HOUSEHOLD INDEBTEDNESS SURVEY REPORT

DECEMBER 2021

BANK OF BOTSWANA

EXECUTIVE SUMMARY

This survey[1] measured the level of household indebtedness in Botswana, using data collected from commercial banks, statutory banks, micro-lenders, hire purchase stores, and Savings and Credit Cooperative Societies (SACCOS). The data was collected by means of an online questionnaire, which supplemented the regular statutory returns of commercial and statutory banks for the month of December 2020.

The findings of this annual survey help determine the extent of vulnerability of the financial system to household sector credit exposure and guide the determination and implementation of financial sector policies, in general, for effective functioning of the financial system and beneficial use of credit. Furthermore, the survey results serve as a public awareness material that makes it easier for the public to comprehend credit markets and guide households towards more effective financial management.

As at the end of December 2020, total household debt amounted to P54.8 billion, comprising bank loans (88.9 percent)[2], micro-lenders loans (9.1 percent), hire purchase credit (1 percent) and SACCOS loans (1 percent). As a percent of Gross Domestic Product (GDP), total household debt was 31.7 percent in the same period, this compares to 28.4 percent in 2019. As with the previous surveys, the current survey indicated that men incur more debt than women and that the population group aged 30 to 49 years old have proportionately more debt than other age segments of the population. Furthermore, households earning were between P3 001 and P20 000 per month actively participated in credit markets compared to those outside this income range.

The survey indicated that COVID-19 related factors affected the supply and demand for credit in 2020. Generally, banks (commercial banks and statutory banks), microlenders and hire purchase stores viewed the outlook for demand for credit as moderate in 2021. Many banks indicated that they were reluctant to supply credit in 2020; however, the credit supply conditions were viewed more favourably in 2021 than in 2020.

[1] The Household Indebtedness Survey is published annually by the Bank of Botswana based on the previous year's financial information and expectation about credit developments. Data collected does not include informal credit arrangements such as metshelo and family loan arrangements. In addition, the survey did not collect information on household assets and income flows.

[2] Bank loans (including statutory banks) to households increased from P48.7 billion in December 2020 to P51.1 billion in October 2021.

1. INTRODUCTION

1.1 This survey measured the level of household indebtedness in Botswana, using data collected from commercial banks, statutory banks, micro-lenders, hire purchase stores, and proxied figures for SACCOS. The survey examined the demographic profile of borrowers; purpose of household credit; cost of credit; quality of the loan book; as well as lending policies/strategies and risk mitigation measures. The results were expected to inform policy formulation, macroprudential policy action, as well as institutional frameworks and regulations to facilitate disciplined and beneficial access to credit and mitigate the risks associated with any form of unsupported high levels of borrowing from multiple sources by the households and/or retail sector. Overall, in the context of the broader objectives of financial inclusion and economic development, policy makers need to carefully balance the benefits and risks of household debt over various time horizons and economic cycles.

1.2 A general expansion in borrowing by households is supportive of economic growth and development, mainly through consumption spending and acquisition of high-value assets, such as property (land and housing) and other income-generating assets (for example, capital goods and private equity investing). However, there can be an increase in financial risks when increasingly higher rates of household credit growth are either not supported by a commensurate increase in personal incomes or fail to generate sufficient wealth. Risks are especially elevated when financing conditions become unfavourable such as when interest rates or financing costs increase or when declining economic activity results in reduced employment and income earning opportunities; thus, adversely affecting the borrowers' ability to continue to meet the repayment obligations in a sustainable manner.

1.3 The remainder of the Survey report is organised into three sections. Section 2 describes the methodology used in conducting the Survey. Section 3 discusses the findings of the Survey, while Section 4 concludes the report.

2. DATA DESCRIPTION AND METHODOLOGY

2.1 The survey covered the features of household debt, including debt-to-income ratios, debt service capacity and alternative sources of funding in 2020. The debt service ratio is a key parameter for assessing the capacity of households to meet their debt obligations in a sustainable manner. The analysis makes use of information gathered from commercial and statutory banks, twenty micro-lenders and three large hire-purchase stores. To achieve the objective of the Survey, primary data was collected using an online questionnaire. The analysis was augmented with secondary data from statutory returns of commercial and statutory banks submitted to the Bank of Botswana (the Bank). Proxied data from the Department of Cooperatives for SACCOS in Gaborone Region was also utilised. The Survey questions covered aspects on the outlook for the demand for credit; demographic characteristics of households; credit application processes; characteristics of the credit/loan book; and credit risk strategies relating to household debt.

2.2 For purposes of this survey, household debt refers to a loan or credit acquired, or debt incurred for, among others, the purchase of assets such as owner-occupied residential property, commercial real estate, equipment, vehicles, and consumables. Households also incur debt for miscellaneous other uses. Interest rates, installment payments, expectations regarding future income, and wealth are all factors affecting households' decisions to borrow.

3. FINDINGS

(a) Demography of Households

3.1 As at the end of 2020, there were 583 286 household borrowers, comprising 370 122 (63.5 percent) males and 213 164 (36.5 percent) females, at banks, micro-lenders, hire-purchase stores and SACCOS. According to Morsy (2020), credit bias towards males primarily reflects females' own evaluation of low creditworthiness because of relatively low financial literacy (particularly among low-income groups)[3] and high-risk aversion. Indeed, banks have indicated that they did not have lending products designed to enhance financial inclusion for women.

