Business Debt Index

Quarterly Summary - Q4 2023

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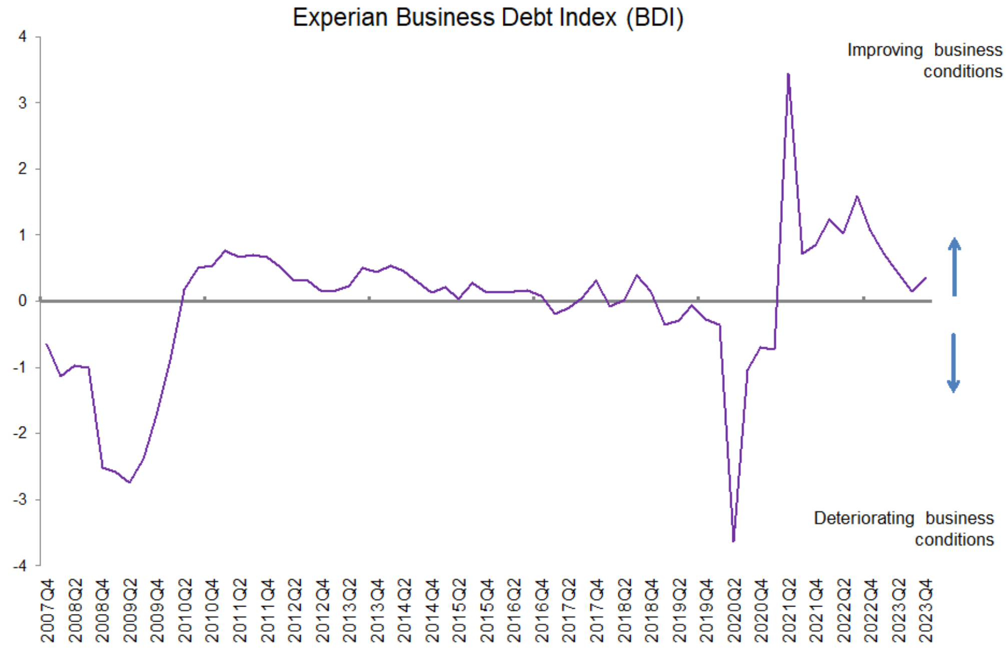
EXPERIAN BUSINESS DEBT INDEX (BDI) RESULTS FOR Q4 2023

Modest improvement in Experian BDI in Q4 reflects ability of businesses to cope with a low-growth environment

The Experian Business Debt Index (BDI) rose moderately in Q4, to 0.364, from 0.148 in Q3 and 0.432 in Q2.

This modest increased improvement in business conditions was a function of a combination of factors, mainly reflecting some resilience on the part of the South African economy and the ability of businesses to cope with a low-growth environment that is at least not deteriorating further.



Source: Experian

	Q4 2022*	Q1 2023*	Q2 2023*	Q3 2023*	Q4 2023
Index >0= Improving business conditions <0 = Deteriorating business conditions	1,074	0,719	0,432	0,148	0,364

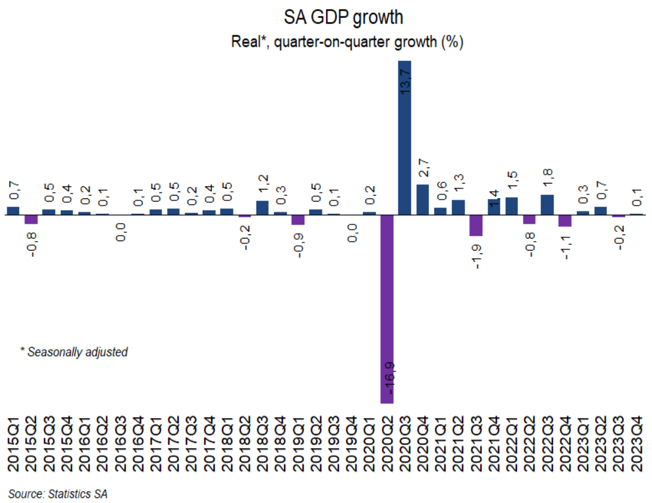
** Revised*

Macroeconomic factors influencing Q4 2023

From a business health point of view, what has helped is that interest rates remained stable for most of 2023 instead of rising continuously from quarter to quarter as they had in 2022.

