt profile are home loans and vehicle loans and that retail debt is typically ranked as the lowest priority, with some consumers choosing which retailers to pay especially when there are other financial needs to tend to.

The last tell-tale sign is lower demand proxied by retail trade sales data. Seasonally adjusted retail trade sales decreased to 1% q/q in the second quarter of 2023. Sales were lower across all the retailer types with the biggest drop recorded for household furniture, appliances and equipment sales. This also speaks to consumers buying fewer non-essential items.

Chart 11: General increase in credit defaults across the different credit products




*Source: Experian*

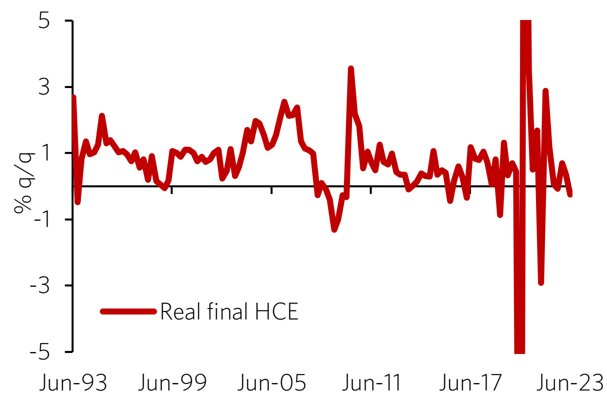
*The weight of home loans to the composite CDI is the highest at 53% given the value of this product type and retail loans have the smallest weight of 2%.*

## Household consumption expenditure under strain

Signs of consumer stress are becoming apparent given a deterioration in credit metrics which are reflecting the lagged effect of higher inflation on consumers' disposable incomes and their purchasing power. However, the uptick in consumer sentiment to less negative levels bodes well for a mild improvement in household expenditure next year from an expected 0.8% this year to a projected 1.3%. We expect this to be largely based on an improvement in real incomes as lower anticipated inflation in 2024 should drive a recovery in real household income.

Real final household consumption expenditure (HCE) contracted by 0.3% q/q in the second quarter of 2023. We expect household consumption to remain weak in the coming quarters with the rising need to allocate more income to repay debts. The early sign of lower appetite for credit further illustrates that there may be a need to cut back on expenditure if credit cannot be used to bridge the income gap.

Chart 12: HCE contracted in the second quarter




*Source: Stats SA, Momentum Investments*

We expect some reprieve on consumer finances from next year. This is on the back of a moderation in inflation, higher real wages and rate cuts from the second quarter of 2024.