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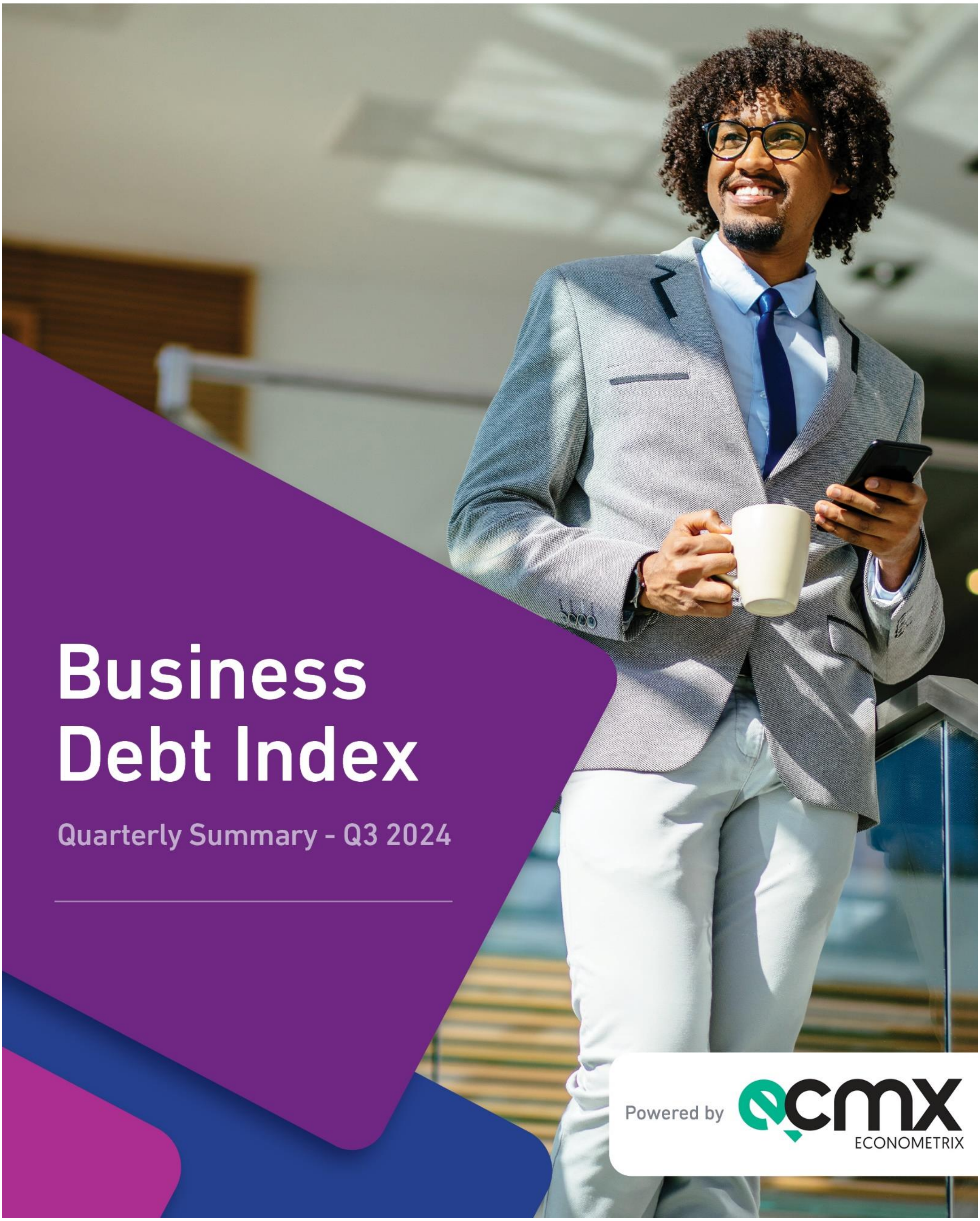

