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DEBT RELIEF POLICY – MAKING DEBT MANAGEABLE

Engagement with the Portfolio Committee on Trade and Industry with respect to policy on debt relief
National Treasury, 14 June 2017



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What is our vision?

- First, we want to give South Africans that are chronically overindebted and have no chance or way to escape that debt, **the opportunity of a fresh start**
- Second, we want to **change the way that South African’s interact with the financial sector**, so that this “fresh start” paves the way for **new or changed borrowing behaviour**.

*Changing behaviour means getting South Africans to **save for future expenditure rather than borrow for immediate consumption**, and where borrowing, choose to **borrow to fund an investment like a home** rather than cheap consumable goods like a TV (noting also that many South Africans are **borrowing just to survive**)*



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2

Propose guiding principles for debt relief

- Will need **different solutions for different “categories” of distressed persons**, depending on their circumstances:
 - Are you earning an income, how high is that income?
 - Do you own assets?
 - Do you have a secured or unsecured loan?
- If a person can pay, **he or she should pay** (unless the loan was granted recklessly)
- **Promote responsible lending**: want to disincentivise reckless lending, incentivise secured over unsecured lending especially for homes
- **Promote responsible borrowing**: change behaviour, promote borrowing for capital growth rather than consumption and within affordable and sustainable limits



3

Propose guiding principles for debt relief (cont)

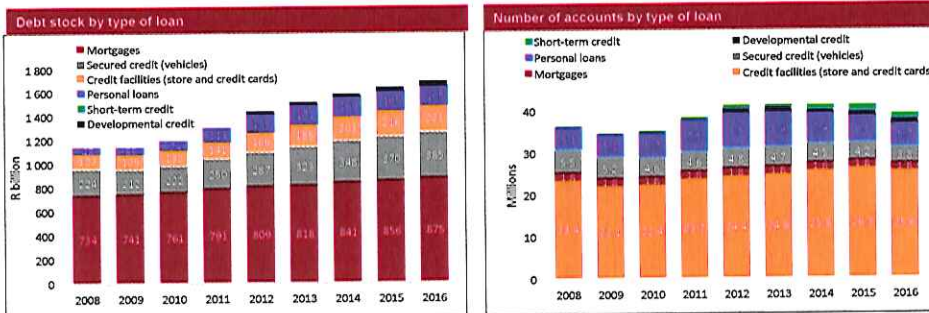
- **Extinguishing of debt** should only apply to unsecured loans, with focus on no or low income (those groups who cannot afford debt review)
- To the extent possible and reasonable **protect a borrowers asset**; selling that asset should be **absolute last resort**, and where done should be done **fairly and with dignity**
- Requires **holistic response**, should be a **shared responsibility across government, bank and non-bank credit providers, debt collectors and debt counsellors**
- Do **comprehensive impact assessment** of agreed options in support of evidenced-based policy
- **Maintain systemic stability**



4

Market Overview

- Half of debt is mortgages, with 1.8m accounts (R875 billion)
- Accounts dominated by store and credit cards (25m) (R221 billion)
- Personal loans debt at R165bn, 5.7m accounts



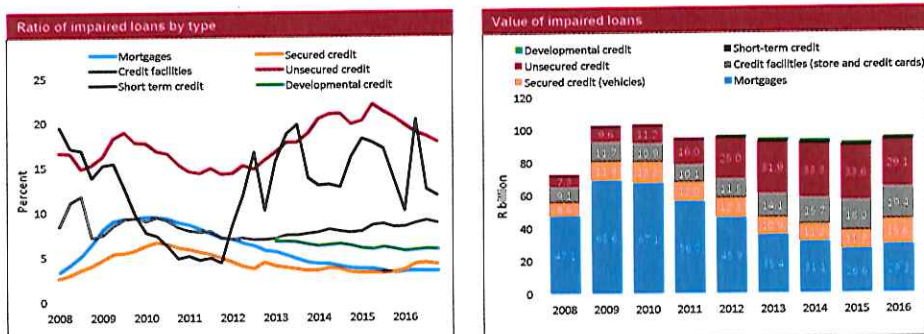
Source: NCR



5

Impaired loans (91+ days overdue)

- Personal loans the most impaired, followed by short-term credit
- R29bn of personal loans overdue
- But rand value of short-term credit small