Having increased by 4.75% from November 2021 to March 2022, the absence of further increases in debt servicing costs beyond the early part of last year prevented further erosion of business profitability.

Also contributing to the stability of business debt conditions was the fact that domestic economic growth, whilst weak, continued to be relatively stable. GDP growth increased to 0.1% on a q/q basis in Q4, from negative growth of -0.2% in Q3.

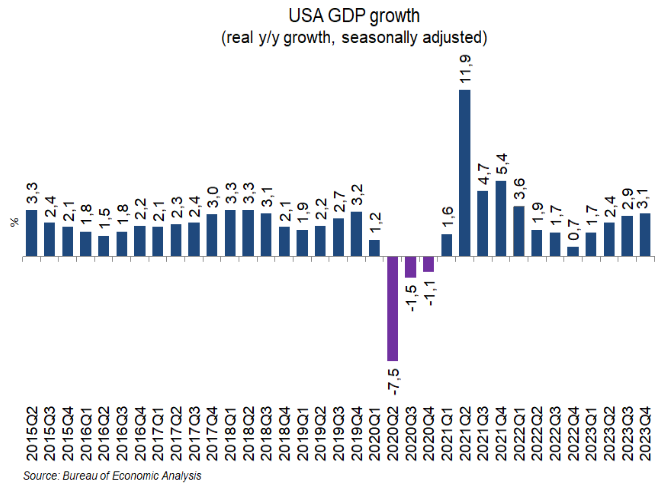


The reduction in the intensity of electricity load-shedding in Q4 and the improvement in logistical bottlenecks at South African ports, which had previously impeded the delivery of supplies to various parts of the country and hindered exports, were important contributors to this stabilisation of economic performance.

Finally, from an international perspective, there were signs of economic growth holding up much better than had been expected in the face of the preceding sharp rise in global interest rates.

In particular, US economic growth sustained an upward trend that surprised with its strength through 2023.

This allowed for South Africa's export performance to hold up slightly better than might have been expected.

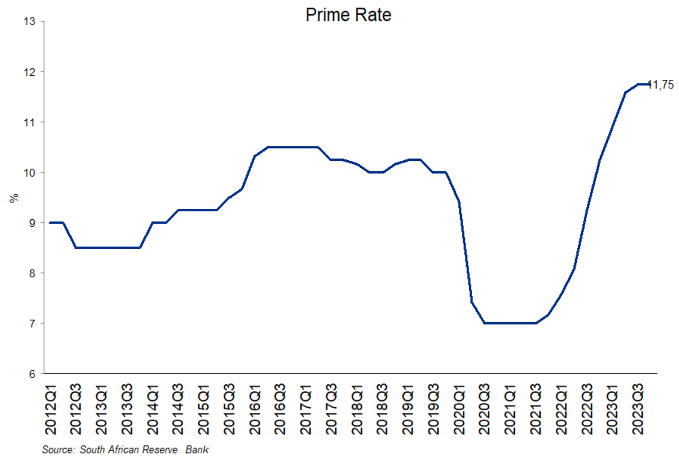


More specifically, Q4 witnessed a disappointing reduction in gross fixed capital formation (GFCF) for a second consecutive quarter, following an encouraging upward trend in this critical measure of investment in the country's future that had been developing in the preceding two years.

Fortunately, the contraction in GFCF, at -0.2%, was significantly more moderate than the -3.8% decline in GFCF recorded in Q3. On the other hand, Q4 witnessed moderate recovery in the industrial heartland of the South African economy.

All of mining, manufacturing, and electricity production saw growth picking up meaningfully in Q4 from the slumps they experienced during Q3. Much of this can be attributed to the improved environment in respect of electricity production and supply bottlenecks at South African ports.

