UNISA university of south africa

momentum

Consumer Financial Vulnerability Index

QUARTER 2, 2017 RESULTS

Can we avoid the perfect storm?

The perfect storm is a rare combination of events or circumstances that create an unusually bad situation. During the second quarter of 2017 (Q2 2017), South African consumers witnessed a mix of adverse economic events and negative political developments. This translated into a sense that the perfect storm had started, and these perceptions are reflected in the CFVI Q2 2017 results.

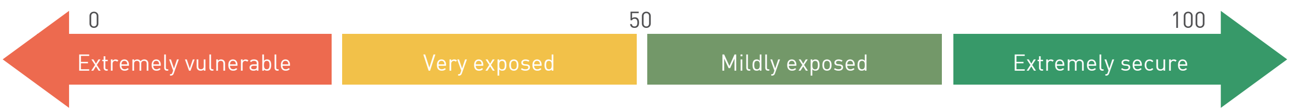
The second quarter of 2017 shows a dramatic deterioration in consumers' feelings about their personal financial situations. The CFVI declined sharply - from 52.3 points in Q1 2017 to 48.4 points in Q2 2017 - indicating that consumer finances are now very sensitive to changes. This means that even a slight mishap will have a severe impact on the average consumer's cash flow situation.

Table 1 provides an overview of the changes in the quarterly scores of the CFVI and its sub-components during Q2 2017 and the two preceding quarters. The measurement scale shows that consumers perceive their finances to be very exposed to influential events during this quarter, compared to mildly exposed in Q1 2017.

Moreover, this is the first time since the inception of the index in 2013 that all four sub-components are classified as very exposed. This means that compared to Q1 2017, consumers (in general) experience uncertainty regarding their income and believe that they can't purchase what they used to buy, are struggling to pay accounts/ debts and are unable to save sufficiently for retirement and other goals. Being very exposed in all four sub-components is a very dangerous situation because it means that consumers don't have a "fall-back" option, as is the case with being mildly exposed. When in the mildly exposed category, consumers are indicating that they feel like they will be able to juggle between components to make things work. The new status quo means consumers will have to consider giving up doing well in more than one sub-component to do better in another.

Table 1: Overview of CFVI and its sub-components (quarterly)

CFVI components	Q4 2016	Q1 2017	Direction	Q2 2017	Direction
Income	53.6	53.0	↓	49.0	↓
Expenditure	56.5	53.8	↓	49.1	↓
Savings	50.8	52.3	↑	48.8	↓
Debt servicing	50.4	50.2	↓	46.6	↓
Overall CFVI	52.7	52.3	↓	48.4	↓



Economic and political events that impacted consumers' cash flow during Q2 2017

"Political instability in South Africa was the main reason for the country's economic woes"

Various economic and political events affected consumer financial vulnerability during Q2 2017. According to a recently released Grant Thornton study, political instability in South Africa was the main reason for the country's economic woes during Q2 2017. This includes the removal of leaders in a large number of prominent government institutions, new allegations of state capture and corruption, as well as the subsequent downgrades of South Africa's sovereign credit rating by key ratings agencies during the end of Q1 2017. In this respect, Moody's and Standard and Poor's (S&P) have placed South Africa on a negative ratings outlook, suggesting that further downgrades are possible. Fitch's outlook remained stable.

In addition, following two consecutive quarters of negative economic growth in Q4 2016 and Q1 2017, the economy entered a technical economic recession in Q1 2017. Consumer and business confidence were also low during this quarter, mainly due to:

- Increases in personal income tax rates that became effective during the second quarter and had a negative impact on consumers' disposable income. These increases may have offset any modest, real increase in salaries and wages.
- A high unemployment rate that fuelled higher levels of uncertainty regarding job and income security, and dampened the outlook for new employment opportunities. With 112 000 fewer people employed during Q2 2017, the unemployment rate increased to 36.4%.
- A decline in credit extension by banks and retailers, which led to households having to adjust their purchasing and spending habits.

The outlook for a recovery is not promising. During the previous economic recession in 2009, the government was able to stimulate the economy by easing fiscal policy, while the South African Reserve Bank (SARB) had greater scope to cut interest rates. These remedies are not available to the authorities in the current situation, or at least not to the extent required to lift the economy out of its current predicament.

