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The Land and Agricultural Development Bank of South Africa- Brief Summary of 2018/19 Annual Report

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1. Introduction

In South Africa, Development Finance Institutions (DFIs) such as the Land Bank have a key role to play in promoting economic growth and supporting social development. DFIs operate in the intermediary space between public aid and private investment, where they provide credit and a wide range of capacity-building programmes to households, small, medium, and micro enterprises (SMMEs), and even larger private corporations whose financial needs are not sufficiently served by commercial banks or local capital markets. In the case of the Land Bank, the role of this particular DFI is to address areas of market failure¹ in the agricultural finance market.

The Land Bank seeks to promote inclusive agricultural and rural development for improved food security and economic growth. In particular, it seeks to provide appropriate financial services that: 1) transform and foster an inclusive agricultural sector by increasing agricultural land ownership and promoting greater participation by previously disadvantaged persons; 2) promote sustainable agrarian reform; 3) develop land and other agricultural resources on a sustainable basis; 4) promote a competitive and profitable agricultural sector².

This paper provides a brief overview of the agricultural sector and some of the challenges that may have implications for how the Land Bank carries out its mandate. It further provides a brief summary of the Bank's 2018/19 financial and non-financial performance.

2. Legislative Mandate

The Land Bank is constituted in terms of the Land Bank Act, No. 15 of 2002³. As set out in Section 3(1) of the Act, the objects are the promotion, facilitation and support of:

- Equitable ownership of agricultural land, in particular increasing ownership of agricultural land by historically disadvantaged persons
- Agrarian reform, land redistribution or development programmes aimed at historically disadvantaged 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
- Food security

¹ A market failure is a situation where free markets fail to allocate resources efficiently due to issues such as monopoly power or negative externalities

² Land Bank (2019a)

³ Ibid



3. Funding Sources

The Land Bank obtains or raises funding for two distinct business purposes, namely commercial operations and development operations. Commercial funding is raised from institutional investors and commercial banks and the funding is usually unguaranteed, whilst development funding is raised from multilateral institutions and this type of funding often requires government guarantees⁴. Commercial funding grew by 5.3% from R40.07 billion in 2018 to R42.17 billion in 2019. Even though the size of development funding is significantly smaller than commercial funding, it has, however, grown faster between 2018 and 2019; it grew by 48% from R1.19 billion in 2018 to R1.77 billion in 2019.

4. Brief Overview of the Agricultural Sector

Sector Growth

Owing mainly to the late start to the grain planting season and diseases in various livestock sectors as well as the drought experienced in several areas across the country, sector growth has declined. In the first quarter of 2019 the sector contracted by -13.2%⁵.

Employment

Table 1 below shows employment in the agricultural sector between 2015 and 2019. It reveals that employment in the agricultural sector has remained low. In particular, between 2015 and 2019 the number of employed persons only grew by 2.9%. Worryingly, there has been a 32% decline in skilled agricultural jobs between the first quarter of 2017 and the first quarter of 2019⁶.

Table 1. Employment in Agricultural Sector

	Q4 : 2015	Q4: 2016	Q4:2017	Q4:2018	Q4:2019
Number Employed	860 000	919 000	849 000	849 000	885 000

Source: Quarterly Labour Force Survey (2008-2019)

Food Security

At the national level, South Africa can be regarded as food secure but at the household level food security remains a challenge. In 2017, 6.8 million people experienced hunger and 20% of households did not have adequate access to food⁷. Limpopo had the highest number of households that had adequate access to food, whilst households in the North West, Northern Cape, Eastern Cape, KwaZulu-Natal and Mpumalanga had the highest number of households reporting inadequate access to food.

⁴ Land Bank (2019a)

⁵ Ibid

⁶ Ibid

⁷ Statistics SA (2019b)



5. Challenges Faced by the Agricultural Sector and the Land Bank

The main challenges that are facing the agricultural sector and the Land Bank relate to:

- **Continuous drought conditions** – negatively affects agricultural outputs and the Bank's loan book⁸
- **Debt** - is growing significantly in the sector, which may have adverse effects for agricultural lending for the bank⁹
- **Land Reform**– uncertainty around regulatory proposals for land expropriation without compensation remains a strategic risk for the Bank¹⁰
- **Downgrade by Moody's Investor Service**–it has direct and indirect implications for the agricultural sector. For example, the Bank might have to revise their pricing model for individuals and businesses. It may force the Bank to lend at higher interest rates. Farmers will be the most affected as it will make it harder for them to access affordable financing; farmers' debt will increase; employment will fall; there will be a reduction in investment in the sector; adverse effect on food security¹¹

6. Financial and Non-Financial Performance

6.1. Corporate Governance

Internal Control

A case of fraud was investigated in the 2019 financial year. A loan of R100 000 was disbursed to a client to purchase cattle, however the client utilised the loaned funds for other non-agricultural business¹².