Business Debt Index

Quarterly Summary - Q3 2024

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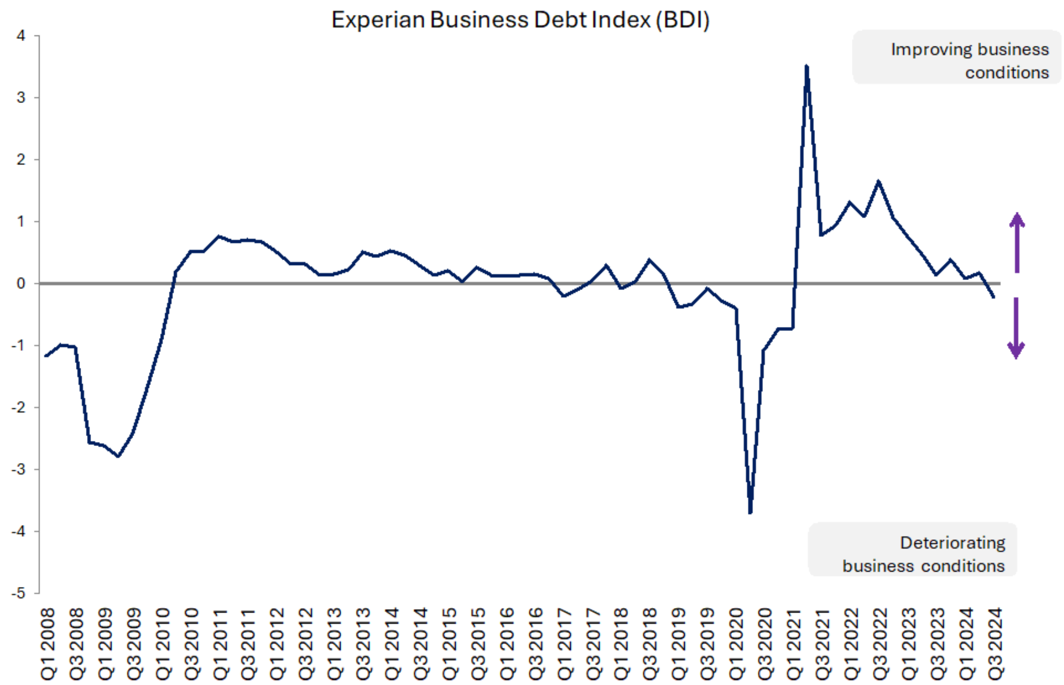
EXPERIAN BUSINESS DEBT INDEX (BDI) RESULTS FOR Q3 2024

Disappointing outcome for Experian BDI in Q3 highlights the deterioration in business finances

The Experian Business Debt Index (BDI) disappointed in Q3, declining to -0.20, reflecting deteriorating business debt conditions.

This contrasted with a positive BDI of 0.18 in Q2 (revised downwards), which reflected marginally improved business debt conditions.



	Q3 2023*	Q4 2023*	Q1 2024*	Q2 2024*	Q3 2024
Index >0= Improving business conditions <0 = Deteriorating business conditions	0,14	0,40	0,09	0,18	-0,20

** Revised*

Macroeconomic factors influencing Q3 2024

One had been encouraged by the improvement in the BDI in Q2 2024 to a positive figure from a near-zero one recorded in Q1.

One had attributed this improvement in the BDI for Q2 to the cessation of load-shedding at the end of March and a peaceful general election in May of Q2.

Despite the ANC losing its overall majority, relative peace prevailed in South Africa after the elections, resulting in the formation of a Government of National Unity (GNU).

The latter was seen to hold up a prospect of further structural reforms which might improve economic growth in the country.