A closer look at the CFVI Q2 2017 Sub-indices

"On the up side, moderating consumer price inflation (CPI) has provided some relief to consumers"

Income vulnerability

The income vulnerability measure of the CFVI declined sharply to 49.0 points in Q2 2017 from 53.0 points in Q1 2017. This is the first time since Q3 2015 that consumers experienced very exposed emotions in terms of their income. This is reflected in the large proportion of negative responses in the following areas:

- **61%** disagreed that consumers' chances of retaining or obtaining employment during Q2 2017 improved.
- **67%** felt that consumers' income earning prospects did not improve over this period.
- **57%** disagreed that consumers' ability to acquire some income from friends or family improved over the second quarter.

Furthermore, high levels of unemployment and weak business activity led to greater uncertainty about employment opportunities and job security, which in turn contributed to greater income vulnerability.

Expenditure vulnerability

The expenditure vulnerability score of consumers has historically been the best performer among the CFVI sub-indices. Although consumers' expenditure vulnerability levels have not been below the 50-point mark (in the very exposed territory) since Q3 2013, during Q2 2017 the sub-index declined to 49.1 points. Indications from key respondents included that:

- **61%** felt that consumers were not able to improve their ability to make their normal purchases during the second quarter of the year.
- **64%** of respondents said that consumers were not able to stick to their expenditure budgets over this period.
- **69%** of key informants disagreed that consumers' expenditure hardly ever exceeded their income during the second quarter.

Considering the weaker consumer confidence over this period, subdued consumption expenditure during the second quarter of the year can be expected. Furthermore, the restrictive lending environment, which is illustrated through private sector credit extension to households remaining low at only 2.8% and 2.9% in May and June 2017 respectively, limits consumers' capacity to spend and forces them to adapt their spending habits. On the up side, moderating consumer price inflation (CPI) has provided some relief to consumers, but it may not be enough to lift consumer confidence or encourage increased household spending.

Savings vulnerability

The consumer savings vulnerability score also declined in the second quarter of 2017 to 48.8 from 52.3 in the previous quarter. This is the lowest score for savings vulnerability since Q3 2015. Growing pressures on consumers' wallets owing to, among other things, increasing personal income tax rates, declining employment, a persistently volatile rand exchange rate and little-to-moderate growth in salaries and wages, contributed to consumers' limited savings ability. This is reflected in the following results:

- **65%** disagree that consumers' ability to save improved during Q2 2017.
- **65%** disagree that consumers' ability to save for old age improved in Q2 2017.
- **68%** disagree that consumers were able to improve their savings for hardships/emergencies during Q2 2017.

Debt servicing vulnerability

The perceived recovery in consumers' debt servicing vulnerability in Q4 2016 and Q1 2017, where scores of 50.4 and 50.2 were achieved respectively, was short-lived as the score declined to 46.6 points in Q2 2017. This reflects a return to the very exposed category and is the lowest score for debt vulnerability since Q1 2014. The decline is reflected in the following results related to consumers' debt servicing capabilities:

- **69%** believed that consumers were not able to improve their ability to repay their outstanding debt during Q2 2017.
- **74%** disagreed that consumers' debt situation improved to such an extent over the period that they did not need to consider seeking assistance from someone else.
- **67%** felt that consumers needed to consider reducing their other commitments in order to repay their debt during the second quarter.

What is driving consumer financial vulnerability?

The increasing income and expenditure vulnerability of consumers during the past three quarters could be explained by various macro- and microeconomic dynamics. These include, among other factors, the following:

- The slump in GDP growth,
- Growing unemployment rates, and
- A less elastic relationship between GDP growth and employment, which means that there is a lower likelihood that GDP growth will be translated into increased employment opportunities.

The CFVI survey results also indicate that almost 35% of respondents feel that adverse economic conditions played a major part in consumer financial vulnerability during Q2 2017. Many mentioned the credit ratings downgrades, slow economic growth or the economic recession as the main reasons. Furthermore, 31% of respondents feel that unemployment contributed to consumer financial vulnerability. A further 25% of respondents indicated that consumers spend more than they earn and that inflation plays a significant role in constraining consumers' finances.

Some of the microeconomic reasons mentioned by key respondents as to why consumers are vulnerable with respect to their incomes and expenditures include the following:

- **68%** believe that consumers are generally financially illiterate.

- **70%** believe that consumers do not plan their finances in advance.
- **80%** believe that consumers do not demonstrate self-control when it comes to spending.
- **68%** believe that consumers are not able to adapt to changing financial conditions.
- **81%** believe that consumers struggle to expand their incomes.
- **77%** believe that consumers are not capable of managing their own finances.