3.2 Banks financed 59 percent of household borrowers, followed by microlenders (23.2 percent), hire purchase stores (14.8 percent) and SACCOS (3.1 percent). The survey indicated that household borrowers aged 30 to 49 years were in the majority in the overall credit market, at 70.6 percent (60.7 percent in 2019), followed by those aged 50 years and above (15.8 percent) and those less than 30 years (13.6 percent). In value terms, 56.3 percent (of the loans) went to males compared to 43.7 percent for females. This represented a decline from 2019 for males (61 percent) and an increase for females (39 percent).

3.3 The summary of findings presented in Table 3.1 shows that most of the household borrowers were Government employees (including parastatals) (59.8 percent), followed by private sector employees (36.9 percent). Those that are self-employed accounted for 2.7 percent while the unemployed individuals accounted for 0.6 percent of total household borrowers. Relating to credit provision based on monthly income levels, most borrowers earned monthly income ranging from P3 000 to P19 999[4] (53.4 percent), followed by those who earned less than P3 000 per month (33.5 percent), while those earning P20 000 and above per month constituted 13.1 percent of borrowers.

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3 Organisation for Economic Co-operation and Development (2013) also notes that women appear to be better than men at short-term money management behaviour; and close monitoring of every day financial expenses is a first step towards building long-term financial security and averting unsustainable levels of debt.

4 Monthly average cash earnings for all employees in the formal sector was P6 014 (P5 853 for citizens and P13 355 for non-citizens) in December 2020.

Table 3.1: Demographic Information of Household Borrowers

	2017	2018	2019	2020
Gender	**Percent**			
Males	56	57.2	54.6	63.5
Females	43	42.8	45.4	36.5
Unclassified	1			
Age	**Percent**			
< 30	12	11.6	20.5	13.6
30 - 50	68	59.9	60.7	70.6
50+	20	19.1	18.7	15.8
Unclassified		9.4		
Employment Status	**Percent**			
Government Employed	94	60.4	54.8	59.8
Privately Employed	1	25.2	43.2	36.9
Self Employed	2	0.7	0.7	2.7
Unemployed	3	2.7	1.3	0.6
Unclassified		11		
Income	**Percent**			
<P3000	19	27.6	33.2	33.5
P3001 - P19 999	71	59.1	56.8	53.4
P20 000+	8	13.3	10.1	13.1
Unclassified	2			

Source: .Banks, Microlenders and Hire Purchase Stores

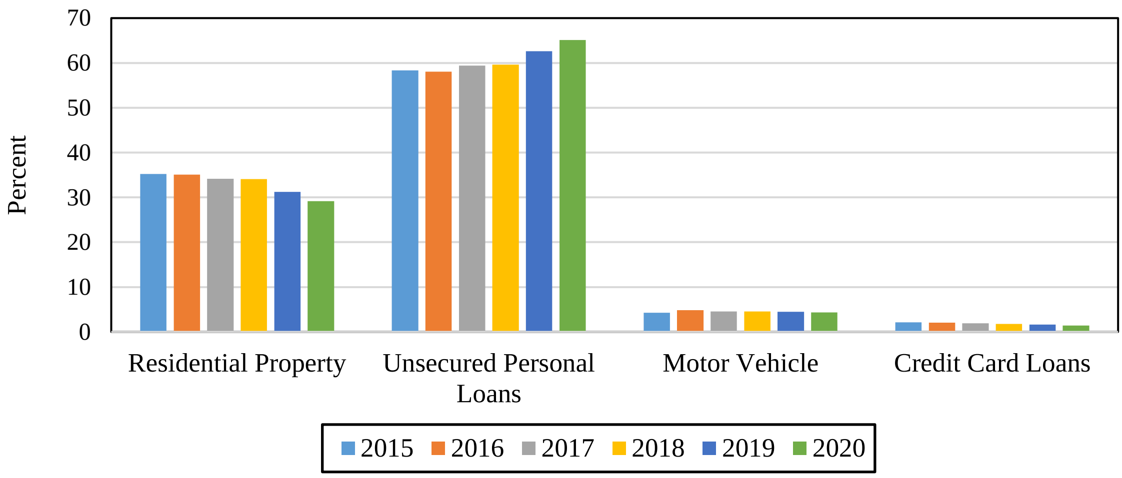
Note: . Household Indebtedness Survey for 2017 covers banks; 2018 covers banks, microlenders and hire purchase stores; and 2019 covers banks, microlenders, hire purchase stores and SACCOS; while 2020 uses estimated numbers for SACCOS.

3.4 In Botswana, the Government is the single largest employer and that explains the dominance of Government employees in total household debt obligations. Employment contracts in Government are mostly on permanent and pensionable basis, making Government jobs more secure or reliable for purposes of loan provision. Furthermore, domestic credit tends to be channelled to the most productive age group (30 - 50 years) in line with the dictates of consumption smoothing concept of the life cycle income hypothesis; thus, being supportive of welfare enhancement, economic growth and development.

