

Presentation to Standing Committee on Finance

21 August 2019



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1. Land Bank Mandate and Purpose
2. Strategy
3. Development
4. Business Model to deliver Development
5. Funding
6. Bank Operations
7. Financial Overview: Equity Performance



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RECOGNISING THAT

racially discriminatory practices and laws of the past and apartheid deprived historically disadvantaged people of land resulting in their **exclusion from the agricultural sector and racially skewed patterns of ownership of land in South Africa;**

IN ORDER TO

effect a change in the patterns of land ownership by promoting greater participation in the agricultural sector by historically disadvantaged persons and an increase in ownership of agricultural land by such persons through the provision of appropriate financial services;

IN ORDER TO

promote **sustainable agrarian reform and development of agricultural resources.**



Land Bank is committed to its Transformation & Developmental Mandate, as expressed in the ongoing Strategy and Operational Activities of the Bank.

Mandate of the Land Bank



The Mandate of the Land Bank, the Constitution and the National Development Plan highlights the importance of the agriculture sector to the country's development and transformation agenda...

Mandate:

The objects, as per the Land Bank Act, No. 15 of 2002, are the promotion, facilitation and support of:

- **Equitable ownership of agricultural land**, in particular increasing ownership of agricultural land by HDI's **Agrarian reform**, land redistribution or development programmes aimed at HDI persons;
- **Land access for agricultural purposes**;
- **Agricultural entrepreneurship**;
- **Removal of the legacy of racial and gender discrimination in agriculture**;
- **Enhancing productivity, profitability, investment and innovation**;
- **Growth** of the agricultural sector and better use of land;
- **Environmental sustainability** of land and related natural resources;
- **Rural development and job creation**;
- **Commercial agriculture**; and
- **Food security.**



Dual Nature of the Bank's mandate to support both:

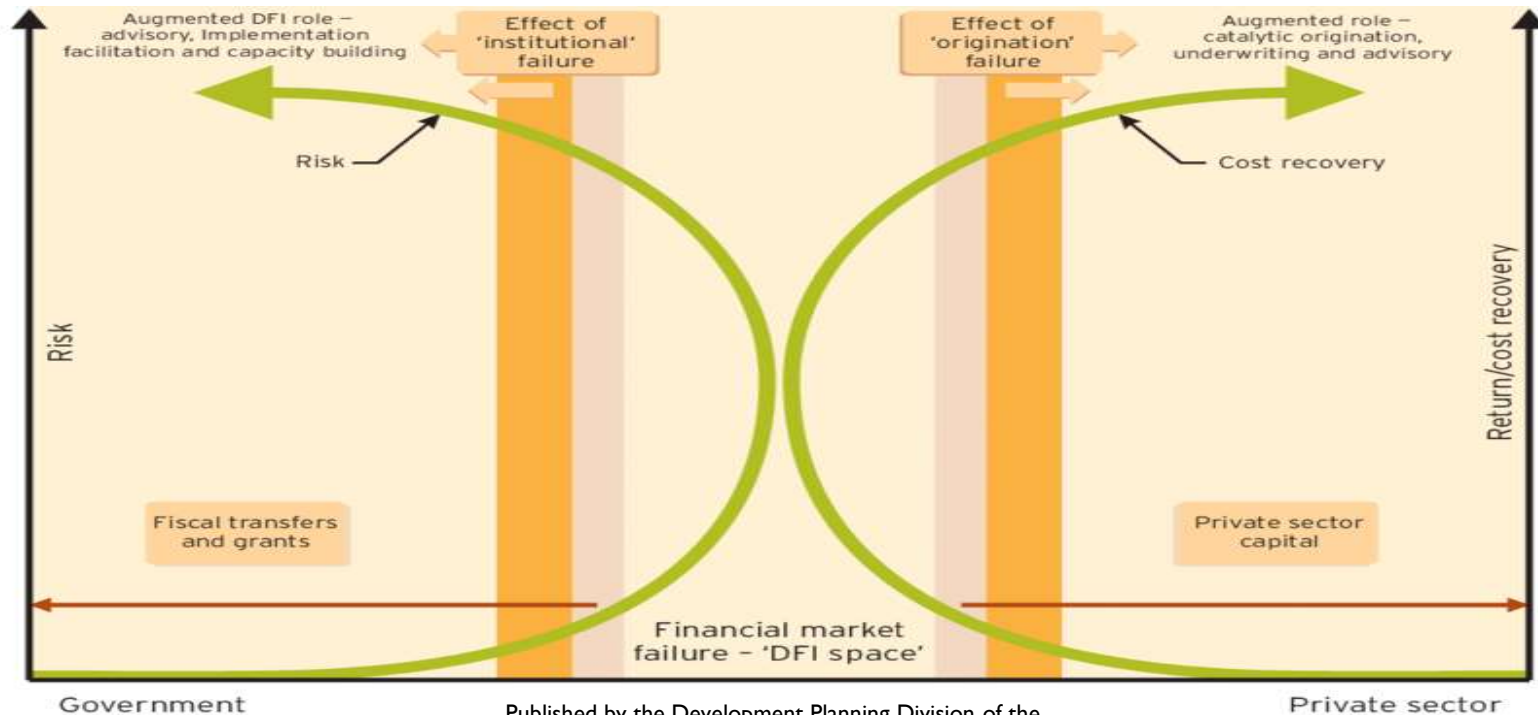
- Established Commercial Agriculture; and
- Emerging / Development Sector.