Source: NCR

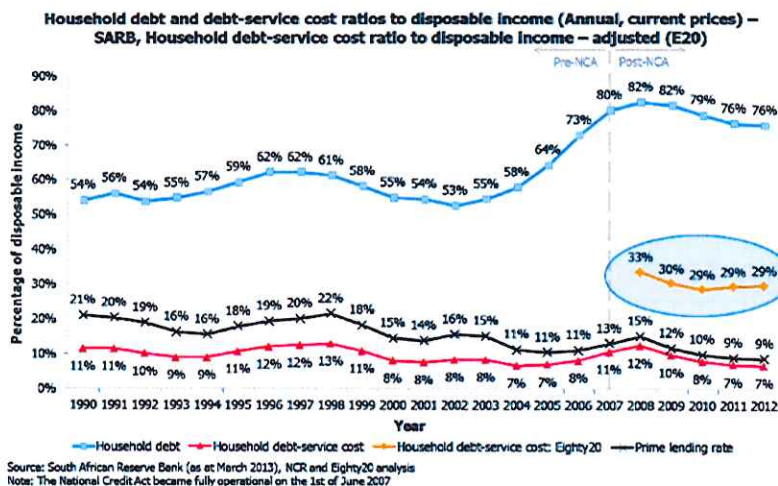


6

Some evidence of past interventions – 1st Amnesty

- First clean up of credit bureaux in 2007, based on civil court judgments paid up, very low amounts or old – did not remove obligation to pay debts
- Bureaux **subject to internal and independent audit**
- All information was declared removed – bureaux did not keep a list of ID numbers that benefitted through amnesty
- However a data comparison was performed and about **600 000 consumers were identified and used as a statistical sample** (by the CBA)
- **64% of the individuals who benefitted from amnesty subsequently opened accounts**
- **74% of the individuals who obtained credit had bad (30%) or adverse (44%) accounts**
- **19% of the individuals had a judgment in 5 years**
- Of course this conversely means that **more than half (52%) of amnesty beneficiaries remained in clear**

Evidence of how South Africans are borrowing, 80-20 report commissioned by NT (2013)



Evidence of how South Africans are borrowing (cont)

Debt to net income by income band and income category

		Personal gross monthly income				
		R1 - R3 500	R3 500 - R10 000	R10 000 - R15 000	R15 000 - R30 000	R30 000 +
Product category	Asset finance	0.00	0.03	0.13	0.30	0.45
	Mortgage	0.01	0.18	0.55	1.13	1.53
	Credit card	0.00	0.03	0.03	0.03	0.03
	Personal loan	0.01	0.05	0.06	0.07	0.03
	Microloan	0.07	0.17	0.07	0.04	0.01
	Any retail account*	0.07	0.08	0.03	0.02	0.01
	Total	0.2	0.6	0.9	1.6	2.1

* Clothing or furniture credit

Evidence of how South Africans are borrowing (cont)

Debt servicing to net income by income band and income category

		Personal gross monthly income				
		R1 - R3 500	R3 500 - R10 000	R10 000 - R15 000	R15 000 - R30 000	R30 000 +
Product category	Asset finance	0%	1%	5%	10%	18%
	Mortgage	0%	3%	7%	14%	19%
	Credit card	0%	6%	6%	5%	5%
	Personal loan	1%	4%	3%	3%	2%
	Microloan	7%	14%	5%	3%	1%
	Any retail account*	19%	20%	6%	7%	2%
	Total	29%	49%	33%	44%	48%

* Clothing or furniture credit

Evidence of how South Africans are borrowing (cont)

CREDIT PRODUCTS USED BY MORTGAGE AND NON-MORTGAGE BORROWERS

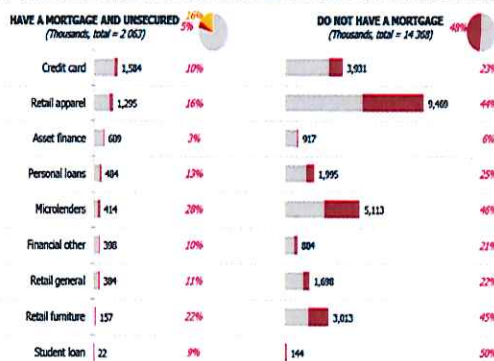


Source: XDS data
 Note: Unsecured loans include microloans, personal loans, credit cards, retail apparel, retail furniture, retail general, student loans and financial other
 Note: Pie: Red segment shows proportion in arrears on product that makes up segment, yellow shows arrears on any other credit product



Evidence of how South Africans are borrowing (cont)

CREDIT PERFORMANCE OF MORTGAGE AND NON-MORTGAGE BORROWERS



Source: XDS data
 Note: Unsecured loans include microloans, personal loans, credit cards, retail apparel, retail furniture, retail general, student loans and financial other
 Note: Pie: Red segment shows proportion in arrears on product that makes up segment, yellow shows arrears on any other credit product



Evidence of first time borrower patterns


- **Retail apparel accounts dominate as the initial credit product** accessed by first time borrowers. **In 2012 40% of first time borrowers opened a clothing account** as their first product; **19% opened a loan from a microlender**
- **Around half of those who took out a microloan as their first product in 2012 had taken out another microloan by July 2013**
- **53% of borrowers** who accessed credit for the **first time in 2010** and who were still active in July 2013 were **in arrears in July 2013**; **31% of borrowers** who accessed credit for the first time in **2012** and who were still active in July 2013 were **in arrears**.
- Banks indicate that people who **start off with a retail account tend to evolve through the credit space into banks**, whilst those that **start with a microloan struggle to evolve along the path and don't**

Options for over-indebted consumers

Option	Applicable law	Description	Only applicable if:	Additional notes
Debt Review	National Credit Act	Debt Counselor calculates repayment plan - if accepted by creditors a legal consent order obtained.	1) Debtor is employed 2) Debtor can afford the fees and charges of counseling process 3) The DCRS solves	
Administration	Magistrates Court Act	Court order that legally hands over the management of a debtor's financial affairs to a debt administrator.	Outstanding debt does not exceed R50 000.	- Administrator may charge up to 12.5% fee - Payments to creditors made very three months - Administrators aren't required to register with a regulatory body, thus there's increased potential for abuse.
Voluntary Sequestration	Insolvency Act	A sequestration order is a formal declaration that a debtor is insolvent	The order is beneficial to creditors	Costly High Court Application

Do these options serve the most needy?