Furthermore, the stabilisation of interest rates following their steep upward trend through 2022 meant that growth in consumer spending also stabilised, recording 0.2% positive growth in Q4 after having contracted by -0.2% in each of Q2 and Q3.



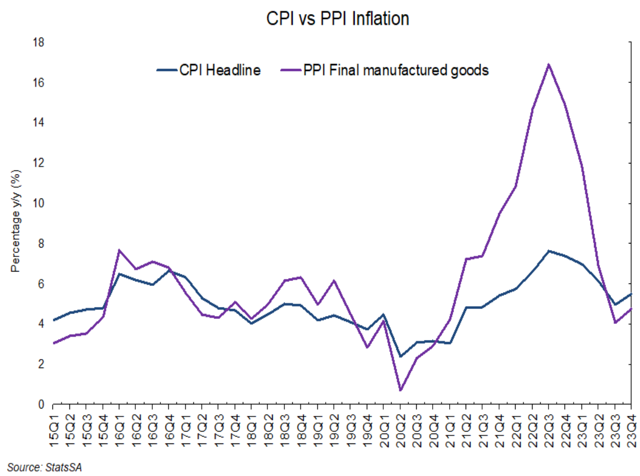
Despite significant signs of deterioration in consumer credit health, the ability of consumer spending to avoid weakening unduly might also have been assisted by resilience in employment. Employment grew by 4.9% y/y in Q4, way above GDP growth of 1.2%.

It appears as though, following the huge destruction of employment during the COVID-19 pandemic, businesses have attempted to replenish their workforces now that they find that economic activity is not collapsing completely.

Undoubtedly, the driving forces for the pickup in the BDI in Q4 were the improvements in GDP growth in both South Africa and the US. The impact of other macroeconomic variables on the BDI was relatively small.

There were minuscule changes in the differential between South African and US interest rates and between short- and longer-term interest rates domestically.

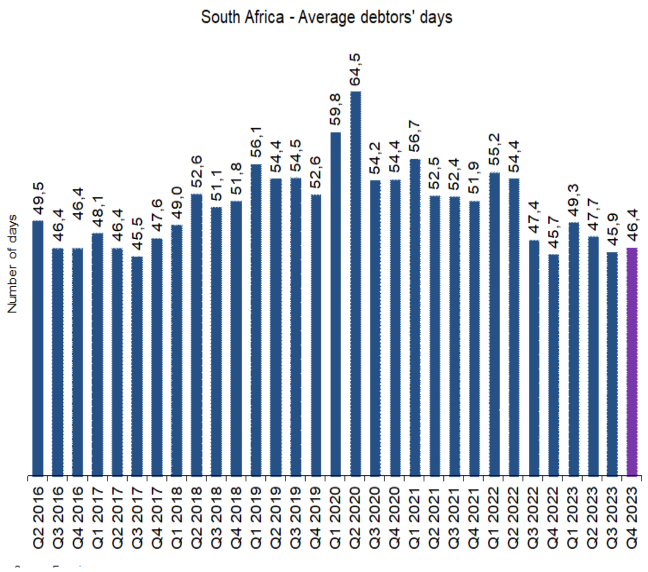
In addition, the differential between the PPI and CPI barely altered, suggesting a virtually unchanged contribution of profit margins to the BDI.



Business debt metrics in Q4 2023

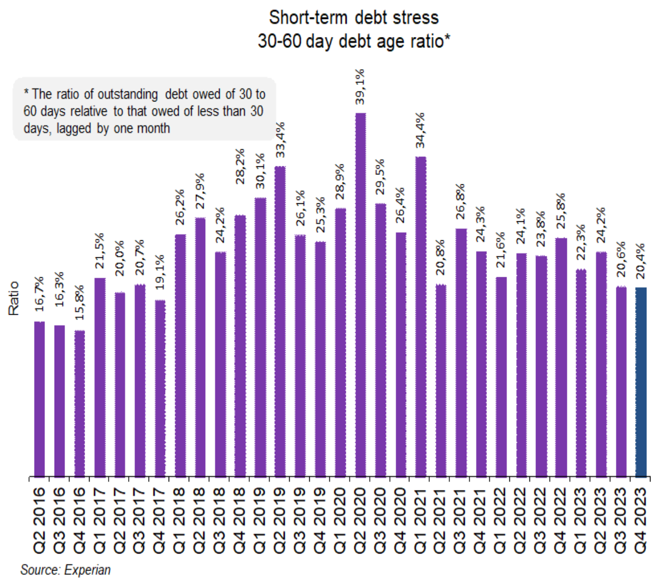
The impact of Experian data relating to outstanding debtors' days also reflected a relatively small change in Q4 of 2023 compared with Q3.