The Bank's purpose as a DFI is to provide financial services that transform, grow and protect the agricultural sector on a sustainable basis and to **close the gap created by market failure.**

Role of Land Bank as a DFI

Success depends on facilitated support from both Government and Private Sector



Published by the Development Planning Division of the
Development Bank of Southern Africa

- **Financial market failure** in the agricultural sector occurs because government departments do not have sufficient resources to support the crucial financial needs of agri-businesses (in particular, smallholder and development segment of the market) and commercial financial institutions do not have the investment appetite to address them.
- **Land Bank's role is twofold:** Finance development transactions effectively, and play an important part in the economic development strategies of SA.

Purpose of Land Bank's Existence:

Stakeholder Expectations



Shareholders

- Land Bank must be financially sustainable to ensure it is not dependent on the fiscus
- Must contribute to transforming the agricultural sector
- Must provide financial services to smallholder farmers
- Must provide financing at concessionary rates
- Must service subsistence farmers
- Must be well-governed
- Must be the leaders in the sector on Govt. position

Funders

- Financially sustainability
- Provide market related returns
- Strong corporate governance and Transparency
- Multilateral Funders expect Land Bank to provide financial services to small holders famers
- Responsible business practices for environmental and social governance
- Prudent risk management
- Some funders have imposed conditions regarding material changes in terms of disposal of assets, change in executive authority, and change in business model

Organized Agriculture

- Provide leadership with regards to development in the sector
- Support commercial agriculture
- Provide financial services to smallholder famers
- Credit requirement to all farmers must be softer than those of commercial banks
- Bank should be lenient in its requirements for collateral and security
- Provide financial services at affordable and concessionary rates
- Facilitate provision of Technical Support to smallholder farmers
- Must be financially sustainable
- Must be well governed

Client

- Support clients through good times and bad
- Support commercial farmers
- Provide financial services to smallholder and subsistence farmers
- Reasonable turnaround times on loan application and ongoing feedback
- Information on policy issues
- Accessibility through channels
- Provide solutions/guidance/options to commercial clients who want to embark on transformation
- Access to technical support and markets
- Must be easy to do business with Land Bank – less onerous requirement

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Strategic Development Objectives



