Box 1 A trend analysis of South Africa's credit extension pre- and post-COVID-19[1, 2]

Trends in the pace of expansion in credit extension to households and corporates are influenced by changes in the repurchase (repo) rate[3], the prevailing economic conditions and other developments, such as the onset of the coronavirus disease 2019 (COVID-19) pandemic, as mirrored by trends in gross domestic product (GDP) and the business cycle[4].

This box focuses on the pre- and post-COVID-19 trends in both nominal and real total loans and advances extended to the domestic private sector[5] and whether growth in credit extension has returned to pre-COVID-19 levels.

During the pre-COVID-19 period, total nominal loans and advances increased by 22.5% between January 2016 and December 2019, representing annual average growth of 5.8% from 2016 to 2019. This period was characterised by a relatively stable repo rate of 7.00% effective from March 2016 and 6.50% effective from July 2019, and also a transition of business cycle phases. During the COVID-19 period, credit extension slowed to 1.3% between March 2020 and September 2021 when the exogenous sudden stop in economic activity was followed by a gradual relaxation of restrictions.

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1 This box relates to the credit extension by all monetary institutions statistics on page S–22 in this edition of the *Quarterly Bulletin (QB)*, as adjusted to account for seasonality. The monetary sector comprises the following monetary institutions: commercial banks, mutual banks, the South African Reserve Bank (SARB), the Land Bank and Postbank.

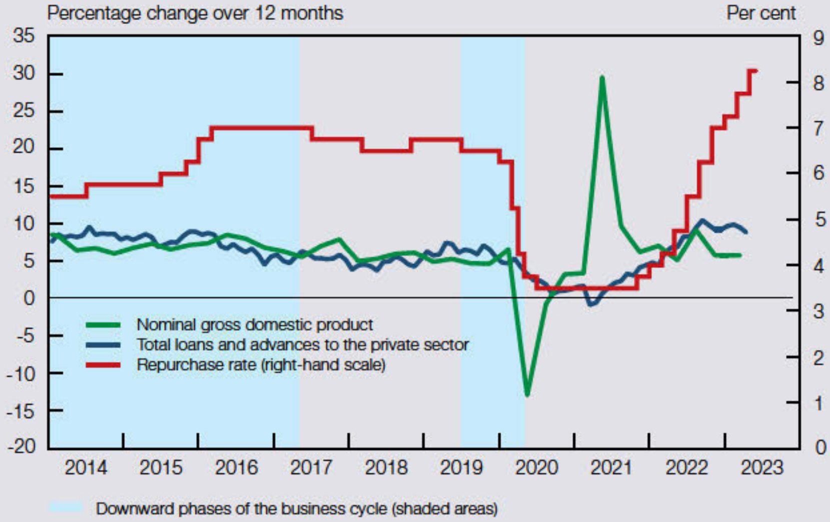
2 All trends were estimated by regressing the seasonally adjusted statistics along a linear trend with a constant term. The pre-COVID-19 sample covered January 2016 to December 2019 and the post-COVID-19 sample October 2021 to April 2023. Most of the COVID-19 lockdown restrictions curtailing economic activity were lifted on 1 October 2021 when they were adjusted to level 1 followed by the termination of the state of disaster as from 5 April 2022.

3 The repo rate is an interest rate determined by the Monetary Policy Committee of the SARB at which private sector banks are allowed to borrow money from the SARB. Banks will then pass along the interest rate to their clients but with adjustment to reflect, among other things, the riskiness of the client, the level of surety provided and the period of the loan.

4 The SARB determines reference turning points in the business cycle in terms of the growth cycle definition, which represent the fluctuations around the long-term trend of aggregate economic activity. The SARB's business cycle chronology, available on page S–164 in this edition of the *QB*, therefore represents reference turning point dates that distinguish between upward phases (periods when the rate of growth in aggregate economic activity either matched or exceeded the long-term trend) and downward phases (periods when aggregate economic activity either contracted or increased at a slower pace than its long-term trend). For a discussion of the most recently identified reference turning points, see 'The South African business cycle from 2013 to 2022' in the March 2023 edition of the *QB*, available at https://www.resbank.co.za/en/home/publications/publication-detail-pages/quarterly-bulletins/articles-and-notes/2023/the-south-african-business-cycle-from-2013-to-2022.