Behavioural impact on the CFVI

A correlation analysis of the behavioural drivers of consumers' financial vulnerability outcomes was conducted. The results are summarised in table 2. The correlation coefficient (r*) reflects the relationship between consumers' financial vulnerability outcomes and a particular behavioural factor/driver. Any coefficient above 0 indicates a positive relationship, while the closer the coefficient is to 1, the stronger the relationship. It appears that the strongest determinants (where r* → 0.250) of the different CFVI sub-components are as follows:

- Income vulnerability: Consumers not being financially literate (r=0.335), consumers not living within their means (r=0.264) and consumers not being able to adapt to changing financial conditions (r=0.287)
- Expenditure vulnerability: Consumers not planning their finances in advance (r=0.331), consumers not living within their means (r=0.409), consumers not demonstrating self-control when it comes to spending (r=0.304), consumers using credit irresponsibly (r=0.303) and consumers not being sufficiently capable of managing their own finances (r=0.391)
- Debt-servicing vulnerability: Consumers not being financially literate (r=0.263), consumers not living within their means (r=0.308), consumers not demonstrating self-control when it comes to spending (r=0.255), and consumers not being sufficiently capable of managing their own finances (r=0.303)
- Savings vulnerability: Consumers not being financially literate (r=0.298), consumers not living within their means (r=0.343), consumers not being able to adapt to changing financial conditions (r=0.292), consumers not being good at expanding their incomes (r=0.251) and consumers not being sufficiently able to manage their own finances (r=0.317)

**Pearson's Product Moment Correlation Co-efficient*

Conclusion

During Q2 2017, consumers felt the greatest pressure on their personal financial situation since the inception of the CFVI. During this period, consumers felt very exposed in terms of their income, expenditure, savings and debt servicing. This means that they are very uncertain as to whether they will be able to comply with all their commitments.

Being very exposed on each sub-component of their cash flow is a very dangerous situation, as it means consumers have to consider giving up doing well in more than one sub-component (e.g. savings and debt servicing) in order to do better in another (expenditure). Under these conditions, consumers need to be very careful when making financial decisions.

Furthermore, employers need to be sensitive to the current situation and avoid hasty short term decisions which may have significant negative implications for the financial wellness of their business, employees and the economy as a whole. There are specific steps employers wishing to decrease employees' financial vulnerability can take, in order to improve financial literacy, budgeting practices and other financial management behaviours across their workforce.

Table 2: Strength of vulnerability outcomes determinants

	Income vulnerability	Expenditure vulnerability	Debt serving vulnerability	Savings vulnerability	CFVI
Consumers are generally financially literate.	0.335	0.241	0.263	0.298	0.363
The actions of consumers reflect that they plan their finances in advance.	0.207	0.331	0.243	0.211	0.314
Consumers are generally living within their means.	0.264	0.409	0.308	0.343	0.419
Consumers first shop around before deciding on a specific product/service.	0.023	-0.010	0.109	-0.017	0.032
Consumers have access to financial products (such as inter alia savings accounts, insurance and credit cards) and advice.	0.018	0.183	0.193	0.209	0.188
Consumers demonstrate self-control when it comes to spending.	0.062	0.304	0.255	0.238	0.269
Consumers demonstrate self-control when it comes to taking on more debt.	-0.051	0.126	0.040	-0.024	0.026
Consumers are able to adapt to changing financial conditions.	0.287	0.222	0.087	0.292	0.286
Consumers generally consider the risks when taking on more credit.	0.007	0.141	-0.038	0.009	0.037
Consumers are responsible in their use of credit.	0.079	0.303	0.236	0.231	0.266
Consumers are good at expanding their incomes.	0.118	0.222	0.225	0.251	0.257
Consumers are sufficiently capable to deal with their own finances.	0.157	0.391	0.303	0.317	0.368