Transformation



Sector growth



Employment
Quality



Food Security



Sustainable
Development

Strategic Pillars

1

Sector growth support

*Prioritise high-potential
regions
and crops*



2

Supply chain development

*Increase funding in agro-
processing*



3

Production expansion and intensification

*Support next-generation
farming*



4

Agri. innovation

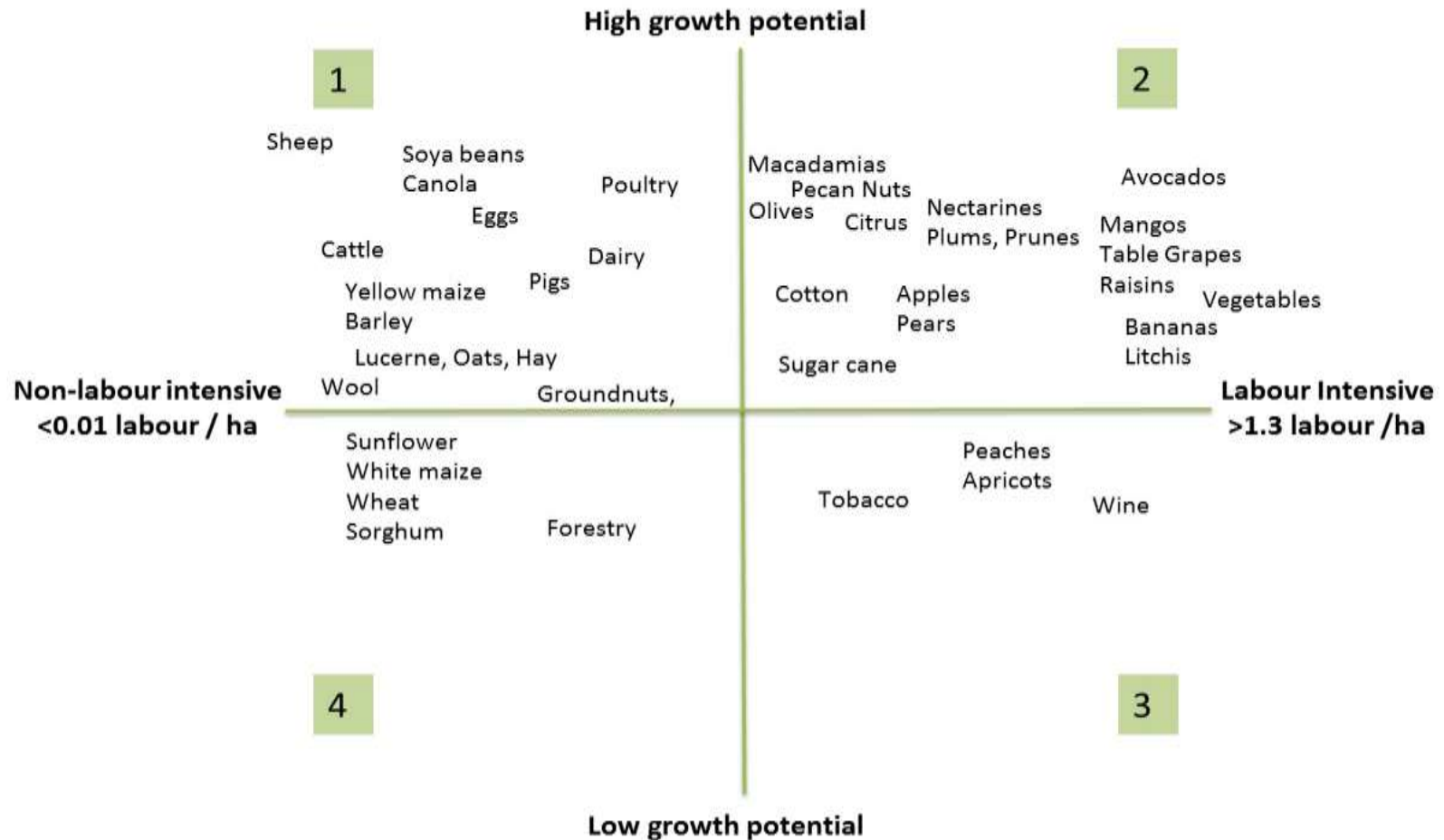
Spur agri. innovation



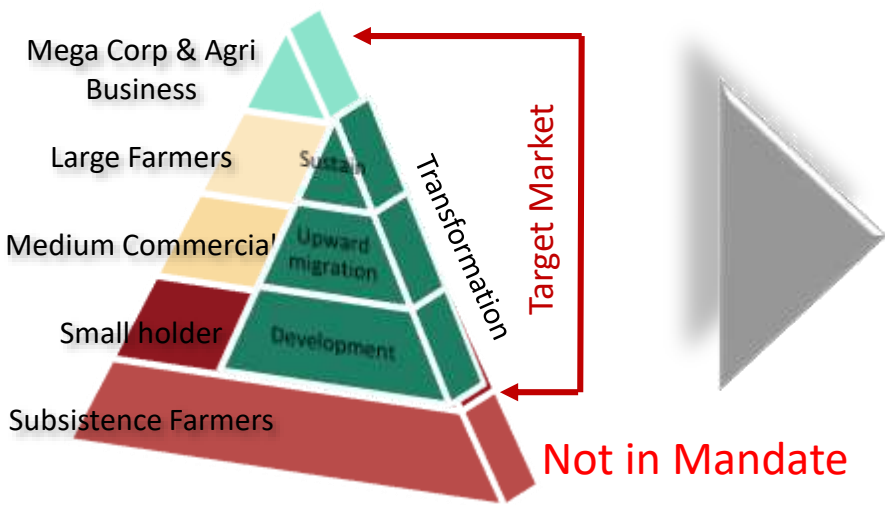
Growth Strategy:

Focus on Priority Commodities

Growth Strategy focused on High Growth potential and Labour Intensive commodities:



Agriculture Client Segmentation



Target Market Profile

AGRI BUSINESS	Established organisations that use agri-produce as an input in the manufacturing of their goods, or provides services or inputs to the agricultural sector. Not involved in primary agriculture, either food processing, commodity trading, input manufacturers or distributors of inputs and financing Turnover more than R50 million
MEGA / CORP	Well-established agriculture enterprise with high-end production and processing capabilities, and distribution networks. Majority of revenue from value-adding activities Turnover more than R50 million
LARGE FARMERS	These are established primary farming enterprises producing for market to make a profit with an annual turnover ranging between R10 million– R50 million
MED COM & EMERGING	Established primary agriculture farming enterprises Sound agricultural skill set and firm market access Growth phase business life cycle. Turnover between R1 and R10 million
SMALL HOLDER FARMERS	Practising primary agriculture on a viable piece of land, use technology, possess some skills and have adequate access to market to service a loan. Turnover less than R1 million
SUBSISTENCE FARMERS	Agricultural activities mainly undertaken to meet household food security needs, often located in a back yard, any surplus sold/bartered within community Little profit and no ability to service a loan

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Development Objectives

Strategic Development Objectives



Transformation



Sector growth



Employment
Quality



Food Security



Sustainable
Development

- **Transformation** of the sector through increased Black ownership and participation.
- **Sector growth** through projects/transactions which create additional production capacity.
- **Job creation** via agricultural value chain development and Employment quality, through upscaling black producers/employers.
- **Food security**, through increased production.
- **Sustainable development**, through provision of risk capital and industry business support that promotes sustainable agricultural practices.

Supporting the Emerging Sector

Differentiating Development and Transformation



Development

The term '**Development Loan Book**' will be limited to the support that will be provided by the Bank to **smallholder and medium scale commercial farmers** as per the definition of the Department of Agriculture, Forestry and Fisheries (DAFF):

- **Smallholder farmer** defined as a venture undertaken by an individual or business entity for the purpose of household consumption and deriving a source of income from agricultural, forestry and fisheries activities along the value-chain. These are usually the new entrants with an annual turnover of between R50,000 and R1 million.
- **Medium-scale commercial producer** defined as a venture undertaken by an individual or business entity for the purpose of deriving a source of income from agricultural, forestry and fisheries activities along the value-chain. These are established enterprises with an annual turnover ranging between R1 million and R10 million.

Transformation

The Land Bank Act places a specific responsibility on the Bank to contribute to the redressing of historical injustices of the past, specifically related to land ownership. It requires the Bank to transform the agricultural sector by increasing land ownership of previously disadvantaged persons.

