Batten down the hatches

By Sasha Planting

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Consumers in SA are facing a triple-whammy of double-digit food inflation, stubbornly high fuel prices and interest rates that have increased by 4,5 percentage points since June 2006.

None of these costs is likely to ease in the medium term, and cash-strapped consumers are finding it harder to service their debts as costs soar above their growth in income.

While the average wage increase was 7,8% in the first quarter of 2008, headline inflation is nearing 10%, according to Stanlib chief economist Kevin Lings. Today a full 12% of disposable income is spent servicing debt, compared with 7% at the start of 2006.

“This is historically high,” says Lings. “We have reached the point where consumers are deciding who not to pay — and bad debt judgments will inevitably increase.”

Easy credit fuels spending

While the inflation rate, interest rates and fuel prices have been increasing steadily, those consumers who could access credit used it to buffer themselves against these financial pressures. However, the ease with which credit could be accessed fuelled spending. When the slowdown finally hit the retailers — last December, a full 18 months after the first interest rate hike — it was sudden and dramatic. Retail sales growth plummeted to 2,7%, down from 9,7% growth in the previous year, according to the Retail Liaison Committee. This was the first annual decline in retail spending since 2001.

Figures for February, which were published after the *FM* went to print, are expected to show negative or, at least, zero growth.

“What Tito [Mboweni] is doing with these rate hikes is trying to shift consumer expectations,” says Nedcor Securities retail analyst Syd Vianello. “He wants consumers to understand that they cannot afford to borrow more — and he is succeeding.”

Certain retailers are more cursed. Those that rely on discretionary spending or access to credit such as furniture, electronic equipment and new vehicles, have been hardest hit. As non-cyclical cash retailers, the food retailers are protected, but they too are feeling the heat as consumer behaviour changes.

Less cash in the pocket

“An increase in interest rates ultimately means less cash in consumers' pockets,” says Pick n Pay CEO Nick Badminton. “Consumer spending constitutes about 60% of SA's GDP and we are concerned that consumers are already feeling a lot of pressure, particularly at the lower end.”

BoE analyst Barbara Price-Hughes adds: “Consumers are trading down. Whether [the purchases are] from Shoprite and Woolworths to private labels and branded goods, they are definitely aware of what things are costing.”

More bad news is on the horizon as house prices are expected to decline by as much as 15% in the coming year. This could have devastating consequences for the retail sector, says Vianello. “The average consumer has a bond of about 80% of the value of their home. If prices slump there will be no equity left in people's bonds.”

Though some retailers, such as Woolworths, did not expect the slump in consumer spending to be as severe, others have been battening down the hatches for some time. Mr Price, for instance, has been tweaking its inventory to hold as little stock as possible. Foschini has a freeze on new staff appointments. In addition, most of the credit retailers have increased their provisions for bad debts.

If there is a silver lining to this cloud, it is the fact that the economy is considered sound, so the slowdown is not accompanied by widespread job losses — as has occurred previously in SA.

Renegotiate

“People are positive about economic development in the medium term,” says Lings. “They don't want to retrench staff they have gone to some lengths to train, only to have to find new skills in a few years' time.”

This means that indebted consumers can renegotiate a payment plan with banks and credit retailers.

The retailers themselves are confident that this is a cycle they will need to sit out. “While we will need to trade through this tough period for at least another year, we think that the SA economy is fundamentally sound,” says Woolworths CE Simon Susman. “There is a strong new consumer base that demands the best and wants a retail experience that supports these aspirations.” -

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