(b) Types of Credit by Banks, Microlenders and Hire Purchase Stores

3.5 As shown in Chart 3.1, most of the lending to households by banks was in the form of unsecured personal loans, which accounted for 65 percent of the total bank credit in December 2020 compared to 63 percent in 2019. The second largest debt category was residential property at 29 percent, which is a decline from 31 percent in 2019, followed by motor vehicle loans at 4 percent and credit cards at 1 percent. In addition, the results of the survey indicated that 80.3 percent of households had a single credit commitment, 16.9 percent had two, 2.1 percent had three and 0.7 percent had four or more credit commitments. Given the expansion of credit products in recent years, it has been suggested that the threshold of four credit commitments as a common indicator of over-indebtedness may no longer be meaningful. Similarly, the number of credit commitments might not reliably detect situations of over-indebtedness since many outstanding small debts do not necessarily imply a condition of difficulty. Nonetheless, for the most part, the indicator (that is, the number of credit commitments) can be a measure of the process of becoming over-indebted. Consequently, the results of the survey (based on this indicator) showed that the clientele of banks were relatively not at the risk of being over-indebted.

Chart 3.1: Share of Household Borrowing by Type

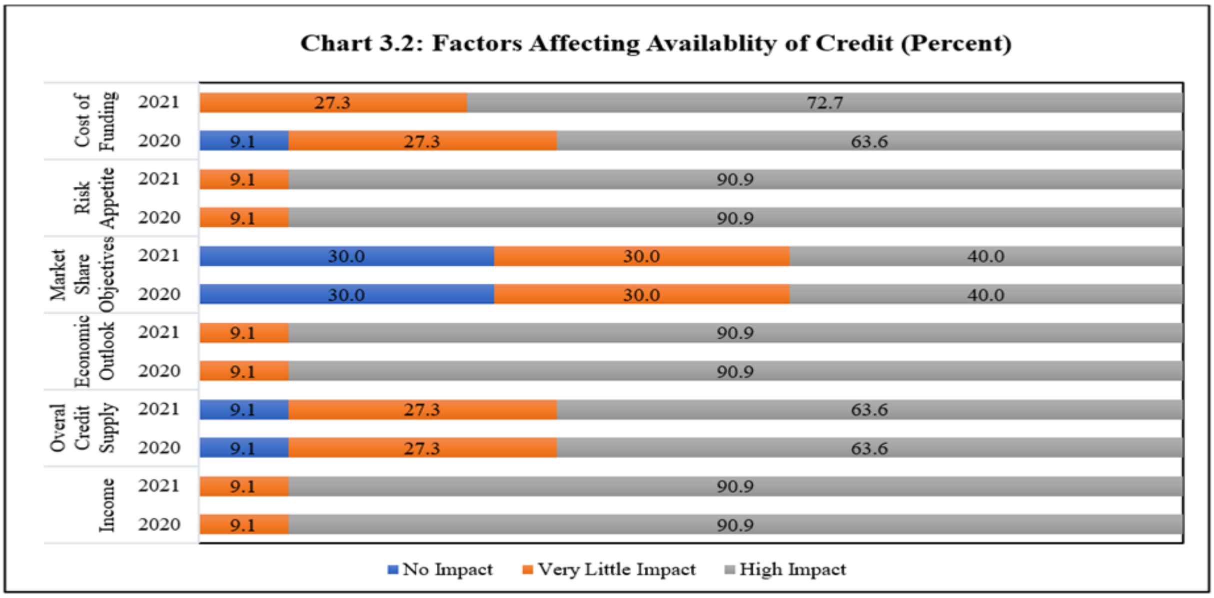


Source: Banks

3.6 The survey showed that hire-purchases were mostly used for the acquisition of furniture (51.3 percent), followed by home appliances (26.4 percent), and electronic equipment and devices (22.3 percent). Loans from micro-lenders were mostly for personal use on education, renovation of property, acquisition or expansion of business and debt consolidation.

(c) Factors Affecting Availability of Credit

3.7 Most banks were of the view that income, economic outlook and risk appetite had a high impact on the availability of credit during 2020 and expected the same factors to have an impact on credit uptake in 2021 (Chart 3.2). Notwithstanding, 91 percent of banks had unfavourable view of credit supply conditions (or unwillingness to supply credit) in 2020 compared to 55 percent for 2021. The Bank's 2020 Banking Supervision Annual Report also notes that, in 2020, banks had not used the capital released, through a 2.5 percentage points reduction in the minimum prudential capital adequacy ratio, for credit provision purposes; all banks were operating significantly above the 12.5 percent.