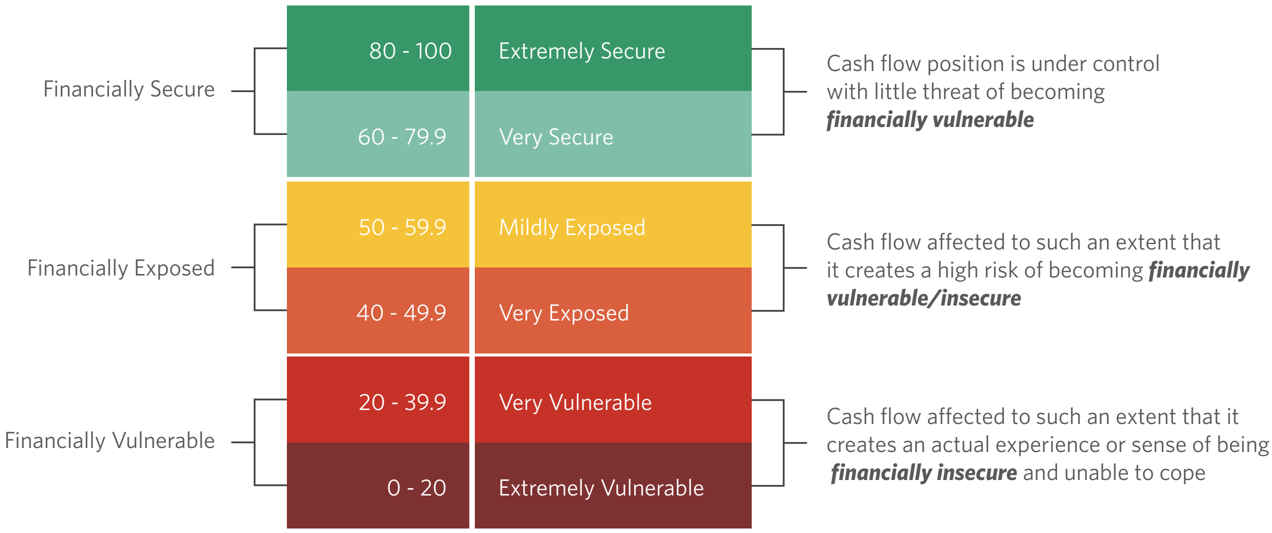
Table 3: Scores of the CFVI and its sub-indices

This reflects the impact of political, economic, social & institutional volatilities & uncertainties experienced by consumers.

Table 3 provides the long-term trend of the CFVI and its sub-indices. It is clear from this table that the consumer financial vulnerability index scores on all the sub-indices was volatile during the 2013 to 2017 period, with vulnerabilities increasing during the period Q4 2016 to Q2 2017. This reflects the impact of political, economic, social and institutional volatilities and uncertainties experienced by consumers. Moreover, these volatilities are exacerbated by the consumers' lack of financial capability reflected in the correlations illustrated in table 2. This mix of macro- and micro-instabilities on the one hand, and consumers' weak financial capabilities on the other hand, makes it inherently very challenging to improve consumer financial vulnerability over the longer term.

Year	Date	Income	Expenditure	Savings	Debt servicing	Overall CFVI
2013	Q1	49.60	51.02	49.60	54.04	51.07
	Q2	43.43	52.35	44.38	53.82	46.67
	Q3	42.11	45.22	44.78	51.58	45.92
	Q4	51.28	53.53	49.96	53.71	52.03
2014	Q1	51.00	52.88	50.23	46.60	50.17
	Q2	47.71	54.61	51.73	48.98	50.18
	Q3	50.98	54.27	51.97	48.41	51.41
	Q4	51.42	53.53	50.52	49.57	51.22
2015	Q1	52.09	56.70	52.69	49.93	52.74
	Q2	52.08	52.48	51.49	47.00	50.76
	Q3	47.23	54.96	48.49	47.77	45.96
	Q4	50.23	53.18	51.67	48.71	50.95
2016	Q1	50.50	52.62	52.13	49.86	51.28
	Q2	52.54	52.34	49.77	48.18	50.71
	Q3	51.50	54.73	52.16	49.89	52.07
	Q4	53.60	56.53	50.83	50.40	52.71
2017	Q1	53.02	53.78	52.32	50.16	52.32
	Q2	48.95	49.12	48.83	46.55	48.36

Figure 1: Measurement scale of consumer financial vulnerability index



ABOUT THE INDEX

The results of this release of the CFVI stem from research conducted by Unisa on behalf of Momentum.

The term 'Consumer Financial Vulnerability' implies that consumers experience a sense of financial insecurity or an inability to cope financially. In essence, the CFVI is an index that identifies the specific financial sub-component(s) that consumers on average feel are causing stress to their cash flow positions. Therefore, it provides a window into the psyche of consumers and how vulnerable they are feeling with regards to their income, expenditure, savings, and debt servicing capabilities. Insights into consumers' financial positions are vital to determine the extent to which economic growth and government programmes translate into improved financial stability of consumers. As a quarterly indicator, the CFVI fills an important information gap in South African data on consumer finances as viewed by consumers in the sense that it regularly provides updates as to the state of consumers' financial vulnerability. The results of this release of the CFVI stem from research conducted by Unisa on behalf of Momentum. The results of this release of the CFVI are based on a selection of approximately 100 key informants from relevant industries (including credit industry institutions, retailers providing credit and municipalities) that are able to gauge consumers' financial perceptions.

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