5 Total loans and advances to the private sector include instalment sale credit and leasing finance, mortgage advances as well as other loans and advances, the last-mentioned of which represent general loans, overdrafts and credit card advances.

Total loans and advances, nominal gross domestic product and the repurchase rate



Sources: Stats SA and SARB

During the post-COVID-19 period, total nominal loans and advances increased briskly by 13.2% from October 2021 to April 2023 despite the increases in the repo rate, with year-on-year growth accelerating from 3.1% to 8.8% over this period.

During these three periods, the drivers of total loans and advances to households and corporates differed over time. In the pre-COVID-19 period, the demand for loans and advances by both the household and the corporate sector was relatively strong. For example, growth in general loans to households by private sector banks accelerated steadily from a low of 2.7% in December 2017 to 12.1% in September 2019, driven by a few key factors. A transition from secured credit to credit sources with no collateral requirement was driven by more conservative and generally risk-averse credit underwriting criteria. However, when the maximum lending amount that consumers could borrow without collateral was raised, in an attempt to counteract the loss of supply through risk adjustment, consumers started to utilise unsecured loans for purposes that they would otherwise have met with secured loans. In addition, banks improved their lending efficiency through simplified online loan origination and digitised processes, thereby increasing clientele. Growth in loans and advances to the corporate sector also maintained a steady pace, with instalment sale credit notably leading the way. However, growth in general loans to companies levelled off somewhat in 2018 and 2019 amid progressively slower economic growth.

The COVID-19 lockdown restrictions resulted in an abrupt and widespread slowdown in growth in most of the subcategories of credit extended to both households and corporates. A variety of measures was subsequently introduced to ease liquidity constraints in the domestic financial markets[6] while substantial interest rate relief was provided to support credit extension and to ease the repayment burden. In addition, the COVID-19 Loan Guarantee Scheme[7] was introduced to provide financial support and relief to small and medium enterprises (SMEs) as these enterprises are estimated to account for more than 90%[8] of formal businesses. However, an aversion to increased exposure to debt led to only a small disbursement of loans under this scheme. Several commercial banks also offered relief measures to households and corporates, ranging from three-month payment holidays to loan term revisions and reduced payment options.

The demand for credit was affected by several factors, such as successive waves of COVID-19 infections and related restrictions, the civil unrest in Gauteng and KwaZulu-Natal in July 2021 and the 2022 floods which impacted on operations at the Durban port and resulted in renewed supply chain disruptions and shortages of raw materials. These developments impacted on the corporate sector in particular, and the overall contraction in the outstanding balance of its loans and advances caused the nominal value of total loans and advances to the private sector to decline to well below the long-term pre-COVID-19 trend, as companies contribute about 50% to the total.

The post-COVID-19 period has been marked by a rapid increase in the nominal value of total loans and advances to the private sector. An extension of the pre-COVID-19 trend shows that the post-COVID-19 trend