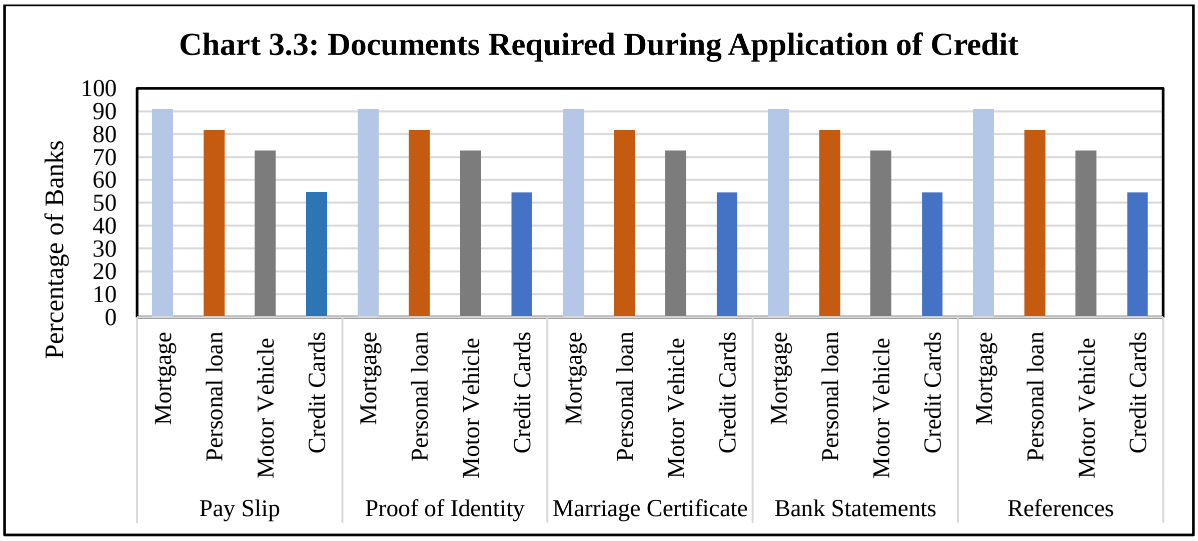


Source: Banks

(d) Credit Application Process

(i) Documents Required During Application for Credit

3.8 The loan review function of banks ensures that the documentation required for a loan application has sufficient information necessary to ascertain the prevailing financial condition of the borrower or counterparty, as well as sufficient information to track the decisions made and life of the credit. Credit files of potential borrowers include, for example, current financial statements, financial analyses and internal rating documentation, internal memoranda, reference letters, and appraisals; and the requirements are normally standard across the banking industry. Chart 3.3 shows documents required by banks per the type of credit facility applied for. While mortgages are considered ‘good’ debt and relatively cheaper than other types of consumer debt, the survey indicates that screening for mortgage applications tends to be stricter than other types of loan products because of the inherently long-term nature of the facility.



Source: Banks

3.9 Other documents required by banks include letters confirming employment; consent by spouse; copy of title deed, sale agreement, valuation report and architectural plan for home loans; valid driver's licence and quotation for new vehicles; and motor vehicle registration book, road worthiness certificate and sales offer indicating price for boarded (used) vehicles.

3.10 During 2020, a total of 13 176 loan applications, valued at P2.5 billion and representing approximately 23 percent (40 percent in 2019) of total loan applications, were rejected by banks (Table 3.2). The survey indicates that rejections were mainly due to observed bad management of personal bank accounts; failure to meet minimum employment period and thresholds such as the debt-to-income ratio (reflecting over-indebtedness); failure to agree on the rate of interest by the bank and the customer; and rejection of property presented as collateral, due to poor structural integrity (in the case of mortgage loans).

Table 3.2: Total Loan Applications and Rejections

	Loan Applications		Loans Rejected	
	Number	Amount P million	Number	Amount P million
Mortgage	2 349	1 890	291	223.2
Assets/Vehicle Insurance	2 244	790.6	422	135.3
Personal Loan	47 104	11 837.7	11 299	2 025.4
Credit Cards	4 597	62	977	13.5
Other	942	135.7	187	75.3
Total	57 236	14 715.9	13 176	2 472.7

Source: Banks

3.11 The majority of the banks (54.5 percent) viewed the approval rate of loan applications as moderate in 2020, while 27.3 percent viewed the rate as low and 18.2 percent viewed it as high. For the year 2021, 45.5 percent of the banks expect the approval rate to be moderate, 36.4 percent expect it to be high, while only 18.2 percent expect it to be low.

(ii) Assessment of Credit

3.12 Credit providers use the debt-to-income (DTI) ratio to evaluate the credit worthiness of applicants and the debt-service ratio (DSR) to assess the borrowers' debt service capacity during the life cycle of the credit facility. The DTI ratio compares the periodic instalment to periodic earnings, while the DSR is the share of a borrower's income allocated to loan repayments over a given period, say one year (total loan repayments/total income). A low (high) DTI ratio indicates good credit worthiness (indicates over indebtedness); while a low (high) DSR indicates an increased capacity to timely service the credit (indicates some financial constraint).

3.13 For 2020, the DTI ratio ranged between 40 percent and 60 percent for banks (average of 54.2 percent), 29 percent and 65 percent for microlenders (average of 44.7 percent); and 25 percent to 35 percent (average of 30 percent) for hire purchase stores. The DTI ratio varies across different products for some banks. In 2019, the DTI ranged between 30 percent and 70 percent for banks, 35 percent and 70 percent for microlenders; and 25 percent to 35 percent for hire purchase stores. On the other hand, some banks use a fixed net take home rule while others use a DSR on net income after tax and income.