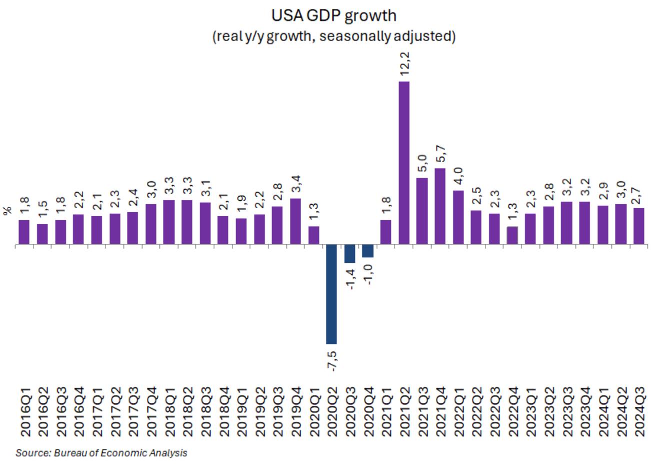
In particular, the newly formed GNU seemed better disposed to collaborating with the private sector to solve South Africa's economic problems than its predecessor.

There was also encouragement to be drawn from the decline in inflation in Q2 from Q1, which led to the expectation of a fall in domestic interest rates following more than a year of relatively punitive rates being held at their highest levels in 15 years.

These positive trends underlying the improved BDI in Q2 were expected to continue into Q3.

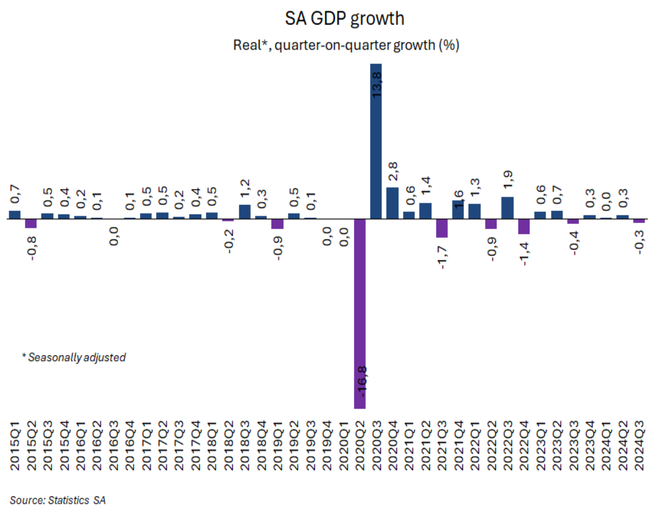
However, the marked decline in the BDI in Q3 to a negative reading of -0.20 was not foreseen and very disappointing.

GDP growth for the US slowed in Q3, but only marginally, from 3.1% in Q2 to 2.8% in Q3.



Additionally, load-shedding continued to be absent, optimism regarding structural reforms by a GNU remained relatively intact and business confidence indices improved, whilst inflation declined to its lowest level in four years in Q3 and interest rates were reduced twice (in July and September) by 0.25% on each occasion.

Therefore, the obvious factor contributing to the deterioration in the BDI in Q3 was a slump in Q3 GDP growth, to -0.4% q-o-q, from positive growth of 0.3% in Q2 (revised downwards by Stats SA from the 0.4% figure initially published).



Expectations had been that, even taking into account statistical factors, the economy would at least maintain the positive growth recorded for Q2 in Q3.

Instead, the principal reason for the surprise decline in GDP growth in Q3 was a horrific contraction of -29% q-o-q in agricultural GDP.

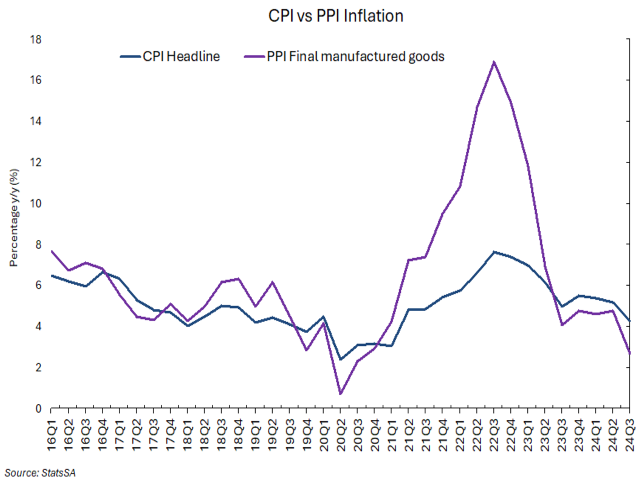
An intensification of drought conditions in the north-western parts of the country, coupled with floods in the Western Cape and diseases in the livestock industry, combined to see this massive slump in the agricultural sector.