Land Bank premised its **definition of Transformation transactions** as those undertaken by persons or entities that are:

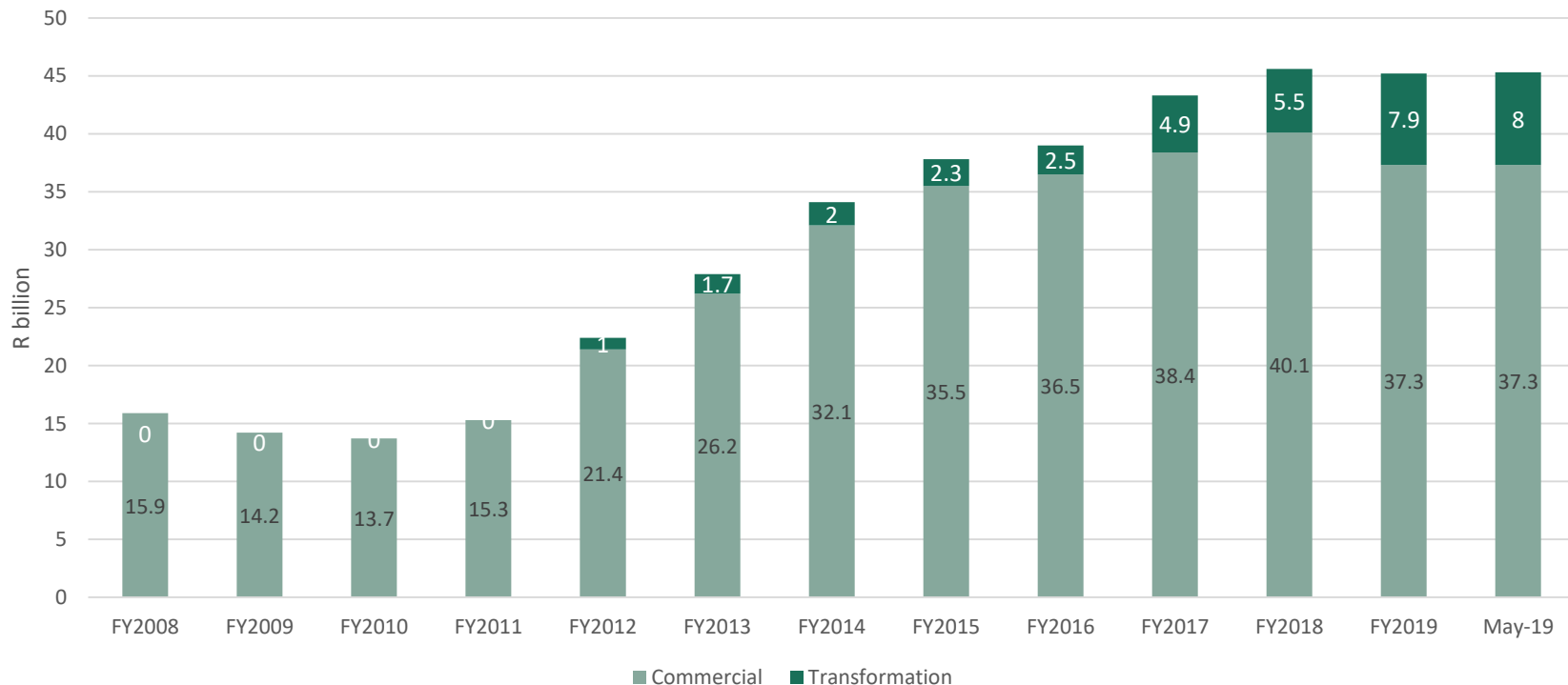
- Wholly Black-owned;
- Majority Black-owned (Black shareholding of 51% or more); or
- Substantially Black-owned (Black shareholding of between 30 and 50% and a BBBEE Level of 1 – 4).

Land Bank's Contribution: Development and Transformation



Based on the Corporate Scorecard definition of transformation, the absolute value of transformational loans as a percentage of the loan book is 17.7%.

Approximately R2 billion of this meet the narrow definition of development



Land Bank's contribution to development and transformation has increased significantly over the past years, but remains at levels below expectations

Supporting Development and Transformation

New Entrant Challenges

Some Challenges Faced by New Entrants:

Lack of **equity** for new-generation farmers

Lack of **affordable finance** for new-generation farmers

Lack of **collateral** for new-generation farmers

Lack of **skills, experience, and track record**

Lack of climate/environmental models for **risk management** in the sector

Lack of access to **value-chains** and market-related prices for production inputs

Lack of **coordination** of private sector funds / skills available to support new-generation farmers

Land Bank Products Assisting Emerging Farmers:

Special Mortgage Loan product for emerging farmers – interest rates initially subsidised and increased to commercial rates as business cash flow improves;

Longer term mortgage loans (25 years) to emerging farmers to improve affordability;

Land as collateral by emerging farmers taken at favourable loan to value ratio than for commercial applicants;

General interest rate subsidies for emerging farmers – offered through concessionary funding sourced by the Bank; and

Lending to emerging farmers in partnership with **intermediaries**, which includes **technical support and market access**, thereby supporting emerging farmers to successfully participate at various levels in the value chain.



To successfully close all these market failures, the Bank requires adjustment from its current “Lending-only Banking Model” to a model that will allow it to source funds and provide fee generating services (over and above funding purely from the capital and commercial markets). To do this, appropriate Funding Model is required.

Supporting Development and Transformation From Limiting Factors to Enabling Instruments



1. Addressing the Barriers to Entry

- Land Availability
- Business Plans inadequately prepared
- Regulatory Compliance (EIA, Water rights, etc.)
- Lack of Own Equity (Over geared Project Capital Structures))
- Market Access
- Technical Expertise
- Collateral

2. Structuring the Financing on a Sustainable Basis

- Affordability of Financing
- Flexibility of Terms
- Cash Flows and Repayability

3. Facilitating Institutional Support Measures for Ongoing Operations

- Production Planning
- Farming Operations
- Extension Services
- Inputs and Technology
- Marketing and Distribution
- Risk Management (Disease Management, Climate Change, etc.)