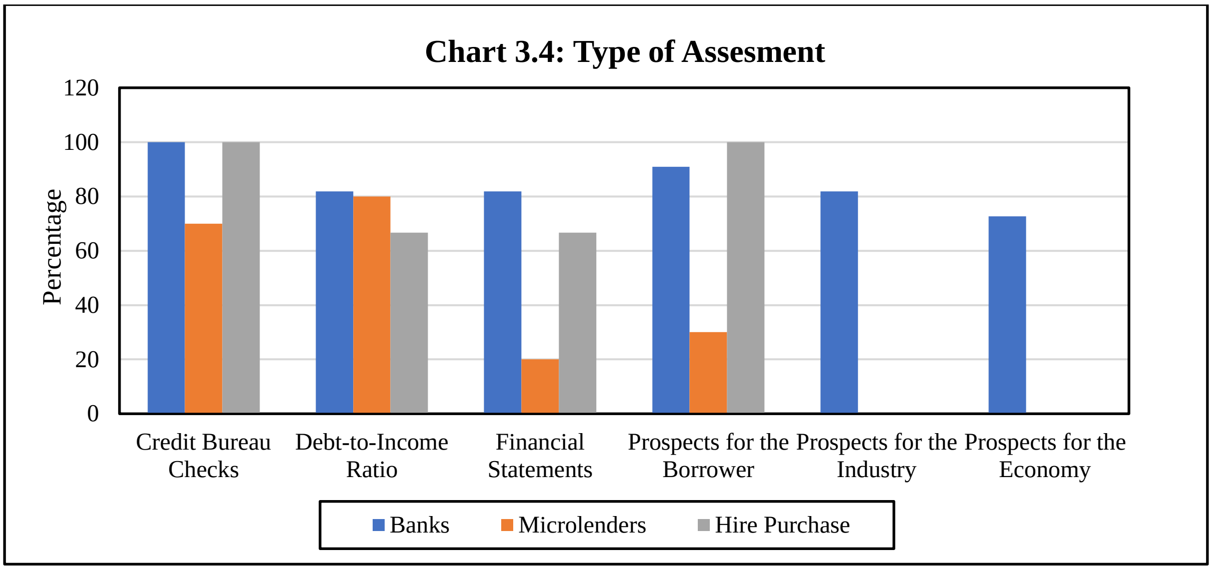
The survey shows that the DTI ratio varies from one lender to the other. Angel and Heitzmann (2015) suggest that the DTI ratio should be 40 percent or below. Thus, households that find themselves with higher DTI ratios would have a relatively higher financial burden than those at the lower end of the spectrum. On the other hand, DSR for banks ranged between 40 percent and 70 percent.

3.14 In addition, the Loan-to-Value (LTV) ratio is used by lenders to assess the potential coverage of outstanding loans through liquidation of collateral, thus the level of risk associated with debt taken. The LTV relates the amount borrowed to the value of property financed, typically mortgage loans. Therefore, the ratio is also often used for evaluating mortgage applications or when acquiring mortgage insurance. A higher LTV ratio represents low "equity" contribution in the property financed, hence exposes the credit provider to a higher risk of loss in the event of a default. As a macroprudential policy measure, LTV thresholds are imposed or recommended to ensure that banks are sufficiently prudent in their lending standards to safeguard individual banks' solvency and the stability of the whole financial system, particularly given the vulnerability of the property market to large price fluctuations.

3.15 In 2020, the LTV for banks ranged between 45 percent and 105 percent. The higher LTV ratios exposed banks to financial losses in situations where the proceeds from the sale of repossessed property (foreclosures) are not adequate to expunge the amount of loan balance outstanding from the books of the lender; particularly in instances of subdued economic activity. This is also what is often referred to as the Loss-Given-Default (LGD) or recovery risk. The average percentage exposure at risk that is not expected to be recovered in an event of default, as measured by the LGD, varied considerably across banks, ranging from nil to as high as 98 percent. That notwithstanding, mortgage insurance can be used as a risk mitigation tool in relation to high LTV mortgages. Additionally, in terms of the capital adequacy requirements for banks in Botswana (i.e., Basel II rules), the LTV ratio that is in excess of 90 percent is assigned a higher risk weight than the standard 35 percent risk weight for owner-occupied residential mortgage loans.

3.16 On average, 89 percent of banks use credit rating models to assess the credit worthiness of customers. Majority of these banks' models include information relating to current and past loans; records and bankruptcy measures; and to unpaid medical and utility bills. Extra information embedded in the models include interest rates, income, years with the bank and employer, dishonoured cheques, years at residential place, tenure of the loan requested, personal contact information (different contact points of a customer like mobile, work and home numbers), unpaid scheduled payments, unauthorised excesses, number of dependents, age and marital status of the borrower.

3.17 In addition to indicators embedded in the banks' credit rating models, credit providers give due consideration to prospects for the economy, industry and the borrower, as well as financial statements when assessing a potential borrower (Chart 3.4). Furthermore, banks use information from credit bureaus to identify high risk borrowers. Credit bureaus are critical in helping lenders make faster and more accurate credit decisions (International Finance Corporation, 2006), and this is the reason why the majority of credit providers subject potential borrowers to credit bureau checks for credit history profile to identify any adverse credit reference, which if any, would disqualify a borrower from being granted the credit.



