LAND AND AGRICULTURAL DEVELOPMENT BANK OF SOUTH AFRICA

BORROWING PROGRAMME

FY2017 TO FY2019

1 APRIL 2016 TO 31 MARCH 2019

I. INTRODUCTION

As a State Owned Entity (SOE) that has limited sources of funding (the Bank is not a deposit-taking institution) and capital (only one shareholder), the Land Bank is dependent on accessing the volatile capital and debt markets to fund its asset growth as well as on-going support from Government to strengthen its capital base. Government's support of the Land Bank through the issue of guarantees (both sustainability – and funding guarantees) has boosted investor and rating agency confidence. Notwithstanding this much appreciated level of support, the Land Bank is determined to develop and deploy liability strategies that will enhance the sustainability and self-sufficiency of the institution.

Although the Bank has a well-diversified funding base, focussed efforts are required to secure "anchor funders" to provide stability to the funding portfolio. The Bank will continue seeking new funding partners to further minimise counterparty concentration risk within its funding base.

Given the inherent weaknesses of the Bank's existing funding strategy, significant efforts are underway to lengthen its funding profile, thereby reducing refinancing risk to acceptable levels. The Bank's long-term aim is a funding profile in which maturities less than one year constitutes no more than 50% of the liability portfolio. The lengthening of the maturity profile is expected to increase the cost of funding in the medium-term, but this will be offset by new and improved pricing initiatives on the asset lending side, as well as a reduction in the funding cost stemming from the expected increase in investor confidence over time. Furthermore, efforts are underway to develop appropriate hedging strategies to address the Bank's interest rate- and basis risk exposure stemming from the Balance Sheet mismatch between prime-linked assets and JIBAR-linked liabilities.

One of the Bank's key objectives of its revised corporate strategy is to play a more meaningful role in the development and growth of the agricultural sector. In support of funding its aspirations in line with the Bank's development mandate, the Bank will continue to explore opportunities for longer-term funding from multilateral institutions in a bid to have appropriately matched funding for developmental projects that require long-dated capital. A development funding pipeline is available through various initiatives, including a R1.0billion loan from the African Development Bank (half of which has been utilised), R5.0billion from the Public Investment Corporation, a potential R1.3billion loan from the World Bank, as well as engagements with other multilateral institutions, such as the German Development Bank KfW. The Bank is currently negotiating a EUR50 million facility with this DFI. The Bank would however furthermore require additional capital support from its shareholder to strengthen its Balance Sheet and have a sufficient buffer to absorb losses.

The Bank intends to meet its funding needs through the issuance of *authorized financial instruments* as set out in the Land Bank Treasury Borrowing and Funding Policy. The Bank also envisages requesting approval from our shareholder between FY2017 and FY2019 for potential capital injections or capital (sustainability) guarantees to further support its development and growth aspirations.

During FY2017 the Land Bank Treasury Division would continue the process of establishing and implementing a strategy for prudently managing the bank's liabilities in order to meet the Bank's financing needs, its costs and risk objectives, and any other management goals.

The Borrowing Programme is required in terms of the Public Finance Management Act and the Treasury Regulations (29.1.3). The Bank must submit a three-year borrowing programme to the National Treasury, as well as quarterly reports reflecting annual borrowings and updates on the borrowing programme. As such, the Bank determines its Borrowing Programme annually and operationalizes its funding requirements after it has established its loan book growth forecast and liabilities redemption profile.

In terms of Regulation 29.1.6, the borrowing programme should include:

- Terms and conditions on which money is borrowed;
- Proposed domestic borrowing;
- Short, medium and long-term borrowing;
- Borrowing in relation to a pre-approved corporate plan;
- Maturity profile of debt;
- Confirmation of compliance with existing and proposed loan covenants;
- Debts guaranteed by Government;
- Motivations for Government guarantees; and
- Executive Authority's approval of borrowing programme.

The purpose of this document is to recommend a Borrowing Programme to fund the Bank's loan book and maturing debt for the forecast period 2017 to 2019 in accordance with the requirements of the Public Finance Management Act and the Treasury Regulations.