This appears to have brought about a more cautious stance within the business community that saw the willingness and/or ability to pay off debts timeously deteriorating substantially.

There also seems to have been a second significant contributor to the slump in GDP growth in the form of a continuation of logistical bottlenecks in rail transport and processing of goods at the country's ports.

Indeed, the transport sector was the only meaningful sector other than agriculture to record negative growth in Q3. Unlike electricity generation, this structural impediment to growth has yet to be removed.

The apparent deterioration in business finances reflected in Experian BDI might also have been brought about by a sharp decline in producer price inflation, which exceeded the decrease in consumer price inflation, resulting in an imputed substantial diminution in profit margins.



The PPI inflation rate dropped sharply in Q3 to almost 2%, in contrast to the 4% average for the CPI inflation rate during the same period.

This contrasted with the PPI inflation rate exceeding the CPI inflation rate earlier this year.

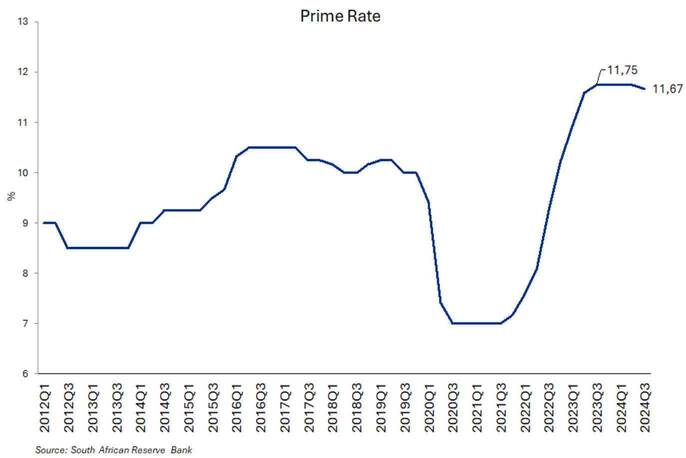
A steep decline in fuel prices resulting from a falloff in international oil prices and a strengthening of the Rand contributed towards this.

Even if it helped pave the way for some respite on the interest rate front, the strengthening of the Rand appears to have eroded profit margins.

Unlike GDP growth and the differential between PPI and CPI inflation, the interest rate differential between domestic rates and those abroad did not play much of a role in the movement of the BDI.

Effectively, the decline in South Africa's interest rates matched those recorded internationally.

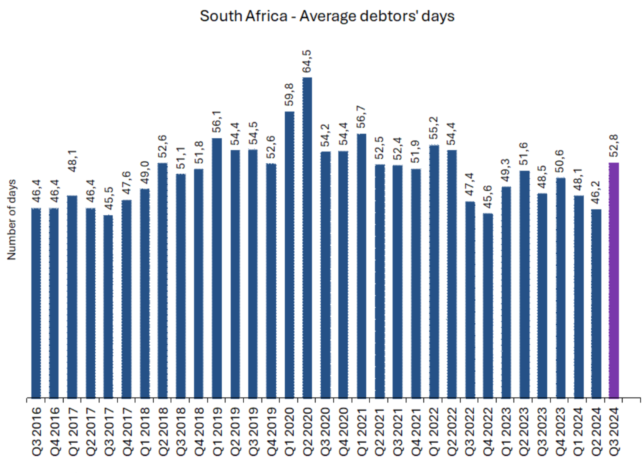
There was also minimal influence on the BDI from the ever-so-marginal change in the differential between short and long-term domestic interest rates.