Cost of doing business in the development sector

The average conversion rate is poor for Development and Transformation clients relative to the Commercial clients, signalling the heavy costs and maintenance required to service this segment of the market.

Conversion Rate

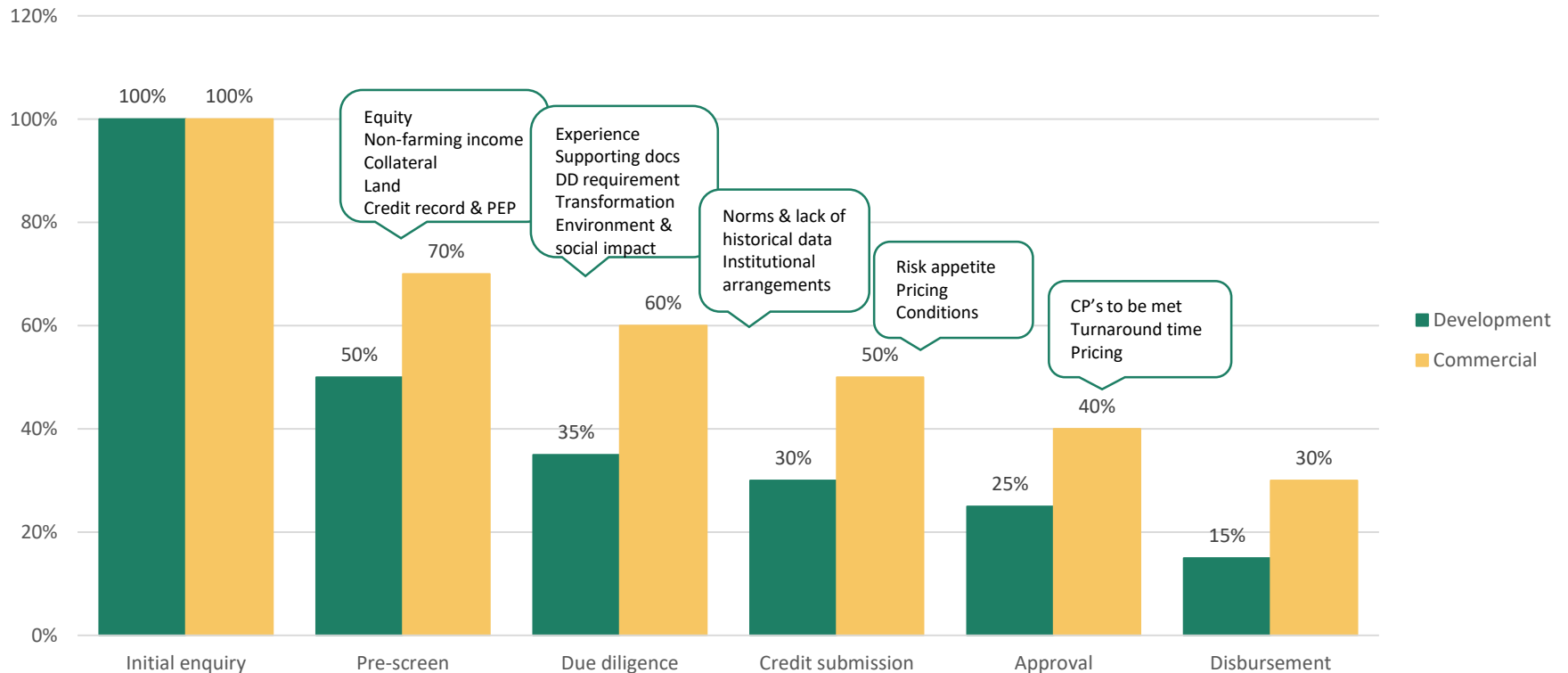


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Value Creation Model

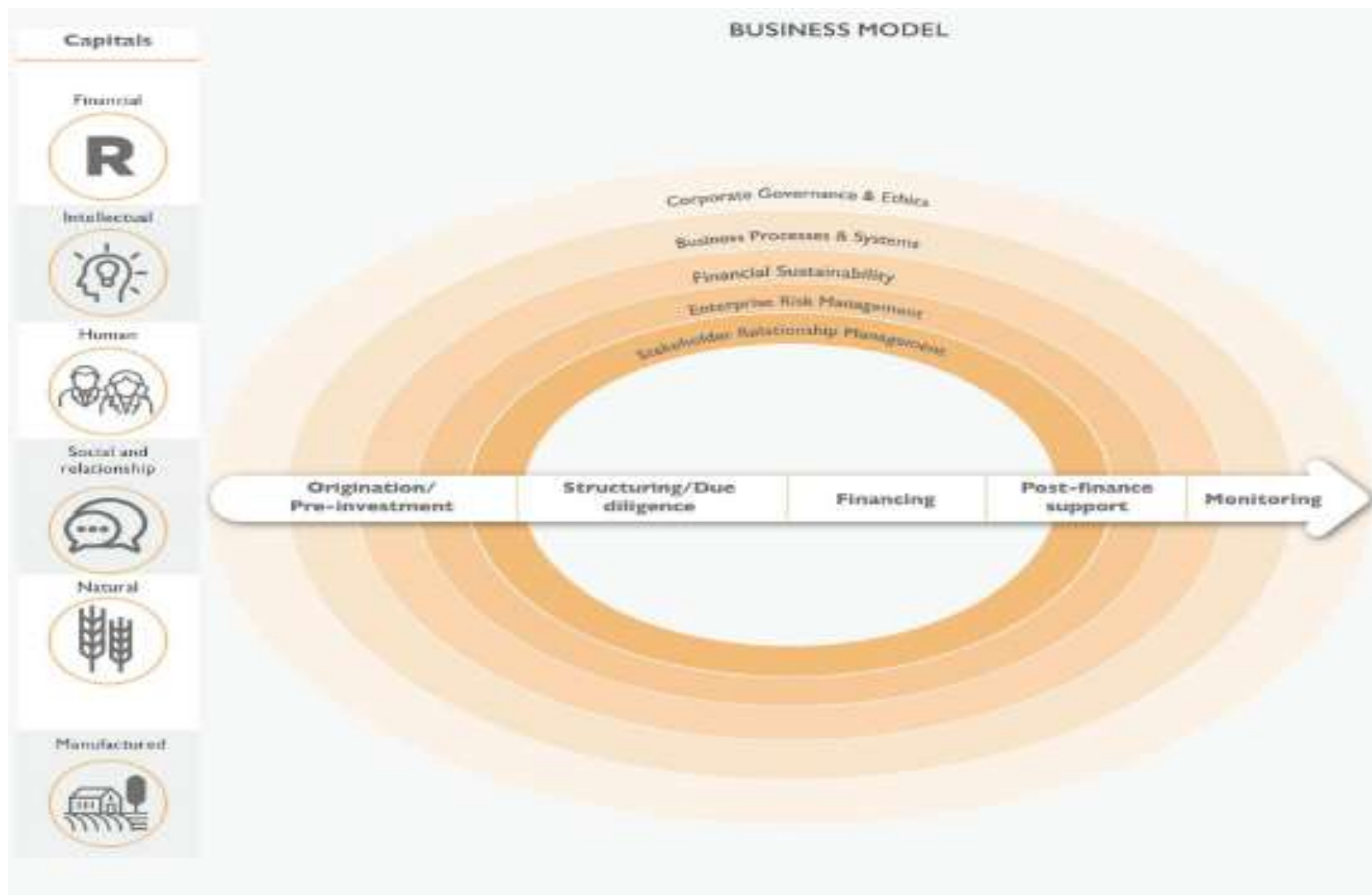


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Cost of Funding

The Bank raises funds from the capital markets at relatively expensive interest rates, and is therefore **constrained from providing affordable financing to development farmers.**

Loan Asset Pricing

Pricing Component

Cost of Funding

+ Liquidity Premium

+ Risk Premium

+ Operating Expense Recovery

= **Break-even**

+ Cost of Equity

= **Sustainable Break-even**

+ Profit Margin

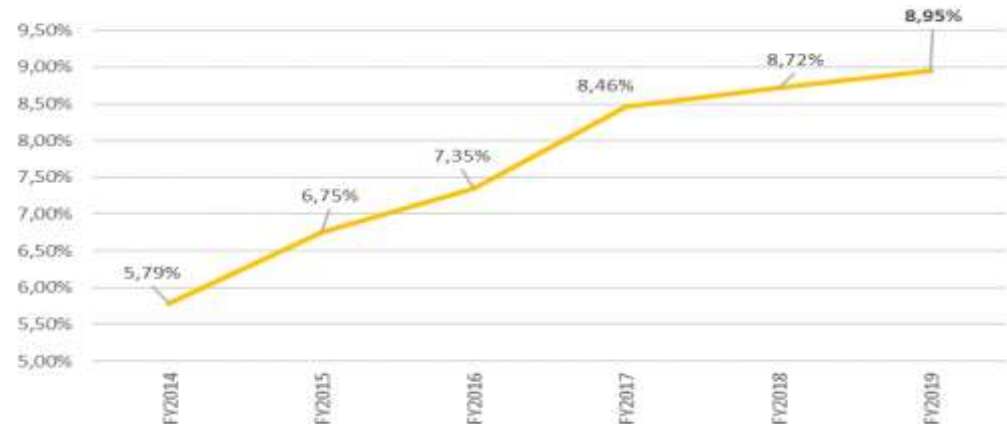
= **Loan Asset Price**

Weighted average interest cost per segment (2019 compared to 2018)

3 Month Jibar approximately 7%

Commercial Funding	3 month Jibar + 1.73% (2018:1.72%)
Development and Multilateral funding	3 month Jibar + 1.62% (2018: 0.68%)

Cost of Funding



- The cost of funding increased from 6.79% in 2014 to 8.95% currently;
- This is as a result of the Bank changing the mix of its liabilities from short term to long term funding;
- The mix in 2014/15 was 69% short dated and 31% long dated, which has since shifted to a 50% : 50% split between short and long term funding
- The increase in the Development and Multilateral funding from 2018 to 2019 was due to the change in counterparty (AFD to World Bank)

Land Bank's Funding Dichotomy

Conflicting Expectations

← Transformation / Development



Commercial →

Small Agribusinesses (Transformational / Developmental):

- Bank has a self-funding mandate, without direct financial support (other than guarantees for raising funding) from the state;
- Organisational growth and sustainability has to be achieved internally;
- Bank's own funding requirements primarily accessed competitively (financial markets) at commercial rates; and
- Necessary to generate margins over commercial borrowing rates to fund operations, maintain and grow own equity base and ensure sustainability.

The erratic / unpredictable availability of Funds from sector departments makes long term planning difficult.

It is suggested that consideration be given by National Treasury for direct appropriation / allocation of funds to the Bank.