Overall, there was a slight increase in average outstanding debtors' days, to 46.4, from 45.9 in Q3.



However, the Q4 figure was still significantly down on the 49.3 and 47.7 level of average outstanding debtors' days in Q1 and Q2, respectively.

In respect of the **30 to 60 days ratio**[1], the ratio improved marginally in Q4, to 20.4, from 20.6 in Q3, but both these figures were down on the 22.3 and 24.2 ratios that prevailed in Q1 and Q2, respectively.



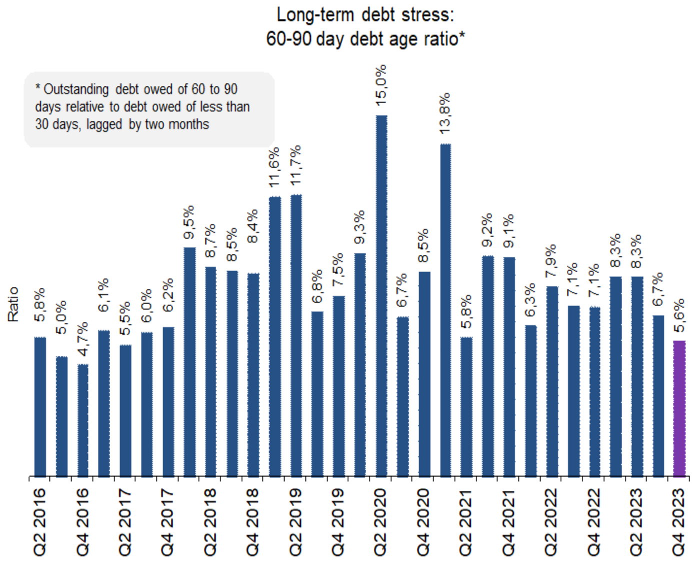
Similarly, the **60 to 90 ratio**[2] fell to 5.6 in Q4, down on the 6.7 of Q3 and 8.3 of both Q1 and Q2.

In other words, the make-up of outstanding debtors' days improved slightly during Q4, notwithstanding the

[1] *The ratio of outstanding debt owed of 30 to 60 days relative to that owed of less than 30 days, lagged by one month*

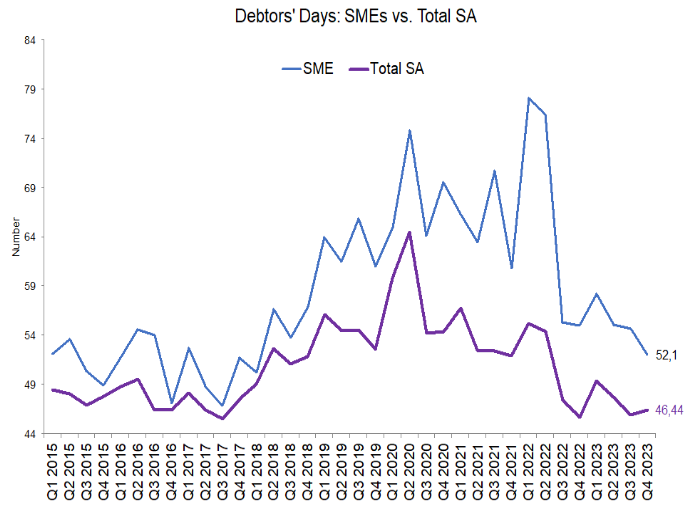
[2] *The ratio of outstanding debt owed of 60 to 90 days relative to debt owed of less than 30 days, lagged by two months*

marginal increase in overall outstanding debtors' days in that quarter.