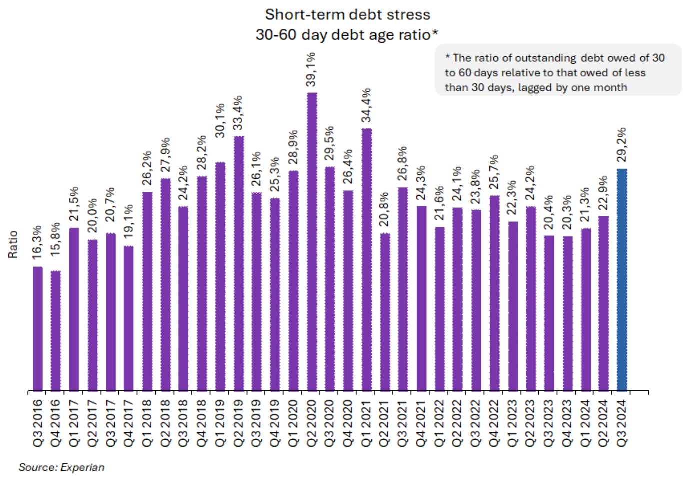
Business debt metrics in Q3 2024

In Q3, South Africa's GDP growth declined sharply, leading to a noticeable tightening in business debt conditions.

This was evidenced by a significant rise in the average outstanding debtors' days during the quarter. The average number of outstanding debtors’ days shot up from 46.2 in Q2 to 52.8 in Q3, the highest such number since Q2 of 2022.

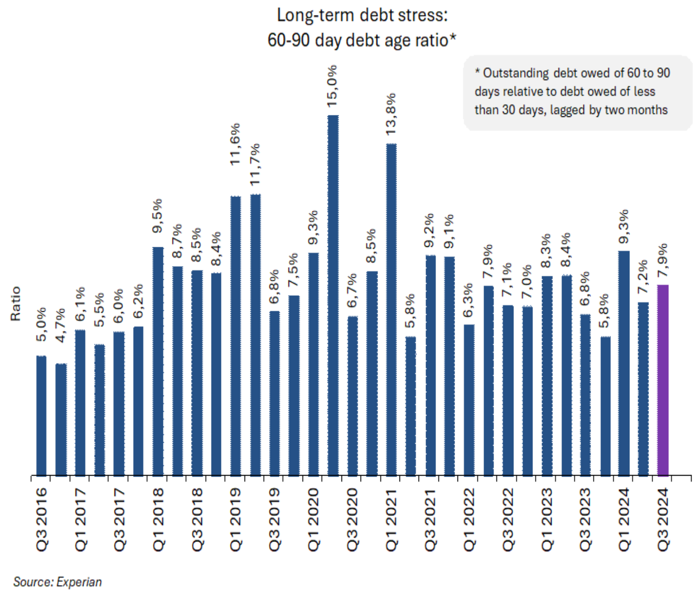


The ratio of debt outstanding for between **30 to 60 days ratio**[1] rose steeply from 22.9% in Q2 to 29.2% in Q3.



Similarly, the other key input of this nature making up the BDI, namely **60 to 90 ratio**[2], rose from 7.2% in Q2 to 7.9% in Q3.

This was not as dramatic an increase as the first ratio but did reflect an increased unwillingness or inability to pay off debt.



BDI by sector

What was particularly noticeable and suggestive of knock-on effects from agriculture's decline as well as logistical bottlenecks was the fact that there was no countervailing substantial improvement in economic growth in any of the other sectors.