Borrowing and Sustainability (Commercial):

- Strong transformational & developmental characteristics, borrowers with limited own resources, low debt affordability - low cost funding;
- Higher risk transactions without concomitant risk pricing; and
- Financial exposure further amplified due to generally lower debt collateralisation versus transactions typically serviced by commercial banking peers.

Take Note

Land Bank, as a DFI, is faced with conflicting goals and opposing imperatives in respect of development objectives and financial sustainability:

- Conflicting sustainability and transformational imperatives
- Mismatch between source and application of funds

Land Bank's Funding Dichotomy

Prioritisation Dilemma



The Land Bank must continue to:

- Run a financially self-sustainable business; whilst
- Delivering significant improvement to its developmental and transformation mandate

The cost of delivering transformation and development funding support is higher than the Bank is able to afford on its current funding and revenue-generating business model.

Given the challenges faced by new commercial entrants and smallholder commercial farmers the Bank aims to obtain and leverage on appropriate government support for:

- Capital and equity support to the Bank;
- Subsidy support to the Bank in order to contribute towards affordable financing; and
- Funding support to enable the Bank to provide pre- and post-finance support services that are essential for the development of new commercial entrants and smallholder commercial farmers.

The ability to achieve both the financial self-sustainability objective and the transformation agenda requires:

- a review of the Bank's funding structure which is currently fully dependent on raising relatively expensive (commercially-priced) funding from the capital markets; and
- and through loans from Multilateral Development Institutions which are not priced at concessionary levels.



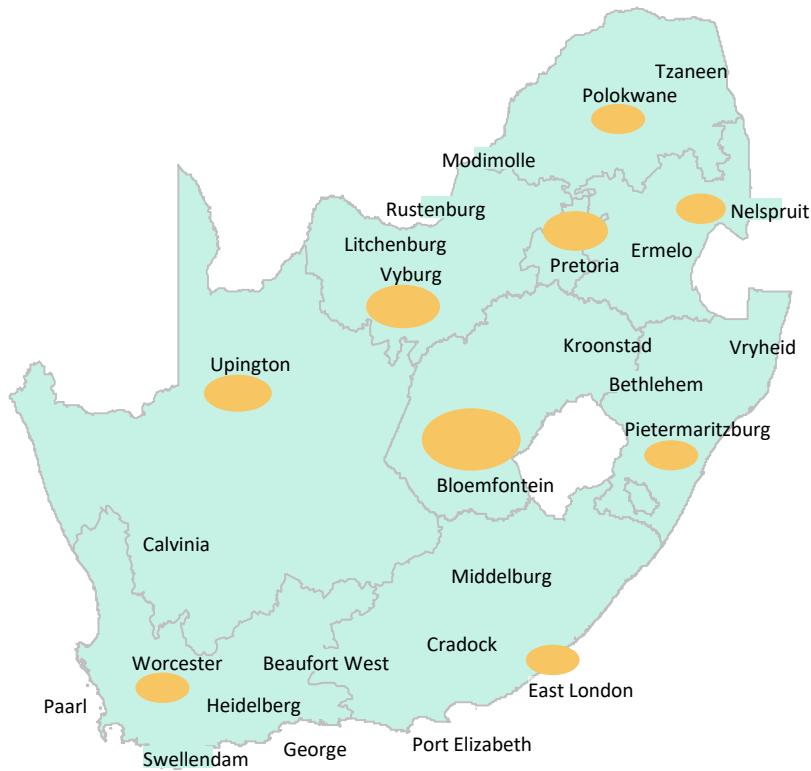
The Bank will require government funding support to accelerate its developmental mandate

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Land Bank Channels: Coverage and Reach



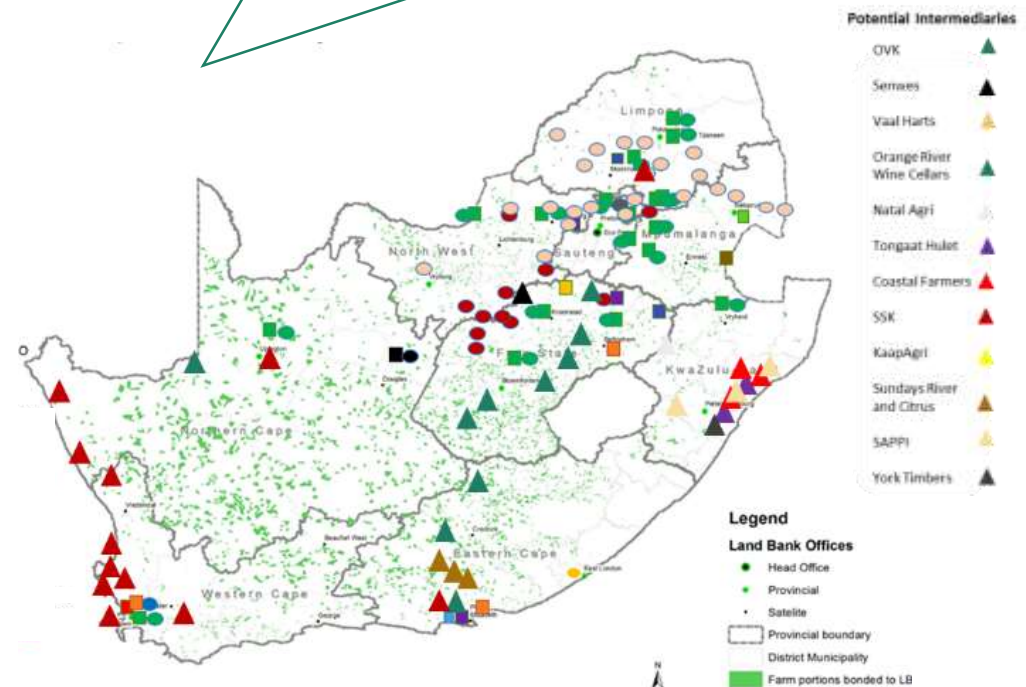
The structure provides co-dependent relationship that enhanced both parties support to the Agricultural sector:

Land Bank:

- Wider footprint
- Single obligor limits problems with Corporate clients

SLA Partner

- Guaranteed liquidity
- Admin fee and net margin sharing



Channel Operating Model

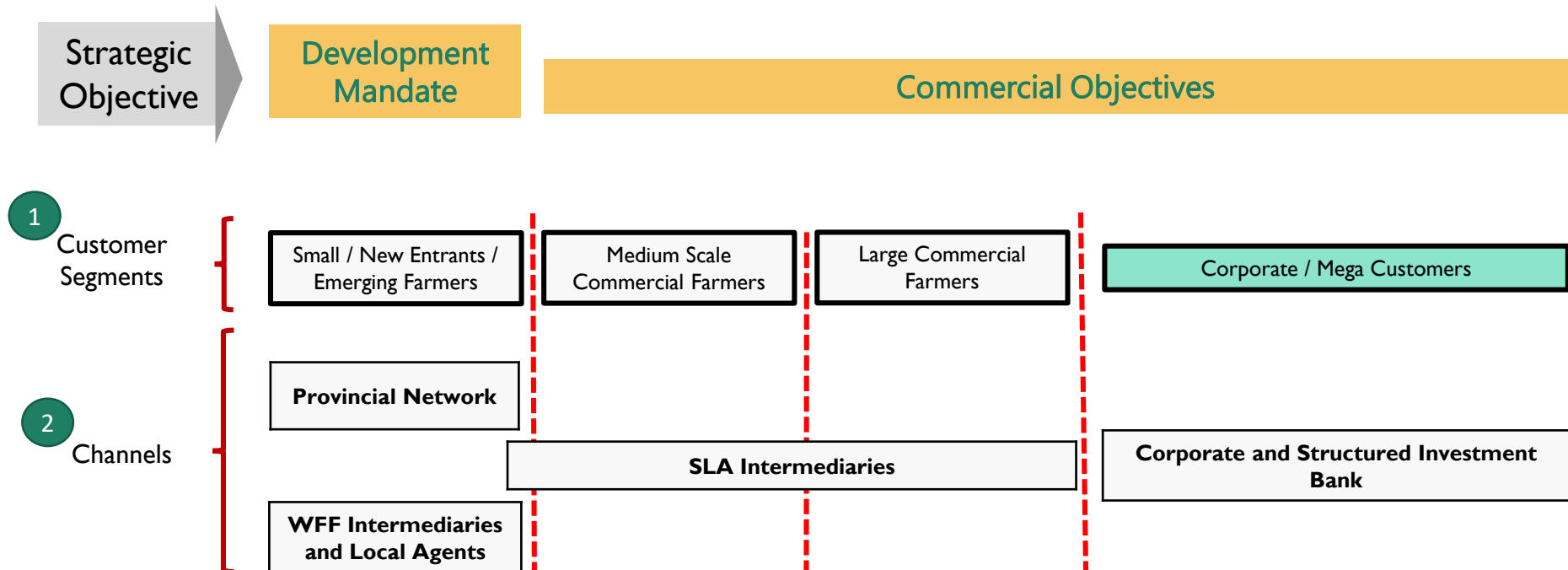


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Financial Overview: Equity Performance



	FY2008 R'm	FY2009 R'm	FY2010 R'm	FY2011 R'm	FY2012 R'm	FY2013 R'm	FY2014 R'm	FY2015 R'm	FY2016 R'm	FY2017 R'm	FY2018 R'm	FY2019 R'm
Opening Balance	1,015	1,710	1,960	2,900	3,896	4,831	5,185	5,750	6,670	5,063	5,365	5,547
Recap from NT	700	-	1,000	747	750	200	300	500	-	-	-	-
Revaluation Reserves	15	10	15	2	5	13	2	1	6	2	0.2	0.9
MtM Reserves	-	-	-	-	-	10	4	(4)	(6)	0.4	(45)	(0.2)
IFRS adjustments	-	-	(278)	-	(23)	-	-	-	(1,679)	-	-	-
- Prior period error	-	-	(278)	-	(23)	-	-	-	-	-	-	-
- IFRS 9	-	-	-	-	-	-	-	-	(1,679)	-	-	-
Profit and Loss incl. OCI	219	369	271	293	247	169	288	464	107	258	219	115
- Profit/ (Loss)	219	369	271	315	277	192	272	481	130	269	279	131
- OCI Profit/ (Loss)	-	-		(21)	(31)	(23)	16	(17)	(22)	(11)	(60)	(16)
Sub Total	1,949	2,088	2,968	3,942	4,875	5,223	5,779	6,711	5,098	5,323	5,539	5,663
Discontinued Ops	(239)	(128)	(68)	(45)	(45)	(38)	(29)	(41)	(36)	48	(36)	13
Total	1,710	1,960	2,900	3,896	4,831	5,185	5,750	6,670	5,063	5,365	5,547	5,675

THANK YOU!



- 420 Witch-Hazel Avenue
- Eco Glades, Block D, Eco Park
- Centurion Pretoria