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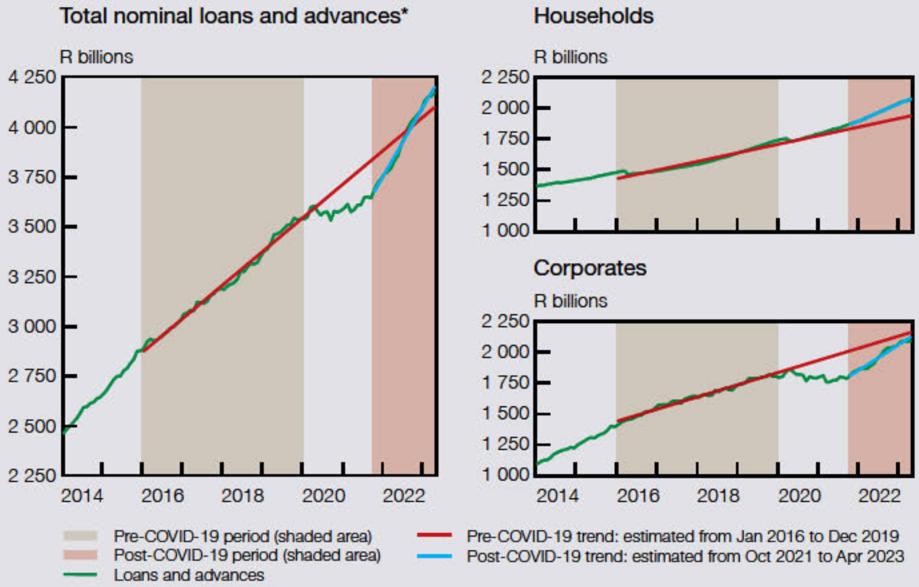
6 See 'Note on South Africa's liquidity measures in response to the COVID-19 pandemic' in the June 2020 edition of the *QB*, available at https://www.resbank.co.za/content/dam/sarb/publications/quarterly-bulletins/articles-and-notes/2020/10089/Note-on-South-african-liquidity-measures.pdf, as well as 'Box 3: Unpacking special liquidity measures in response to the COVID-19 pandemic' in the March 2022 edition of the *QB*, available at https://www.resbank.co.za/en/home/publications/publication-detail-pages/quarterly-bulletins/boxes/2022/March/UnpackingspecialliquiditymeasuresinresponsetotheCOVID19pandemic.

7 See the SARB media release at https://www.resbank.co.za/en/home/publications/publication-detail-pages/media-releases/2020/9931.

8 See the McKinsey report at https://www.mckinsey.com/featured-insights/middle-east-and-africa/a-credit-lifeline-how-banks-can-serve-smes-in-south-africa-better.

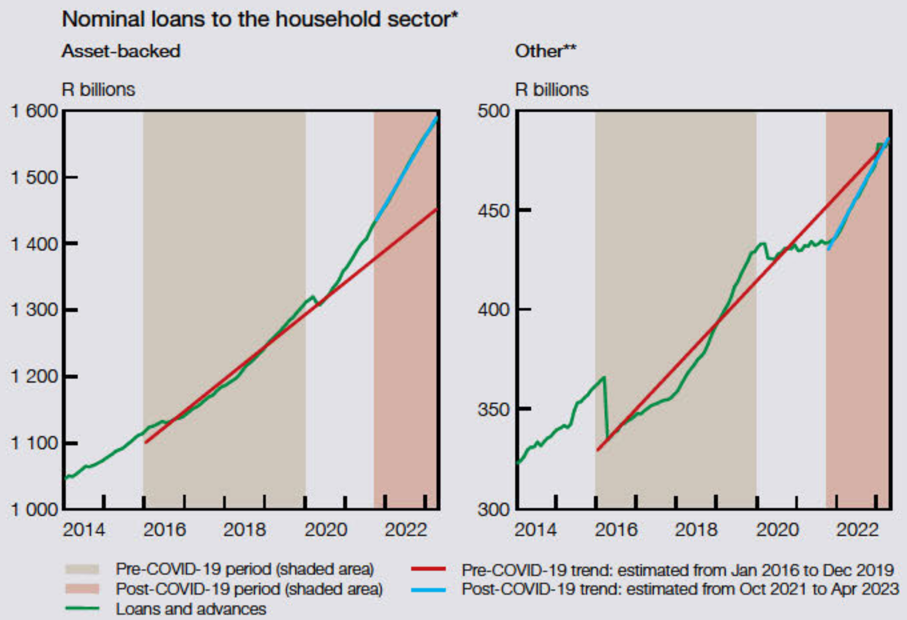
has become steeper and has surpassed the pre-COVID-19 trend. Loans and advances to the household sector generally maintained steady growth throughout the COVID-19 period, and the outstanding balance barely deviated from its long-term pre-COVID-19 trend, before accelerating during the post-COVID-19 period to exceed the pre-COVID-19 trend. Loans to the corporate sector were significantly affected during the COVID-19 period, and their post-COVID-19 recovery is still falling short of the pre-COVID-19 trend. The marked increase in the outstanding nominal value of total loans and advances to the private sector during the post-COVID-19 period occurred notwithstanding a 425 basis points increase in the repo rate between 18 November 2021 and 31 March 2023.



