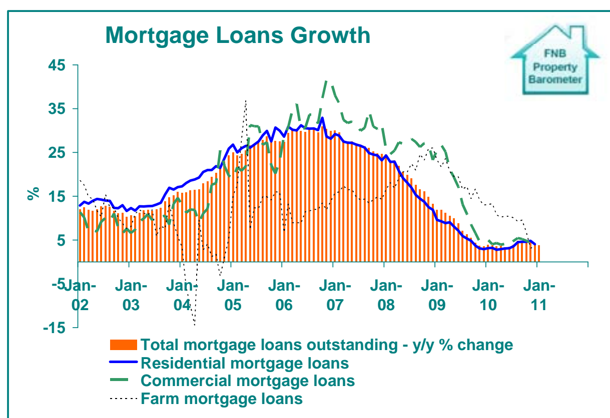
MORTGAGE AND HOUSEHOLD CREDIT

Mortgage growth stays slow, but overall household credit growth doesn't, with shorter term borrowing starting to "misbehave".

28 February 2011

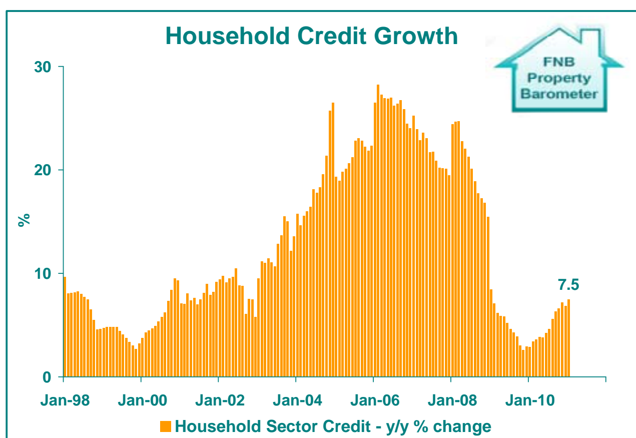


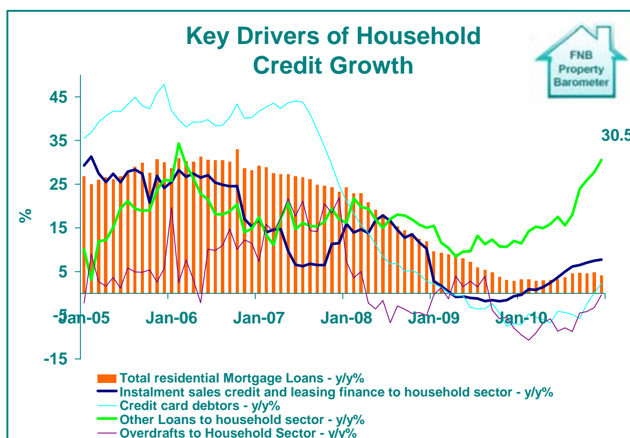
In January, the total value of mortgage loans showed further slowing in year-on-year growth, from 4% in the previous month to 3.8%. The residential mortgage market, due to its sheer size, is almost always the key driver of the direction of the country's total mortgage advances, but although the data split by segments runs a month behind the total figure, it would appear that slowdowns in commercial mortgage growth as well as farm mortgage loans growth have also played a role.

The very slow growth in the dominant residential component of mortgage loans (4.1% in December 2010 and slowing) remains unsurprising, given the weak state of household sector finances, which includes a weak savings rate that causes many to battle with relatively conservative home loan banks' affordability calculations and widespread deposit requirements, and of course the fact that the home loan is for many the biggest loan that they will ever take out.

The picture, however, looks significantly different in the area of shorter term borrowing by households, and January saw total household sector borrowing actually resume its accelerating growth trend in spite of the "drag" of the large mortgage component.

From 6.8% in December, the year-on-year rate of growth in total household sector credit accelerated to 7.5% in January 2011, the highest rate of increase since January 2009. Examining the key drivers, based on banking sector BA900 data up to December, the category "Other Loans to the Household Sector" is blazing the trail with a massive 30.5% year-on-year growth, followed by the important "Instalment Sales and Leasing Finance" category at 7.8%. While the "Overdrafts" and "Credit Card" categories were still at lower growth rates than "Mortgage Advances", one could see them steadily awakening from their slumber", emerging from negative growth and looking set to make a more meaningful contribution to overall credit growth.





Comment

While some may see accelerating household borrowing growth as a reflection of better economic or interest rate times, it may also be sustaining the high level of vulnerability of the household sector to external shocks. A 7.5% overall household credit growth rate remains moderate by standards of a few years ago. However, the rising trend is a little ominous against the background of weak job creation, nominal household disposable income growth ticking along in single digits, and an already very high household debt-to-disposable income ratio of 78.5% as at the 3rd quarter of 2010 (and up on the previous quarter). Unless household income growth accelerates more meaningfully, it will not take much further rise in household credit growth to drive the debt-to-disposable income ratio to higher levels. And the problem is? Firstly, the last interest rate hiking cycle showed that the high levels of household sector indebtedness of recent years can (and did) lead to

"severe pain", suggesting that we would do well to enter the next interest rate hiking cycle with a significantly lower debt ratio. Secondly, there exist certain ominous signs that the next interest rate hiking cycle may not be too far off, hardly the time to be ratcheting up the borrowing growth.

Even before last week's surge in oil prices, on the Back of huge Middle East political uncertainty (with Brent crude ending the week above $110/barrel), many commentators including those of us at Firstrand had believed that the next interest rate move would be up later in 2011, on the back of rising global inflation pressures. Notable were already-rising oil prices as well as global food prices, and the January consumer price data had begun to show a slightly higher impact of food in the overall South African CPI, though admittedly nothing troublesome yet. The Middle East crisis raises the inflation risks further through its impact in pushing on oil prices even higher than what global economic growth was already doing.

It would also be good to take heed of government finance trends and their impact on household sector finances. Last week's Budget Speech indicated the probable further rise in the personal income tax burden as a percentage of gross income, with adjustments for income tax bracket creep looking likely to be insufficient to arrest the rising personal tax burden trend of recent years, at least for the middle and higher income groups. And then, of course, we are near to the next big annual Eskom tariff hike. The rising tax and parastatal tariff burden for the household sector is no surprise, with government revenues having been under pressure in recent years accompanied by the pressing need to address a myriad of expenditure backlogs, notably in the area of infrastructure, but it does compete with other household expenditure items including interest payments.

In short, therefore, one could argue that accelerating household sector credit growth is a sign of better economic times. That may be so, with interest rates at lowest levels in decades. However, when seen against the backdrop of rising inflation, and thus interest rate, risk, and given the already high level of household indebtedness and weak savings rate, perhaps the accelerating growth trend in household borrowing should raise some concern, as it looks increasingly likely that we may enter the next interest rate hiking cycle with a still-high debt-to-disposable income ratio. That would surely sustain the pressure on the already-weak housing market.

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