CONSUMER AND RETAIL BAROMETER

-HOUSEHOLD SECTOR FINANCIAL STRENGTH

FNB Property Barometer

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SARB Quarterly Bulletin still points to positive developments in terms of lowering Household Sector Indebtedness. But a savings rate improvement continues to take its time.

INDEBTEDNESS SITUATION IMPROVES, BUT ALREADY-DISMAL SAVINGS TAKES A STEP BACK

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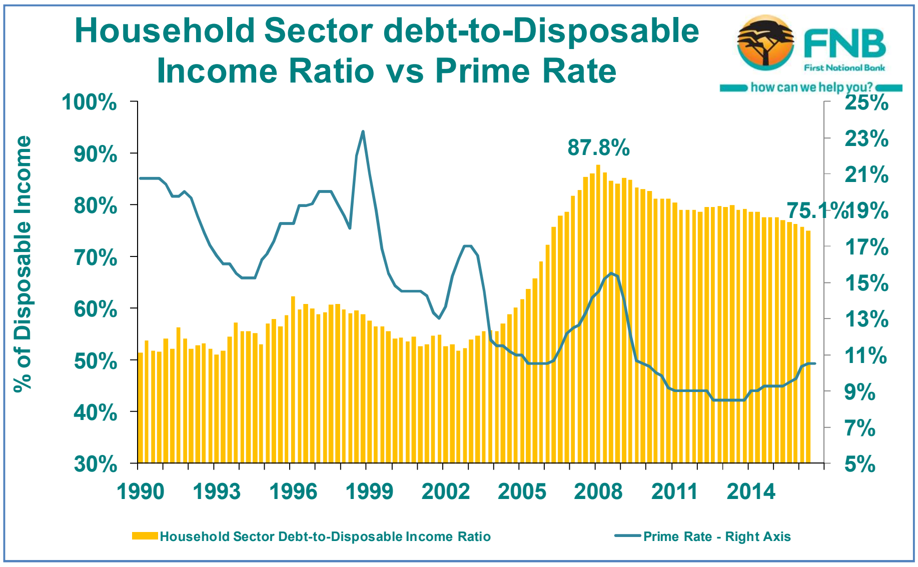
The SARB Quarterly Bulletin continues to point to a dismal savings rate, the glaring weak point in consumer finances. But although the 2nd quarter data saw it take a slight step backwards, we remain of the belief that mild improvement is not far away.

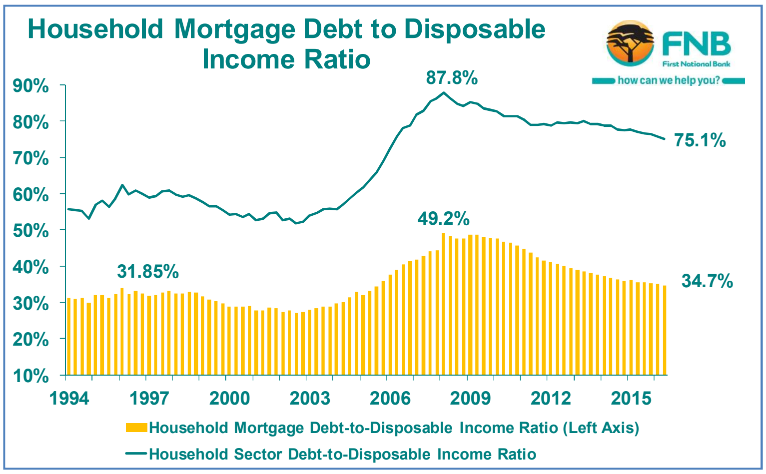
The SARB (SA Reserve Bank) Quarterly Bulletin released today completes the Household Sector Finance picture for the 2nd quarter of 2016. With economic growth hovering not far from zero, formal sector employment decline, and an already lengthy period of extremely weak consumer confidence behind us, we have believed for a while that the environment exists for a more cautious Consumer, and some improvement in the Household Sector Savings Rate.

This certainly does not mean that we expect the savings rate to "shoot the lights out". But we believe that a meaningful improvement in this dismal savings rate is both desirable and to be expected. Some may question this expectation, arguing that tougher economic and financial times make it more difficult to save. Theoretically, this is a valid argument. But in practice it seems that consumers make more effort to save when times get tough, and achieve some mild success. Fear drives greater caution.

On the Household Sector Indebtedness front, the good news has been ongoing for some years now, and it continued in the 2nd quarter of 2016. We have observed a gradual decline in the Household Debt-to-Disposable Income Ratio, all the way from a historic high of 87.8% as at the 1st quarter of 2008, to 75.7%by the 1st quarter of 2016. The 2nd quarter stats just out show a further decline in this percentage to 75.1%. It is now quite possible that this percentage can decline to below 70%, a healthy development which would mean that the Household Sector's vulnerability to economic and interest rate shocks is greatly reduced since 2008.



The SARB's gradual interest rate hiking since early-2014 has had a very positive impact in terms of keeping the Debt-to-Disposable Income Ratio on its declining trend.