Source: Experian

This contrasted with the slight increase in the overall average number of outstanding debtors' days between those two quarters.



In conclusion, the contribution of Experian data on outstanding debtors' days had a modest positive impact on the overall BDI, supplementing an equivalent modest boost to the BDI provided by macroeconomic factors.

As a result, the overall BDI improved moderately during Q4.

BDI by company size

What did emerge somewhat conspicuously in Q4 was a relative improvement in the business debt conditions of small businesses relative to the total sample of companies.

This pattern appears to have corresponded with the improvement in employment identified in Q4 and, for that matter, over 2023.

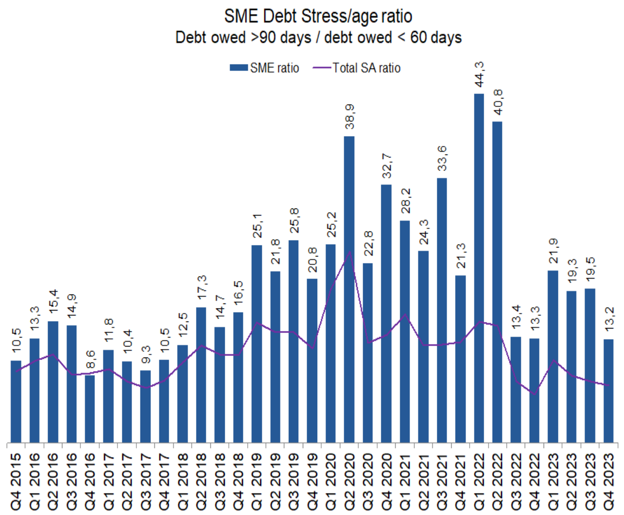
It would seem that business conditions stabilised for the SME sector following the devastation to small businesses during the COVID-19 pandemic.

The average number of outstanding debtors' days amongst small businesses declined to 52.1 in Q4, from 54.7 in Q3.

As a result, the SME debt stress ratio[3], declined sharply to 13.2 in Q4 from 19.5 in Q3. This was, in fact, the lowest measure of this ratio since Q1 2018, i.e., almost six years ago.

This is an encouraging outcome, reflecting a general stabilisation of South Africa's economic situation even when growth remains suboptimal.

It is apparent that the general private sector business environment has remained surprisingly resilient despite such significant headwinds.

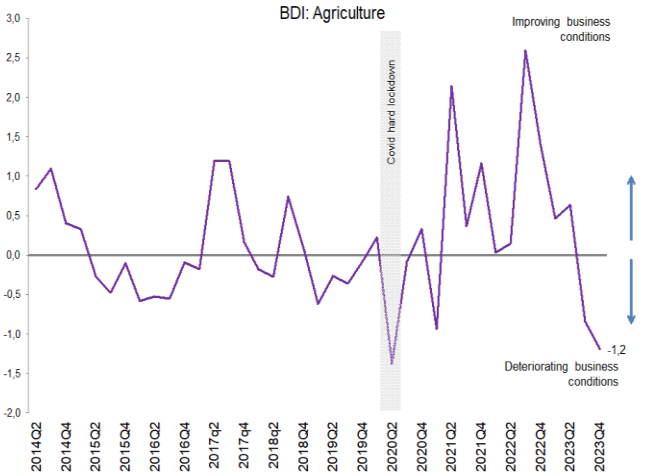


BDI by sector

[3] *The ratio of outstanding debt owed by SMEs of 90 to 120+ days relative to that owed of less than 60 days*