Other internal control deficiencies that were noted were that management did not in all instances prepare regular, accurate and complete financial performance reports that are supported and evidenced by reliable information. Furthermore, management did not in all instances review and monitor compliance with applicable laws and regulations as the annual financial statements submitted for audit did not comply disclosures on collateral held as security and loans by credit quality as required by International Financial Reporting Standards.

External Audit Report

The financial statements present fairly, in all material respects, the financial position of the Land Bank as at 31 March 2019. There were no material findings on the usefulness and reliability of the reported performance information for the following objectives: contribute to transformation in the agricultural sector; environmental sustainability; and financial sustainability.

⁸ Land Bank (2019a)

⁹ Land Bank (2019a)

¹⁰ Ibid

¹¹ Land Bank (2020)

¹² Land Bank (2019a)



With respect to the report on the audit of compliance with legislation, material misstatements on disclosures of collateral held as security and loans by credit quality were identified during the audit in submitted financial statements.

6.2. Loan Book Performance and Amounts Owed to Related Parties

Table 2 below compares the Bank's loan book performance in 2018 with that of 2019. It shows that, whilst performing loans account for the bulk of the loan book, their performance has declined between 2018 and 2019. What is of concern is that under-performing and non-performing loans are growing.

Table 2. Loan Book Performance, 2018-2019

	2018	2019
Performing Loans	85.7%	82.1%
Under-performing Loans	7.6%	9.1%
Non-performing Loans	6.7%	8.8%

Source: Land Bank 2019 Annual Report

Amounts owed to related parties has grown by 50% from R503.74 million in 2018 to R755.98 million in 2019, where the amount owed to the Department of Agriculture, Forestry and Fisheries accounts for the bulk of this amount¹³.

6.3. Key performance indicators and targets

Table A1 in the annexure compares the targeted or planned performance with the actual performance. The performance indicators are based on seven material matters that are most relevant to the achievement of the Land Bank's mandate and sustainability objectives for 2018/19, namely:

- 1) **Financial sustainability** - ensuring that the Land Bank operates on a financial sound basis so as to sustainably support the sector
- 2) **Development Outcome and Transformation** – ensuring that efforts aimed at addressing historical injustices also reach smallholder farmers in the sector
- 3) **Corporate Governance** – ensuring sound governance
- 4) **Employee Development, Retention and Remuneration** – finding ways to attract and retain talented leadership and a strong complement of capable management to lead and manage the organisation
- 5) **Technical advancement (Innovation)** – strengthening IT capabilities and making use of advanced technology
- 6) **Climate Risk and Environmental Sustainability** – understanding and managing climate risks; ensuring long-term environmental sustainability

¹³ Land Bank (2019b)



7) **Poorly executed Land Expropriation without Compensation** – monitoring and understanding the implications that it has on national food security, sustainable farming the economy

With respect to the performance indicators that relate to development outcome and transformation, corporate governance and climate risk and environmental sustainability, the Bank achieved good results. With respect to financial sustainability, only 37.5% of the targets were met. The factors that contributed to this poor performance relate to the ongoing drought and changing weather patterns that have affected the Bank's ability to grow its loan book. The climate risk effects have also meant that some farmers have been unable to repay their loans, which serves to increase the rate of non-performing loans. Other factors include the sovereign credit downgrades that have resulted in costly funding and several livestock diseases that have had a negative effect on exports.

7. Issues for Consideration

a. Restoring Stability

Given the recent downgrade to junk status, the poor performance of the loan book (particularly in respect of growing non-performing loans) and the lack of stability in the Bank's leadership, what measures are being put in place to restore or ensure stability?

b. Implications of Proposed State Bank

In the 2020 Budget Speech, the Minister of Finance announced that National Treasury is ready to set up a state bank, where he spoke to the idea of consolidating "the currently fragmented system of national and provincial Development Finance Institutions":

- What is the Bank's position on this?
- Does the Bank have any concerns around this? What should the Committee be worried about?
- What would be the implication for the Bank's mandate or its role in the agricultural sector?

c. Transformation and Inclusive Growth in the Agricultural Sector

In understanding that the Bank has a dual mandate of supporting both commercial and emerging agriculture positions, what is evident, however, is that the Bank is biased towards agricultural commercial business, which would suggest that the Bank's source of capital is a key determinant of its lending and the type of risk it is committed to taking on:

- How then is the Bank's model different from that of commercial banking if the developmental role remains limited?
- The limited development role adversely impacts rural development because it would mean that emerging farmers in rural areas are excluded. It also has implications for food security in rural areas (where poverty and food insecurity is highest). Roughly, what percentage of funding or transformational loans goes to towards emerging farmers and household producers in rural areas specifically?