Source: Banks, Microlenders and Hire Purchase Stores

(e) Characteristics of the Loan Book

(i) Quality of the Loan Book

3.18 Banks indicated that the loan default rate was adequately managed during 2020; the same sentiments were expressed for the survey conducted for the year 2019. On average, 63.6 percent of banks experienced a moderate default rate and 27.3 percent experienced a low default rate. The default rate reported by banks in 2020 ranged between 1 percent and 18 percent, with an average of 4.5 percent. For 2021, overall, the default rate, is expected to be moderate; 36.4 percent of banks expect a high default rate while 45.4 percent and 18.2 percent expect the default rate to be moderate and low, respectively. Banks which indicated that the default rate is likely to be high in 2021 attributed the anticipated development to the expected impact of COVID-19 on jobs, thus impairing the ability of households to service their debt. Meanwhile, banks that anticipate a low default rate based their conclusion on the good portfolio assessment for 2021 by some banks and the fact that the majority of customers are Government employees with deduction at source arrangement. By October 2021[5], commercial banks household loans in areas amounted to P1.3 billion, a decrease from P1.4 billion in December 2020.

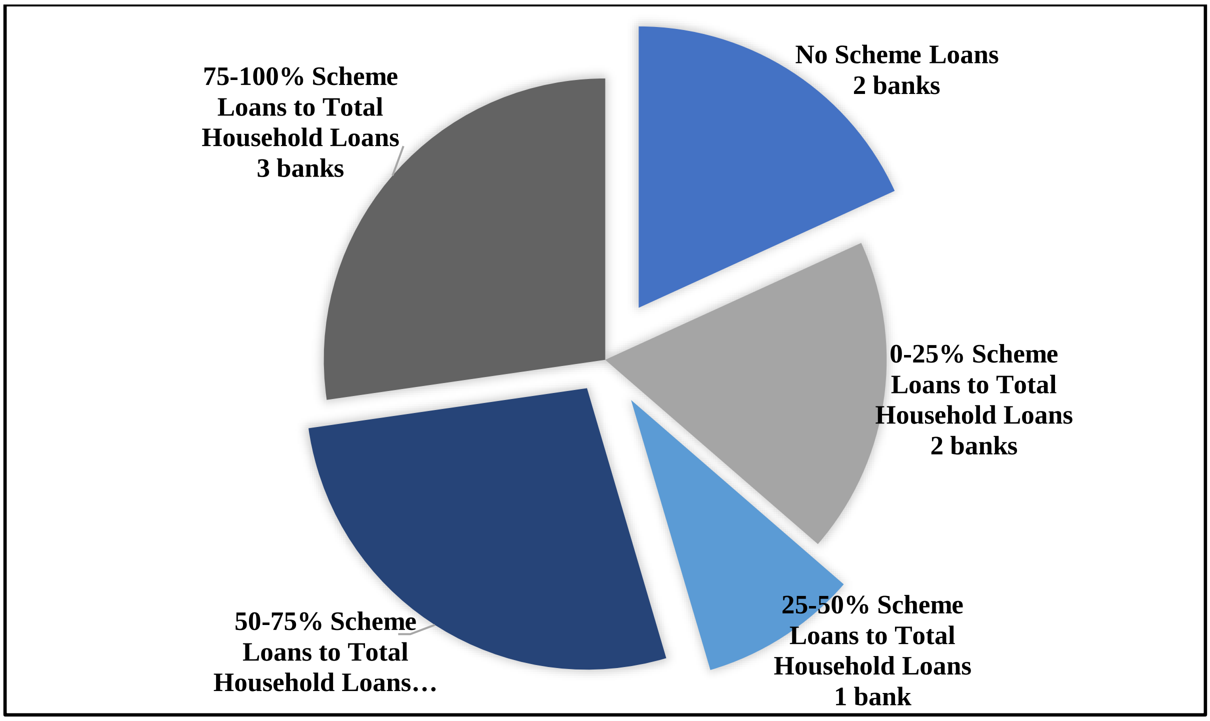
3.19 A large percentage of microlenders indicated that they were concerned about the high default rates during the period under review compared to the prior years. They attributed the increase in default rates to COVID-19, which also made it difficult for them to follow up defaulting customers. Similarly, hire purchase stores respondents indicated that the default rate was a concern in 2020.

[5] Botswana Financial Statistics, November 2021.