	No income no assets	Low Income no assets	No / low income with asset/s	Income > R10000
Debt Review	✗	✗	✗	✓
Administration	✗	✓	✓	✓
Sequestration	✗	✗	✓	✓

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Note: Administration does not solve long term debt problems.

19

Possible approach to debt relief: NINAs

Group 1: indigent persons earning less than R3500

- **Indigent persons and/or SASSA grant beneficiaries** to proxy for NINAs – aim towards meeting a **“living income,”** what does a South African need to live?
 - Three options:
 - 1) Consolidate loans, eliminate all fees, charges and interest, and apply 20% debt servicing:income ratio ceiling over 3 years and extinguish the rest on pro-rata basis (across lenders/collectors)
 - 2) Extinguish aggregate debt up to certain ceiling like R2000 on pro rata basis
 - 3) Extinguish all debt

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Possible approach to debt relief: NINAs (cont)

Group 1: indigent persons earning less than R3500 (cont)

- Pros and cons for each option. Preferred solution will depend on whether policymakers think this group **should have access to credit** – if yes then **options 1 and 2 preferred to foster improved credit culture**
- **Who will oversee the transactional work, who will pay for this?**
- To qualify a **borrower should elect in**, as will be subject to certain conditions like financial education and wellness programme
- Will be **flagged in bureau** and cannot be given another loan for the 3 year period
- Consider whether a person in this group should have to prove that “under stress”: **don’t think so** as then penalising those showing “good” borrowing behaviour



Possible approach to debt relief: low income earners

Group 2: South Africans under severe financial distress earning R3500 – R5000

- This group of South Africans fall into debt review “gap” as cannot afford debt councillor fees
 - Options:
 - 1) **Loans that were issued when a borrower already in severe distress** (as flagged in bureau) deemed to be **reckless and extinguished** (*consider whether this should apply for distressed borrowers or all?*)
 - 2) **For distressed borrowers only**: for the remaining loans consolidate, eliminate all fees and charges, and apply 30% debt servicing:income ratio ceiling over 5 years and extinguish the rest on pro-rata basis **OR**
 - 3) Extinguish aggregate debt up to certain ceiling like R3000 on pro rata basis
 - **Prefer options 1 with 2**, as the debt servicing is the crucial driver of disposal income after debt obligations



Possible approach to debt relief: low income earners (cont)

Group 2: South Africans under severe financial distress earning between R3500 – R5000 (cont)

- To qualify a **borrower should elect in**, as will be subject to certain conditions like **financial education and wellness programme**
- Will be **flagged in bureau** and **cannot be given another loan for the 5 year period**
- Should we **target groups within this band**, like **mineworkers**?



Possible approach to debt relief: earners at upper end of debt review gap

Group 3: South Africans under severe financial distress earning R5000 – R10000

- This group of South Africans also falls into debt review “gap”
 - Options:
 - 1) Loans that were issued when a borrower already in severe distress (as flagged in bureau) deemed to be **reckless and extinguished**.
 - 2) The remaining loans should be subject to **subsidised debt review and DCRS** – should debt counsellors be required to service an agreed proportion of clients in this group?



Challenges

- **Don't yet have research to determine impact** – should be prioritised
- How to **secure industry buy-in**? Consider issues of **constitutionality**. What is the **role of Government**?
- Expected to **heavily impact retailers and microlenders**: how to ensure that these sectors are kept sustainable?
- Expected to **heavily impact access to credit**, and likely to push desperate people to illegal operators
- What about the debt that sits with **debt collectors**?
- Are we **fostering a worse credit culture** amongst borrowers?



Other supporting interventions

- **Plug the gaps** identified on slides 18-20
 - **Personal insolvency bill** through DoJ
 - **Strengthen debt review process**: propose reforms additional to dti proposals that support better governance (esp around reporting) and fit and proper standards
- **Urgent solution required for assets of distressed South Africans**: banks as an industry should commit to improved process ahead of DoJ reforms
- **Total cost of credit Key Information Document (KID)**
- Should we consider a **debt relief proposal for students**? **Retrenchments**?
- Propose automatic enrolment **payroll deduction savings programme** – 1% of gross salary that can be accessed every three years.



Proposed next steps

- On guidance from the PCTI, the NT can **oversee the necessary research** to assess impact of different options
- **Banks already sourcing data; NT engaging with industry expert analysts**
- This should take approximately 6 weeks
- **NT to lead process with banks to come forward with a solution to mortgage loan abuses**