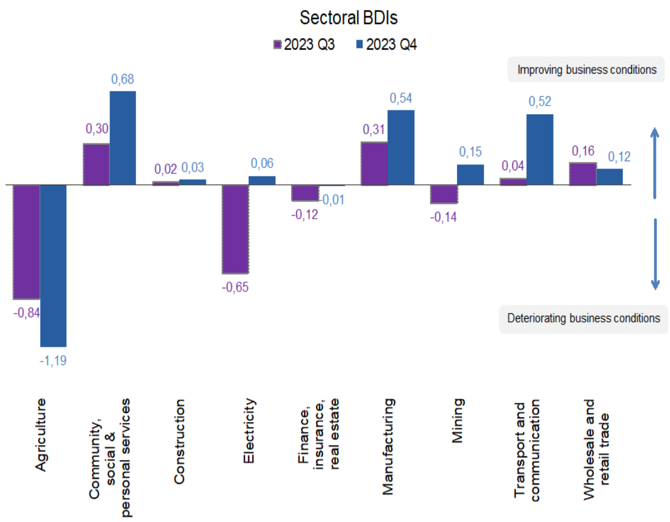
The trend of BDI by sector have been primarily influenced by the pattern of GDP growth reflected by each sector.

A sharp decline in agricultural production for a second consecutive quarter resulted in the BDI for this sector moving to even more negative levels than before.



Conversely, the improvements in the industrial sectors, namely mining, manufacturing and electricity, saw the BDIs for these sectors improving moderately.

In the case of mining and electricity, the BDIs went from slightly negative in Q3 to slightly positive in Q4. The same applied to the financial services sector. There was quite a substantial improvement in the BDI for transport and communications but very little change for construction, as well as the retail and wholesale trade and accommodation sector, whose performances had remained more or less stagnant during Q4.



Outlook

Preliminary information and forecasts relating to Q1 of 2024 suggest that there may have been a marginal further improvement in the BDI in the early part of the current year.

Indications are that domestic GDP growth may have fallen back marginally in Q1 and that the same thing may have happened to US growth.

However, the PPI inflation rate has shot up in the past few months, suggesting that the profit margins of businesses may have increased more recently. In addition, the hope exists that domestic and international interest rates will gradually decrease during the second half of the year in line with expectations of a modest decrease in inflation, providing some relief to beleaguered consumers.

More generally, the hope exists that the load-shedding level will be sustained on a downward path in the face of increased maintenance of coal-fired power stations, with the concomitant decrease in unforeseen outages. In addition, the coming on stream of renewable energy projects will also help to boost the electricity supply.

Conversely, the massive increase in the uptake of solar panels is reducing the demand for electricity by up to 4000 MW, or 13%, and in so doing, is relieving some of the pressure for load-shedding.

One is also hopeful of improved economic activity resulting from efforts being made under new leadership at Transnet to restore the utility's ability to handle the throughput of cargo at South African ports.

On a more general level, one is hoping that increased investment in renewable energy projects and grid transmission will assist in providing a further boost to overall economic growth in 2024, to take GDP growth to levels of 1% or more for the year compared with just 0.6% growth achieved in 2023.

There are clearly conspicuous risks in the economic outlook over the remainder of 2024 and beyond. Although there is anticipation of a reduction in interest rates at some stage, the timing thereof remains open to debate.

There are also significant global as well as domestic concerns related to higher public debt levels and how debt servicing costs are eating away at the ability of governments to improve service delivery, given such spending constraints.

In South Africa's case, the prospect of a general election fraught with uncertainty also acts as a deterrent to investment and overall business activity.

Even so, it is conceivable that the electoral outcome might usher in an environment that is more conducive towards tackling the economy's structural weaknesses and, in so doing, helps to launch a lift-off in the country's economic performance following more than a decade of declining economic growth and underperformance relative to most other comparable economies.

Explanatory notes regarding the Experian Business Debt Index

What is the Experian Business Debt Index?

The Experian Business Debt Index (BDI) is an indicator of the overall health of businesses, as well as the South African economy. It measures the relative ability for business to pay its outstanding suppliers/creditors (i.e. amounts owed to other businesses) on time and tracks macro-economic indicators that can impact on the ability of companies to pay their creditors.

A number of debtors and macro-economic variables are combined into a single indicator of business debt stress.
In other words, the BDI is a reflection of the overall health of businesses and the position of debt settlement between businesses in the economy.