* Seasonally adjusted

Source: SARB

The nominal value of asset-backed loans[9] to the household sector, which accounts for about 76% of household credit, remained fairly robust throughout the COVID-19 period compared to the pre-COVID-19 period. This could most likely be attributed, at least partially, to historically low interest rates during the COVID-19 period, which supported the purchases of vehicles and homes by first-time buyers as well as the upgrading of existing properties in the wake of the adoption of work-from-home practices.



* Seasonally adjusted

** Other loans include general loans, overdrafts and credit card advances

Source: SARB

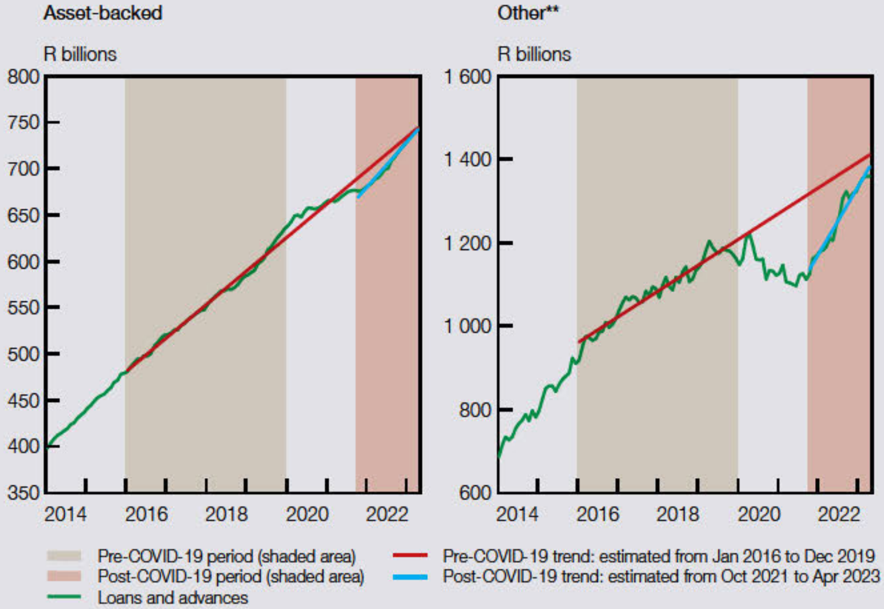
9 Asset-backed loans comprise mortgage advances as well as instalment sale credit and leasing finance.

The post-COVID-19 trend in the outstanding nominal value of these loans, which has increasingly been exceeding the pre-COVID-19 trend since the end of 2020, signals continued strength in demand for asset-backed loans by the household sector. This sharply contrasts with the post-COVID-19 trend in households' demand for other loans[10]. These loans, which are mostly unsecured, account for, on average, 24% of total loans and advances to households. At the onset of the pandemic, other loans contracted to below their pre-COVID-19 trend as households' ability to spend was curtailed by not only strict lockdown measures, but also the pandemic's impact on employment and the loss of income. During the subsequent post-COVID-19 period, household demand for other loans, mostly general loans, gradually returned to the pre-COVID-19 trend of expansion.

The nominal value of asset-backed loans to the corporate sector, which accounts for roughly 35% of total corporate sector credit, moved slightly above its pre-COVID-19 trend at the onset of the pandemic but later moderated to below it. Asset-backed corporate credit subsequently returned to its extended pre-COVID-19 trend in March 2023. Other loans, which account for about 65% of corporate sector credit, contracted markedly during the COVID-19 period. All the subcategories, in particular general loans to non-financial companies (about 68% of their other loans), remained suppressed throughout 2020 and 2021 due to heightened uncertainty and low business confidence, which resulted in caution to take on new debt and a reluctance to indulge in fixed capital formation.

