

Land Bank update: A Snail's Pace**Author: Olga Constantatos, Head of Credit @ Futuregrowth****Published: September 2021**

Since our last update on 22 June, progress on resolving Land Bank's issues has been at a snail's pace. Nonetheless, given Land Bank's presentation to Parliament's Standing Committee on Appropriations (SCOA) on 24 August, it is opportune to give an update on the Land Bank event of default.

At the time of our last update, a summarised set of high-level results for the financial year ended 31 March 2021 had been released, and we provided brief commentary on these results in that update. As of today, the full audited annual financial statements remain outstanding.

Proposed splitting of the Land Bank book

The Land Bank presentation to SCOA outlines the proposed splitting of the Land Bank loan book into a "Corporate and Commercial Book" (C&C book) and a "Developmental and Transformational Book" (D&T book). While this would be a notional and operational split - and not a legal separation - the proposal does materially change creditors' rights. This proposal is termed "version 3" of the liability solution.

Accordingly, it is proposed that the South African funders (i.e. the South African institutions, some SOEs and the commercial banks that invested in Land Bank unguaranteed, listed and unlisted paper), will look to collections from the C&C book for loan recovery, and international DFI¹ and guaranteed funders will look to the D&T book for their repayment.

It is important to state that the event of default from April 2020 remains unresolved, negotiations for the proposal to split Land Bank's activities are still underway, and lenders have not yet agreed to the latest liability solution proposal.

It appears to us, from discussions and from the most recent presentation to SCOA, that government (as Land Bank's shareholder) is determined to split the book, and essentially and meaningfully reduce Land Bank's scope and size of operations. Notably, it appears the R5 billion appropriation from this year's Budget is conditional on Land Bank shifting its focus increasingly to its developmental and transformational mandate.

This is the shareholder's right, and we are not questioning the need to meaningfully transform the agricultural sector and provide support to South Africa's developmental farmers. However, we question whether the full impact and possible financial and fiscal implications of this have been considered. Specifically, we understand that historically the C&C operations (and the profits and cashflows generated from this part of Land Bank's activities) have been used to effectively subsidise the D&T activities - in providing funding to developmental farmers at subsidised interest rates and in ensuring that the operational costs of Land Bank (around R600 million per annum) are funded. In reducing the scope and size of Land Bank - by winding down the C&C operations, and hence reducing the C&C's contribution to Land Bank's total profits and cashflows - we believe that additional financial support from the shareholder may be required to finance the D&T book and operations. In an environment where the shareholder is fiscally constrained, we question whether this possible future financial obligation on the fiscus has been fully considered.

Independent Review of Land Bank

The lenders have insisted on an independent financial review of Land Bank - and this is also mentioned in the SCOA presentation. This review has been set so that we, as lenders, can assess our current position against Land Bank's latest proposal. We are now eighteen months into a continuing default, and the lenders have not yet been provided all the relevant information we need to properly assess the

¹ Development Finance Institution

liability solution. We believe that the outcome of the proposed independent review is a key piece of the puzzle for us as lenders to evaluate our position and decide how best to proceed.

Capital repayments

You may recall that Land Bank repaid about 12% of outstanding capital to all funders in February 2021. This was done in accordance with Land Bank's commitment to treat all creditors fairly given that its international DFI funders were being repaid a similar proportion of capital in terms of their amortising loan profile (which requires capital to be repaid in February/March and September/October each year).

These international DFIs have 6-monthly amortisation payments and their September/October capital redemption is coming due. In response to this, and to continue to treat all funders fairly, Land Bank repaid an additional 10% of outstanding capital to unlisted note holders during July/August 2021.

Listed noteholders have an additional process to go through to get their additional 10% back, as outlined below.

Delisting of Land Bank's bonds

At the time of the February 2021 capital repayment, the listed notes were not suspended, and so unlisted and listed noteholders were repaid simultaneously. The current repayment is slightly different and listed noteholders have to wait for their additional 10% to be repaid. This is because the listed bonds are currently suspended, and the JSE has been unable and unwilling to allow the return of capital to investors on suspended bonds.

Hence, there is a process underway for listed noteholders to vote on a noteholder resolution to delist the Land Bank bonds as a precursor to the 10% capital redemption being made to listed noteholders. Because of the JSE's rules, the bonds must be delisted in order for the capital to be repaid. Therefore it is essential that all noteholders vote on this important resolution if they would like to participate in this capital reduction process. A reminder to all noteholders was issued in the latest SENS, dated 19 August 2021. It is expected that *if the required majority of noteholders pass each resolution* (each note requires a separate resolution), then the additional 10% capital repayment to listed noteholders will be made during September/October 2021.

Untenable situation for listed noteholders

The matter of the JSE not allowing the partial return of capital to investors *on a defaulted listed note* speaks volumes about the JSE's priorities and willingness to protect bond investors. This is a subject we have written about extensively – [have a look here](#).

While the JSE may be acting in accordance with their rules on this matter, we believe it is highly unlikely that any investor would object to the return of capital on an instrument that is in default. This inflexibility on the part of the JSE has resulted in listed Land Bank noteholders having to wait an additional two months for their 10% return of capital. Furthermore, this imposes the risk that certain investors who agree to the resolution to delist the note are at the mercy of other noteholders not agreeing. *If the extraordinary resolution to delist the notes is not passed for each series of listed notes, that entire series of notes will not be repaid their 10% capital.* We believe this is an untenable, unnecessary – and avoidable - risk to impose on capital market investors. This is just another instance where the listed bond market is not fit for purpose, belying the common misconception that listed debt investments are somehow "better protected" or less risky than unlisted debt investments.

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