(ii) Servicing of Debt by Households

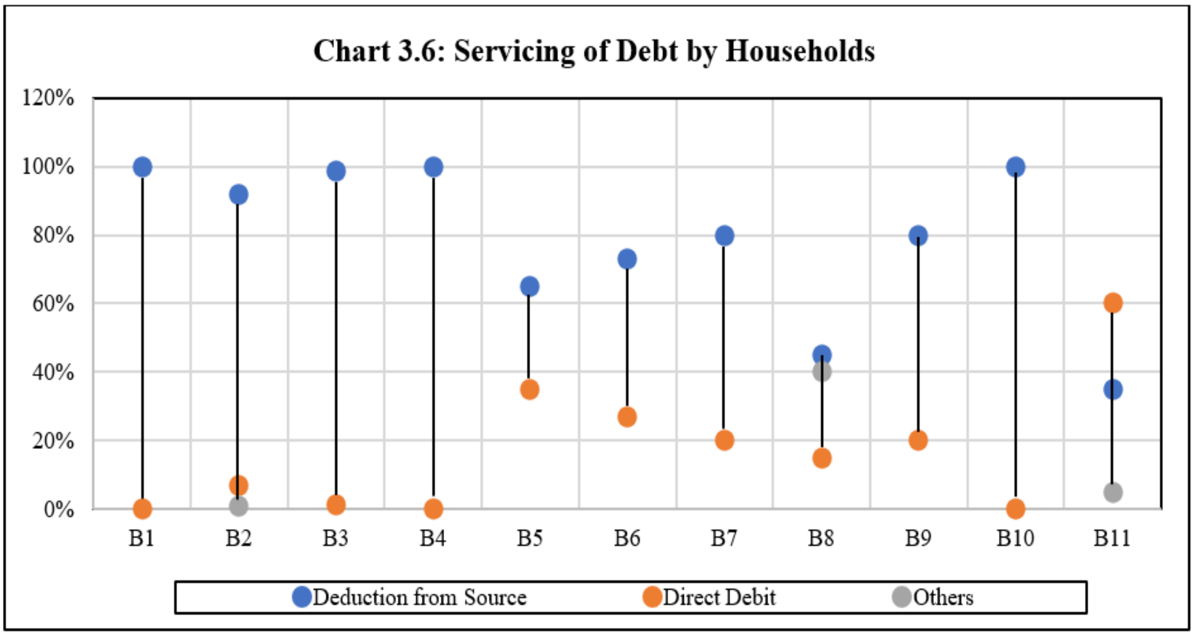
3.20 Across the banking sector, a total of 3 banks had scheme loans accounting for 75-100 percent of their household loans, 3 banks had scheme loans accounting for 50-75 percent of their household loans, 2 for 0-25 percent, 2 had no scheme loans and 1 for 25-50 percent (Chart 3.5). Total value of scheme loans for banks was approximately P29 billion (out of P48.7 billion of total banking sector household loans).

Chart 3.5: Number of Banks with Scheme Loans and Size of Scheme Loans



Source: Banks

3.21 All banks had their scheme loans paid through deduction from source arrangements. As regards the entire household portfolio, the percentage of households who serviced their debt directly from their payroll ranged from 35 percent to 100 percent; while those with a direct debit from personal bank accounts ranged from 1.4 percent to 60 percent (Chart 3.6). Some borrowers service their loans through over-the counter and bank transfers payments. As for hire-purchase stores, the majority of households service their debt through in-store payments (an average of 88 percent) and some microlenders deduct monthly repayments directly from the employer.



Source: Banks
Note: B1 to B11 represents banks that were surveyed.

(iii) Cost of Credit to Households

3.22 In the commercial banking sector, credit card loans were the most expensive (as high as 41.25 percent interest rate per annum), followed by unsecured personal loans (as high as 28.5 percent interest rate per annum) across all banks that have these facilities. Asset-backed facilities, mortgage and motor vehicle loans, are less risky to lenders and thus generally cheaper than other credit. Interest rates charged on mortgage loans, by commercial banks, declined from an average of 8.1 percent in December 2019 to 7 percent in December 2020, reflecting a reduction in the Bank Rate in 2020 from 4.75 in December 2019 to 3.75 in December 2020. Meanwhile, on average, interest rates for personal loans decreased marginally from 12.7 percent to 12.6 percent. In contrast, interest rates charged on credit cards increased from an average of 26.9 percent to 30.1 percent[6].

3.23 In addition to interest rates, banks imposed different types of charges, and these include administration/arrangement/processing fees, documentation fees, insurance fees, collection fees, facility fees and valuation fees. Some banks had early repayment penalty and credit reference or clearance fees. These fees were either proportionate to the loan amount (ad valorem) or fixed.

3.24 Interest rates charged on hire purchase ranged between 24 percent and 35 percent per annum over the period under review. Hire purchase stores also charge late payment fees, application and insurance fees. About 50 percent of micro-lenders who responded to the survey indicate that they charge an application fee and about 25 percent charge administration fees. Some microlenders charge interest rates as low as 7.5 percent per annum, and some as high as 50 percent per annum.

6 Credit cards are the riskiest of the credit facilities available at banks. Interest rates charged on them can be adjusted upwards or downwards to reflect the level of risk, usage and the timing of re-payments. These interest rates are not linked to the prime rate.

(f) Strategy Focus Amid the COVID-19 Pandemic

3.25 In trying to overcome the effects of COVID-19 pandemic, banks focused on enhancing and improving digitalisation in the provision of services, providing attractive interest rates to households, ensuring disciplined lending, growing the loan book and profitability in an uncertain environment; introducing new products that are relevant to the current environment; and embarking on customer education. Some banks indicated that reviews and analysis of both the banks' financial and credit data will continue to be done to ensure that banks maintain a proactive and sound credit risk environment, while at the same time pursuing a healthy and sustainable growth. In response to the pandemic, banks extended repayment holidays and offered debt restructuring to eligible borrowers.