- Are all your clients charged the same interest rates e.g. Would commercial farmers be charged the same rate as emerging farmers or household producers? If not, what criteria do you use to determine who gets charged what?

d. Land Expropriation without Compensation

What is the Bank's position on this?

8. Conclusion

Whilst there have been positive outcomes with respect to development and transformation outcomes and outcomes relating to human capital and climate risk and environmental sustainability, more attention needs to be given to the issue of financial sustainability as it has a direct bearing on how the Bank carries out its mandate.

9. References

Land Bank. (2019a) Integrated Annual Report 2019.

Land Bank. (2019b) Annual Financial Statements 2019.

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Statistics SA. (2019a) Quarterly Labour Force Survey (2008-2019).

Statistics SA. (2019b) Towards Measuring Food Security in South Africa: An Examination of Hunger and Food Inadequacy. [Online]. Available at: <http://www.statssa.gov.za/publications/03-00-14/03-00-142017.pdf> (Accessed on 6 March 2020).

10. Annexure

Table A1. Achievement of Key Performance Indicators, 2018/19

Strategic focus area/Material Matter	Target	Actual	Achieved/Not achieved
Financial sustainability	Achieve R310 million in profit	R130.6 million	Not achieved
	3.1% interest income margin to equate to R1.38 billion in net interest income generated	2.7% (R1.2 billion net interest income generated)	Not achieved
	Cost-to-income ratio $\leq 54\%$	57.1%	Not achieved
	Gearing Ratio $\leq 535\%$ calculated as Interest Bearing Debt divided by	649.5%	Not achieved



	Capital at a Group level		
	Non-Performing Loan (NPL) \leq 7% (International Financial Reporting Standards 9 definition)	8.8%	Not achieved
	Capital Adequacy Ratio(CAR): \geq 15%	16.4%	Achieved
	Net Stable Funding Ratio(NSFR): \geq 100%	102.0%	Achieved
	Liquidity Coverage Ratio(LCR): \geq 80%	549.8%	Achieved
Development outcome and transformation	Disburse R2.5 billion to increase ownership of agricultural land and enable agricultural production by historically disadvantaged individuals: CRITERIA: (i) At least 50% of disbursements to majority Black ownership; or BBBEE Level 4 and higher and \geq 30% Black ownership	R5.07 billion	Achieved
	Provide R0.5bn proprietary equity financing/investments (including preference shares) to enable economic ownership transformation	R611.9 million	Not achieved
	Originate transactions to provide R500 million Land Bank funding	R2.25 billion	Achieved



	to leverage third party funding to co-finance majority Black-owned transactions including grants, private equity, syndicated debt, etc.		
	Finance projects/enterprises with majority Black participation by women, youth and/or employees to support inclusivity in the sector with aggregate value of R600 million, as part of the total disbursement of R2.5bn (or, in addition to R2.5bn above)	R2.468 billion	
	Finance projects/enterprises aimed at expanding productive capacity (greenfields and brownfields) in the sector with an aggregate value of R300 million, as part of the total disbursement of R2.5bn	R307.3 million	Achieved
Corporate governance	Classify 0% (R value) of operating expenses as irregular, fruitless or wasteful expenditure	R140,000 irregular expenditure R0 fruitless and wasteful expenditure	Not achieved
	No findings on unethical behaviour by a staff member	2 findings	Not achieved



	Achieve clean audit	*Performance not indicated in annual report	
Employee development, retention and remuneration	% of Black women in Senior and Executive Management: 25%	25.0%	Achieved
	% of Black women in Professional qualified & Mid-Management: 25%	21.8%	Not achieved
	% of ACI staff: 65%	68.7%	Achieved
	90% of critical roles retained (average over year)	92.3%	Achieved
	Implement 50% of culture survey initiative plan based on survey results from 2018/2019 to improve employee value proposition	60.0%	Achieved
	At least 65% of training budget spend on ACI staff	72.0%	Achieved
Technical advancement (Innovation)	New material matter – no indicators	N/A	
Climate risk and environmental sustainability	Utilisation of at least R80m of EIB climate facility	R118 million	Achieved
Poorly executed Land Expropriation without Compensation	No indicator	N/A	

Source: Land Bank 2019 Annual Report