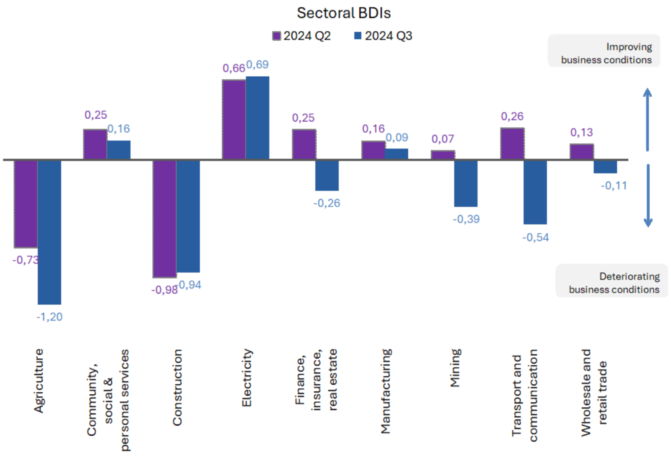
Whilst only agriculture and transport recorded negative growth rates in Q3, there was no meaningful upturn in GDP growth of any of the other sectors during that quarter.

This is also reflected in the fact that the BDI of all sectors, except for electricity and construction, recorded declines during Q3.

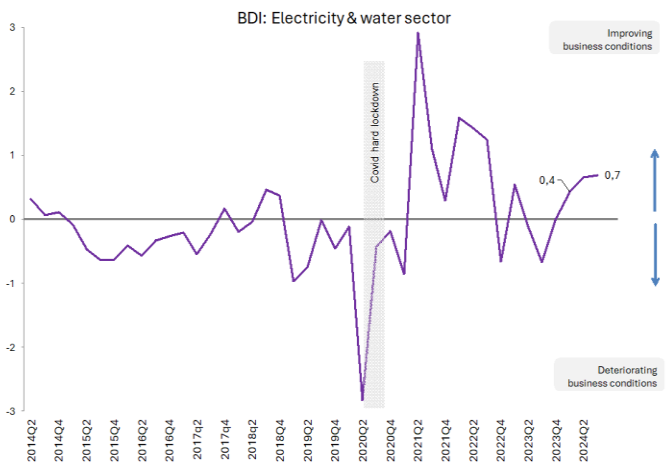
In six out of the nine sectors, the BDI went from positive to negative.

[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*



The improved BDI in electricity and construction simply reflected that both sectors had been extremely depressed in previous quarters due to load-shedding and a lack of investment. So, in Q3, one was comparing against a very poor base.



For the economy as a whole, the one marginal source of encouragement was that gross fixed capital formation improved in Q3, representing the first such improvement on a q-o-q basis in five quarters.

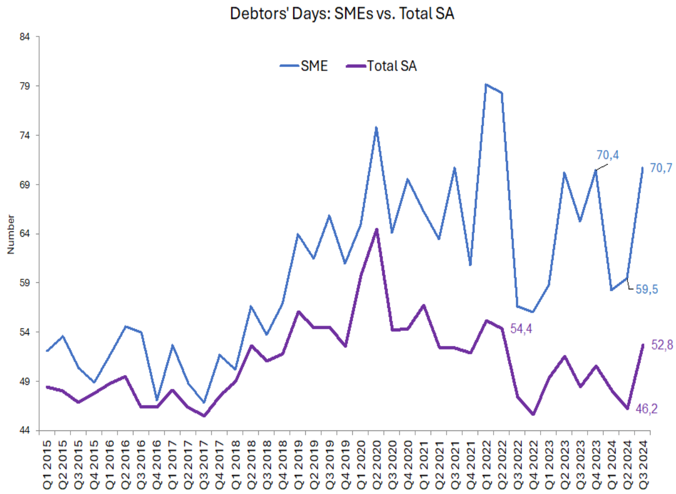
Even so, on a y-o-y basis, gross fixed capital formation was still heavily negative in Q3, at -4%. It is difficult to be excessively optimistic about the medium to longer-term prospects for economic growth when confronted with such weak data for fixed investment.

In addition, growth in consumption expenditure, although still positive, contracted from 1.2% in Q2 to just 0.5% in Q3.