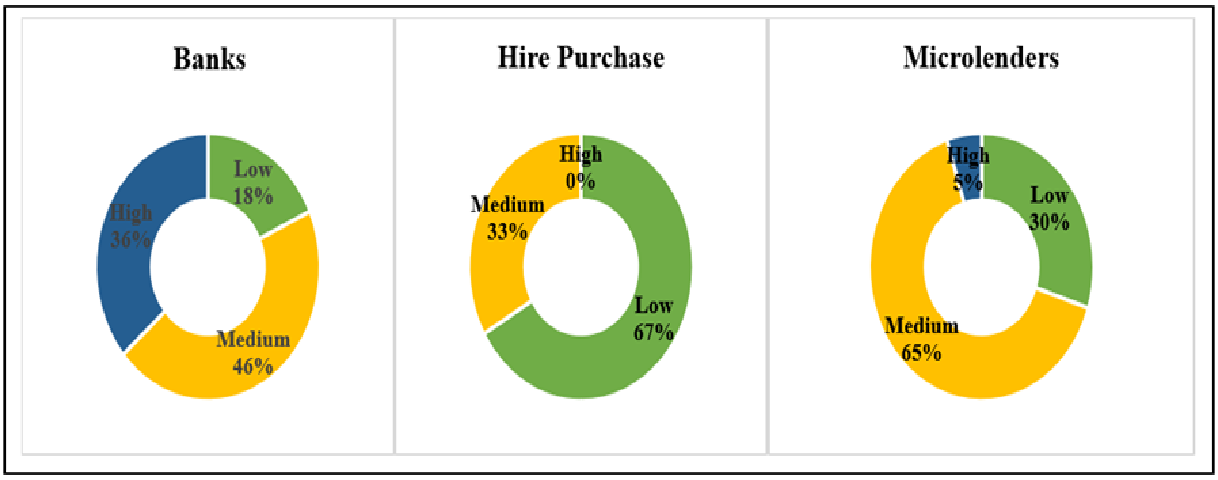
3.26 To mitigate risks associated with lending to the household sector, banks engage in extensive credit worthiness checks and arrange for deduction of monthly repayments from source and through direct debit (standing debit orders). Other risk mitigation measures include cession of credit life policies, obtaining retrenchment insurance covers, personal guarantees and mortgage protection policies. These measures are generally the same for microlenders. Hire purchase stores largely mitigate risks by carrying out extensive credit worthiness checks and obtaining retrenchment insurance cover.

(g) Demand for Credit - 2021 Outlook

3.27 Overall, microlenders (65 percent), banks (46 percent) and hire purchase stores (33 percent) generally viewed the outlook for demand for credit as moderate in 2021 (Chart 3.7). The COVID-19 pandemic was identified as a major factor affecting outlook for demand for credit in 2021. Banks explained that business operations were negatively affected and that the property market was expected to experience a slowdown as the pandemic has affected the ability to sell and slowed origination (process by which a borrower applies for a new loan, and a lender processes that application). Moreover, banks have indicated that the outlook is in line with Fitch's projections that Botswana's banking and financial services industry will face financial constraints associated with COVID-19 and its related restrictions. Similarly, microlenders have indicated that their credit outlook is informed by the COVID-19 related effects on the economy that has resulted in relatively low business activity, loss of employment and income, and in the absence of an increase in salaries of civil servants. Likewise, the risk of retrenchments and loss of income was highlighted by hire purchase stores as factors that informed their credit outlook.

3.28 Meanwhile, 67 percent of hire purchase stores, 30 percent of microlenders and 18 percent of banks stated that they expected demand for credit to be low in 2021. Absence of salary increments, reduction/loss of income as result of COVID-19 informs the expectations of banks and microlenders. The results of the survey also indicated that 36 percent of banks and 5 percent of microlenders expected demand for credit to be high in 2021.

Chart 3.7: Demand for Credit in 2021



Source: Banks, Hire Purchase Stores and Microlenders

4. CONCLUSION

4.1 Generally, the survey results, which were based on data sourced from banks, microlenders and hire purchase stores through the administration of online questionnaires, suggested minimal risks to financial stability posed by the level of household indebtedness in 2020. Credit was largely extended to the clientele that had the most secure jobs and the quality of the household loan book, for the largest credit provider (banks), was relatively good. To that extent, credit extension remains positive for economic activity and welfare enhancement, albeit costly for some categories. However, the functioning of credit markets was negatively affected by the COVID-19 pandemic as shown by the reluctance to provide credit by banks in 2020.

4.2 Banks continued to dominate in providing credit to households, with most loans in the form of unsecured personal loans. Many borrowers were employed by the Government; and most credit providers deducted monthly loan repayments at source, that is from the payroll, thus reducing the probability of default by borrowers. Finally, compared to the previous surveys, the DTI ratios were relatively unchanged in 2020 while the maximum LTV was 105 percent (an increase from 100 percent reported in the previous survey); and the DSR for banks ranged between 40 percent to 70 percent. Overall, there continues to be scope to significantly increase credit and, generally, financial sector role relative to the size of the economy (GDP) under the appropriate credit and risk management frameworks.

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