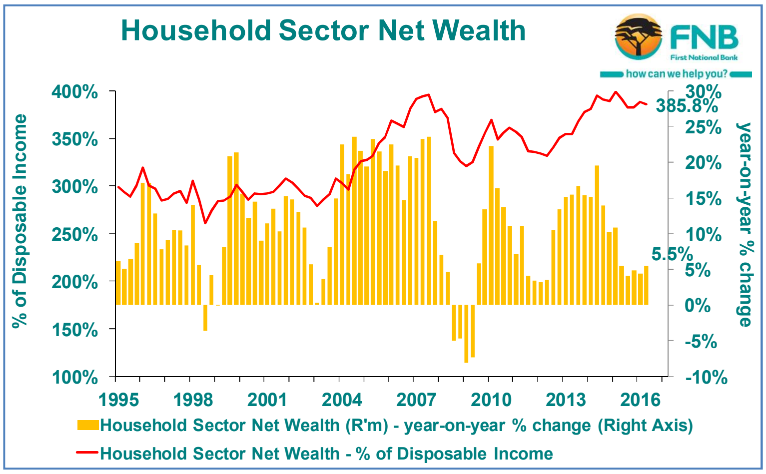


The dominant driver in this decline in the Debt-to-Disposable Income Ratio has been a steady decline in Household Sector Mortgage Advances in real terms (when adjusted for inflation), causing a simultaneous multi-year decline in the Household Mortgage Debt-to-Disposable Income Ratio. From a historic high of 49.2% as at the 1st quarter of 2008, the Household Mortgage Debt-to-Disposable Income Ratio has declined all the way to 34.7% by the 2nd quarter of 2016, a further decline from the 1st quarter's 35.1%

With regard to indebtedness, therefore, some meaningful progress has been made.

Things continue to be more "sticky" on the savings front, however. Some minor Improvement has come slowly, but the 2nd quarter was a step back after prior quarters of improvement.

The Household Savings rate has long been in desperate need of significant improvement, especially given that the fastest growing numbers in SA's various age cohorts are in their 50s and 60s and heading towards retirement age.

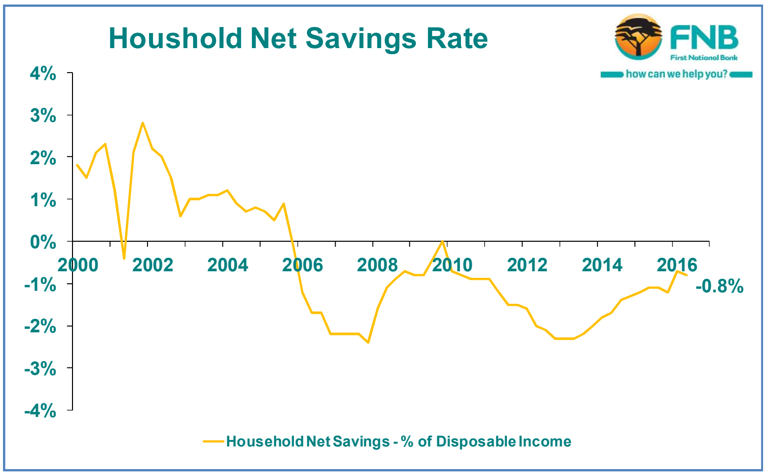


Further adding to the urgent need for a higher savings rate in the country is the slowing in price growth of various asset classes in recent times, which has translated into a slowing in the value of Household Sector Net Wealth since the more rapid growth period of 2013/2014.

While Household Sector Net Wealth did grow at a slightly higher 5.5% year-on-year rate in the 2nd quarter, compared to 4.3% in the prior quarter, it still battles to outperform general inflation and grow in real terms.

This pedestrian 2nd quarter rate of growth translated into a slight decline in the Net Wealth-to-Disposable Income Ratio, from a previous quarter's 388.2%, to 385.8%. This implies no progress since the early-2015 high of 398.9% in this ratio.

If Net Wealth grows at a slower pace due to slower asset price growth, then a higher rate of savings is required to "compensate" for this. And given the state of the global economy, with growth dragged down by a massive debt market bubble, while South Africa's own growth constraining structural problems help keep its own economic growth not far from zero, there exists the distinct likelihood that asset price growth could be on the slow side for some years.



To the Household Net Savings Rate then (Gross Saving net of depreciation on Fixed Assets). We have, prior to the 2nd quarter of 2016, indeed seen some early signs that part of the Household Sector's move towards greater financial conservatism may be starting to translate into an improving savings rate over and above a mere indebtedness reduction.

From the-2.3% of Disposable Income low point in mid-2013, the Net Dis-savings Rate had diminished to -0.7% by the 1st quarter of 2016.

We had hoped to take a step closer to positive net savings during the 2nd quarter, but a slightly better economic performance, and perhaps a slightly less weak consumer confidence level in that quarter, caused a slight improvement in Household Consumption Expenditure growth, and a resultant decline once more in the Net Dis-savings rate to -0.8%.

The Household Savings Rate thus remains one of the very weak points amongst a host of already weak economic data. Nevertheless, we remain of the expectation that we will see a return to positive net savings in the near term, despite the 2nd quarter slight deterioration.

We wouldn't expect too much in terms of savings improvement in this modern day consumer-focused society. But going back to past recessionary or weak economic period, we have typically seen some improvement in the Net Savings Rate. In 2008, a short-lived recession, Household Net Dis-Saving diminished from -2.4% of Disposable Income at the end of 2007 to zero by December 2009, before the good economic times resumed and once again took it weaker. Further back, in the early-1990s it improved from 3.1% in 1990 to 6.1% of Disposable Income by 1992, in the midst of a recession.

We are not in recession currently, and South Africa's consumers are a far cry from the 1960s mindset where the Net Savings-to-Disposable Income Ratio was often well into double-digits. But we are in the midst of a long period of weak economic growth, where recession risk is high and the risk of job loss significant. This should continue to drive the consumer towards a more conservative financial mindset both in terms of indebtedness levels as well as savings rate.