Since early 2022, there has been a noticeable rebound in general loans, in particular from non-financial companies involved in consumer goods manufacturing, mining and resources, agriculture and retail trade for operational and working capital purposes along with investment in renewable energy generation, such as participation in the Renewable Energy Independent Power Producer Procurement Programme. The steepness of the post-COVID-19 trend has exceeded that of the pre-COVID-19 trend and could soon surpass it.

Nominal loans to the corporate sector*

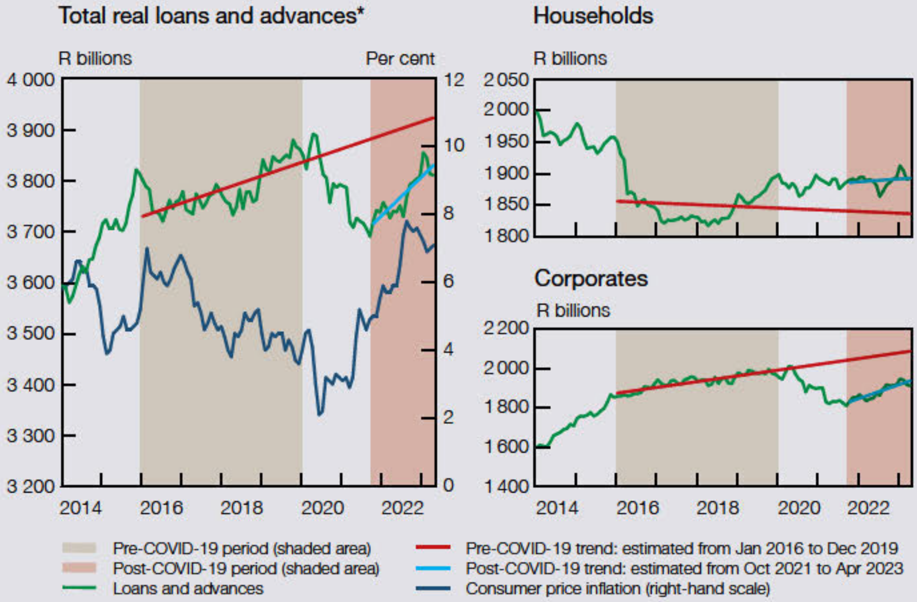


* Seasonally adjusted
** Other loans include general loans, overdrafts and credit card advances
Source: SARB

Due to the impact of inflation, it is also important to analyse credit demand in real terms.[11] Rising inflationary pressures globally, aggravated by Russia's invasion of Ukraine in February 2022, were also evident domestically when consumer price inflation breached the upper limit of the inflation target range of 6.0% in May 2022, mainly due to record-high fuel prices. Most central banks, including the South African Reserve Bank (SARB), subsequently tightened monetary policy to curb the rising inflation. The repo rate increased from 3.50% on 18 November 2021 to 7.75% on 31 March 2023, increasing borrowing costs to their highest level since May 2009. The real value of total loans and advances to the private sector contracted sharply at the onset of the pandemic, with the post-COVID-19 period showing a steep increase, although still well below the pre-COVID-19 trend of expansion. By contrast, real loans and advances to the household sector

10 Other loans are not necessarily asset-backed and comprise general loans, overdrafts and credit card advances.
11 Credit in real terms refers to the nominal value of loans and advances as adjusted for consumer price inflation.

trended downward during the pre-COVID-19 period before increasing during the COVID-19 period and slightly further thereafter. The corporate sector's trend in real loans and advances was broadly similar to the trend in its nominal loans and advances. However, the recovery to the pre-COVID-19 level in real terms will likely take longer than that anticipated in nominal terms.



* Seasonally adjusted

Sources: Stats SA and SARB