EFFICIENT GROUP

ECONOMIC COMMENTARY

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YOUR WEEKLY ECONOMIC UPDATE

26 July 2022

THE COST OF HIGHER INTEREST RATES IN SA

In total, interest rates have increased by 2% during the current hiking cycle in South Africa (SA). In November 2021, the South African Reserve Bank (SARB) started the hiking cycle by increasing interest rates by 0.25%. Many South Africans hoped that these types of increases would continue, especially after a similar increase was made by the SARB in January 2022. But since then, these hopes have faded. Last week, the SARB decided to increase interest rates by 0.75%, after not too long ago increasing rates by 0.50%.

What does this mean? It means that each R1 million debt that a household has will now cost R20 000 more each year, or R1 667 more each month. This is a substantial increase. Although each household should estimate the impact that interest rate increases will have on their budget, and plan accordingly, the picture does not look any better if we consider the impact of higher interest rates on the economy.

According to the SARB, household debt, expressed as a percentage of disposable income, that is, the income that you take home, is about 65% in SA. Total annual disposable income, at current prices, is somewhere close to R3.85 trillion, which means that total household debt is roughly R2.50 trillion. This means that, in total, South Africans will now pay R50 billion more for their debt each year.

The next step is to estimate what the likely impact will be on each household. To do this, we must try and determine what the average debt per household is. Based on credit data from different sources, it seems that there are about 6 million consumers (read households) with debt. Many of these consumers have multiple debt-related accounts, from bonds on their houses, to credit cards, as well as different types of loans. It should also be noted that the figure can differ substantially depending on the source of information that we use, but 6 million seems to be a good estimation of the total. What this means is that these 6 million consumers owe R2.50 trillion, and the average debt is, therefore, about R415 000. If we use this figure as an accurate estimation, it means that indebted consumers are now paying R8 300 more for their debt each year, or R692 more each month. If we then consider that the average income in SA is between R15 000 and R17 500, depending on the source of information that you use, households will now have between 3.22% and 3.95% less to spend on necessities each month.

The question now is: Is it over? Unfortunately, it does not seem so. Although, from a macro perspective, we agree that interest rates should increase, we do not agree with the pace of the increases. Interest rates are not being increased to curb inflation because the SARB's increases have very little impact on higher fuel and food prices, the main culprits of inflation. Also, unlike in rich countries, we do not have above-trend demand pushing up prices. In fact, demand has been under severe pressure for many years in SA. Interest rates should increase to remain competitive in international capital markets that can help with short-term capital flow and long-term economic performance, but for this it is not necessary to increase interest rates at the current pace. It seems that the SARB will increase interest rates by at least another 0.50% this year and should increase interest rates by a further 1.50% in 2023.