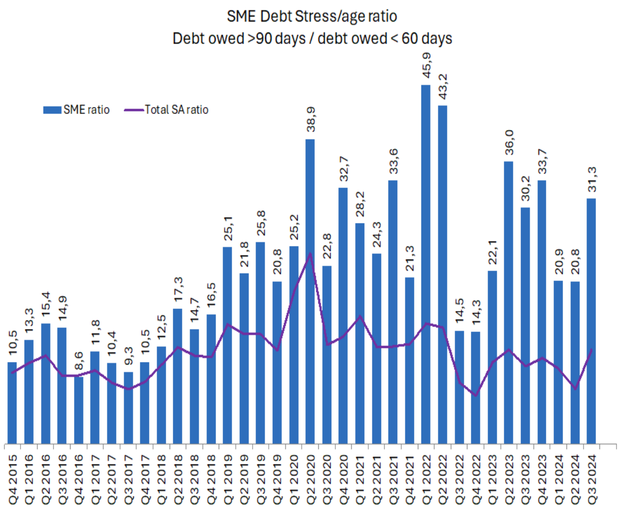
This was all the more disappointing given the decline in inflation and interest rates, which one might have thought would have boosted disposable income.

BDI by company size

The relatively broadly based softening in business debt conditions in Q3 was particularly prominent in respect of SMEs. The average number of outstanding debtors days in this segment of the economy increased sharply in Q3, to 70.7, from 59.5 in Q2.



This resulted in a deterioration in the SME debt stress ratio[3], from 20.8 to 31.3, between the two quarters. Once again, one suspects that there was a general tightening of margins, which was particularly severe in the small business segment.



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

One must also bear in mind that the cumulative effect of interest rates, which had been at their highest levels in 15 years over the past year, might have started taking its toll on business finances by the time Q3 arrived. Knock-on effects from the deterioration in agriculture and transport bottlenecks would almost certainly have also been felt.

Outlook

Looking ahead at Q4 and beyond, one should ordinarily remain relatively optimistic. The absence of load-shedding persists, and confidence regarding the ability of the GNU to pull the economy right remains in place, whilst inflation has fallen so much below original expectations that further interest rate reductions are foreseen.

In addition, September saw the introduction of a two-pot retirement scheme whereby members of retirement funds could access up to a third of those funds to assist them in retiring debt or helping to finance consumer spending that might have been impossible otherwise.

This ought to help boost consumer spending over and above that inspired by lower interest rates and increased disposable income through reduced inflation.

By all accounts, such funds have been taken up with alacrity mainly for spending purposes. Even so, the forecast BDI for Q4 is virtually unchanged from that in Q3.

Unfortunately, one cannot be overly optimistic about the recovery of agriculture. Drought conditions have, if anything, intensified.

Furthermore, attempts at improving the efficiency of the country's ports have been delayed by court action taken to stop a program to improve the port infrastructure, which Transnet had awarded to a Filipino consortium.

Water scarcity is intensifying partly because of weather conditions and partly because of poor infrastructure, especially in Gauteng and KwaZulu-Natal.

Internationally, uncertainty surrounding the effects of Donald Trump's accession to the presidency of the United States and the possible adverse effects this might have on trade and investment relations between South Africa and the United States is also not conducive to improved economic growth prospects.

At the same time, one cannot totally ignore the potential for a turnaround in South Africa's declining economic performance resulting from the formation of the GNU.

There is undoubtedly a risk of cynical perceptions about the economic future of South Africa turning out to be overly pessimistic.

It is just that one is unlikely to see a sudden and dramatic improvement in the actual level of economic activity emanating from this development. Changes to overcome structural weaknesses in economic performance are likely to take time.

In particular, one would like to see an acceleration in capital investment, which hitherto has been promised but has yet to be forthcoming.

More deep-seated structural impediments, such as the poor levels of educational outcomes, spatial inequalities and the relatively poorly developed estate of small business in South Africa, need to be addressed for the employment intensity of the country to improve and, through this, for overall economic growth to benefit more materially than has hitherto been the case.

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: March 2025

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.