How to interpret the index

The Experian BDI, as an indicator of the overall health of businesses, measures the relative ability of businesses to pay their outstanding creditors on time. It also incorporates trends in macroeconomic indicators, insofar as these impact on the ability of companies to pay their creditors. The index is constructed around a mean value of zero.
Values above zero indicate less business debt stress and values below zero indicate business debt stress.
Given the underlying data of the index, relative higher levels of debt indicate a weakening in the ability to pay outstanding creditors. Higher interest rates result in higher borrowing costs and an increase in business stress. Relatively higher production costs vs consumer costs decrease operating margins of business, while higher domestic and international growth could result in a better trading environment for businesses.

Measured by using principle components

The Experian Business Debt Index (BDI) is constructed using principal components analysis. This is similar to the St. Louis Fed's Financial Stress Index (STLFSI) and the Kansas City Fed's FSI (KCFSI) in the USA. The principal components analysis is a statistical method that is used to extract factors responsible for the co-movement of a group of variables. As such, it is assumed that business stress is the primary factor influencing the co-movement and by extracting the principal components, it is possible to build an index with a useful economic interpretation.

Variables included

The Experian Business Debt Index is made up of Experian business debtors' data and public domain data. Variables include the following:

- 30 – 60 debtor days' ratio (debt compared to initial amount invoiced 30 days ago);
- 60 – 90 debtor days' ratio (debt compared to initial amount invoiced 60 days ago);
- South Africa consumer inflation and producer inflation spread;
- Interest rate spread (Repo vs US Federal Fund rates);
- Interest rate spread (R157 vs Repo);
- Real SA GDP (year-on-year percentage change);
- Real US GDP (year-on-year percentage change).

No provision is made for any leads or lags in any of the variables.

Methodology used to construct the index

The index is constructed by first demeaning the individual indices - subtracting the index value from the index average and dividing it by the sample standard deviation (SD). The indices can now be expressed in the same units. Next, the method of principal components is used to calculate the coefficients of the variables in the EBSI. These coefficients are scaled so that the standard deviation of the index is 1. Lastly, each of the indices is multiplied by its respective adjusted coefficient.

When the index is updated quarterly, the values of the Experian Business Debt Index can change. This can occur either through a change in the coefficients (an updated re-estimation) or because of a change in the actual values of the variables in the sample. Because the data are demeaned and standardised, the value of the original sample will change as the sample mean and sample standard deviation of the underlying variables change.

About Experian

We are the leading global information services company, providing data and analytical tools to our clients around the world. We help businesses to manage credit risk, prevent fraud, target marketing offers and automate decision-making. We also help people to check their credit report and credit score and protect against identity theft. In 2016, for the third year running, we were named one of the "World's Most Innovative Companies" by Forbes magazine.

We employ approximately 17,000 people in 37 countries and our corporate headquarters are in Dublin, Ireland, with operational headquarters in Nottingham, UK; California, US; and São Paulo, Brazil.

Experian plc is listed on the London Stock Exchange (EXPN) and is a constituent of the FTSE 100 index. Total revenue for the year ended March 31, 2016, was US$4.6 billion.

To find out more about our company, please visit http://www.experianplc.com or watch our documentary, 'Inside Experian'.

About Econometrix

Econometrix is South Africa's largest independent macro-economic consultancy based in Johannesburg. We are privately owned and, therefore totally independent of any official organisation or pressure groups. Econometrix – which has a successful track record of more than 40 years - is committed to ongoing research and analysis of economic fundamentals thereby ensuring a sound basis for future business decisions. These services are provided through a range of complementary products to more than 150 South African and international organisations.

Our approach is to empower our clients with quality decision support intelligence and assistance regarding the economic and financial environment, and assist them in their strategic and financial planning processes. Our in-depth analysis of economic fundamentals aims to assist our clients in commanding the economic environment and identifying opportunities and risks.

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Next release date for the BDI: June 2024

For more detailed analysis on the debt stress by sector, Experian publishes the *Business Debt Sectoral Overview* report, please contact Taryn Stanojevic at Experian for more information.