II. CORPORATE, CAPITAL MANAGEMENT AND FUNDING STRATEGY FOR FY2017 – FY2019

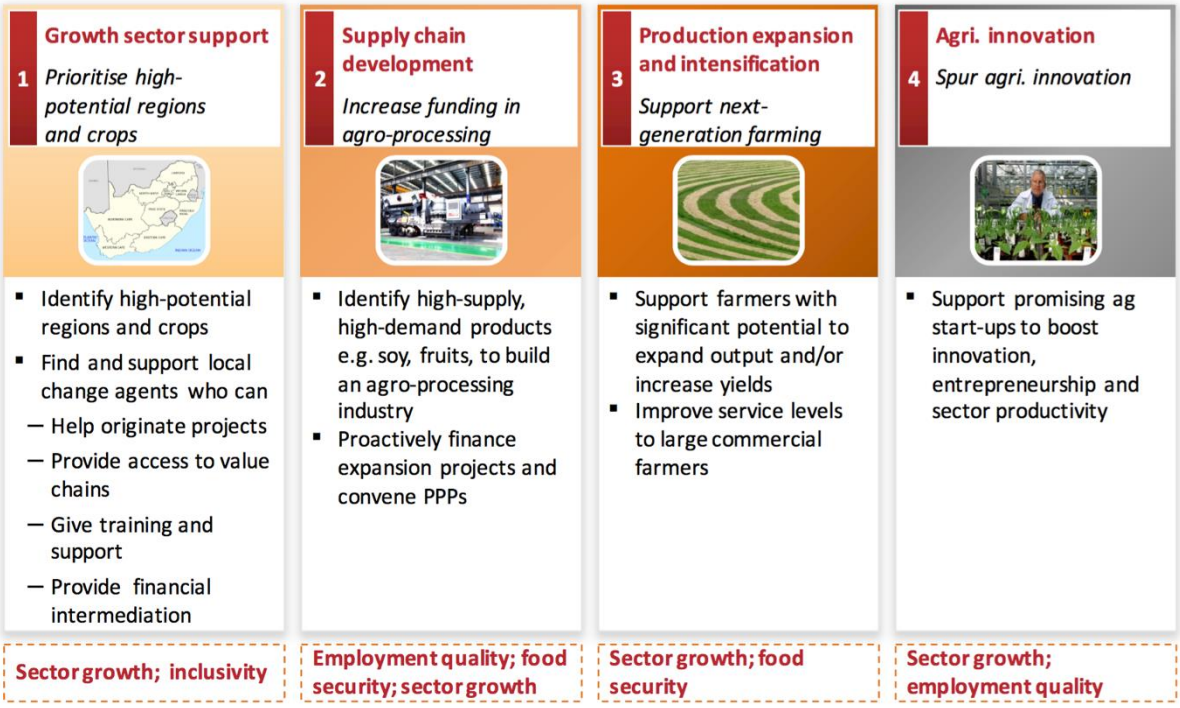
The Land Bank has potential to expand its role as a catalyst of agricultural development in South Africa. During an organisational review process starting February 2015, Land Bank identified four development objectives of the National Development plan as core to its strategy:

- *Sector growth*: Increase the growth of the agricultural sector in order to contribute to the overall growth of the South African economy;
- *Employment quality*: Increase the quality of jobs (i.e. income levels) across the agricultural value chain in order to improve livelihoods and help youth enter the sector;
- *Transformation (inclusivity):* Support the participation of historically disadvantaged individuals in commercial agriculture; and
- *Food security:* Raise the agricultural productivity of key staple crops in order to increase the availability and affordability of and access to food on a sustainable basis.

A. Strategic Pillars

In pursuit of these development objectives, the Bank has defined a strategy with four Strategic Pillars where it can play the role of catalyst and convenor (Figure 1). Under each pillar, the Bank will deliver targeted offerings to a number of priority customer segments. It will also proactively promote funding for sustainable agriculture and initiatives to build climate resilience. The objectives outlined below are properly aligned with both the National Development Plan and the APAP.

Figure 1: Strategic Pillars



Pillar 1: Support sector growth and inclusivity by accelerating the commercialisation of emerging farmers in high-potential regions and commodities: The Bank has a key role in accelerating the commercialisation of emerging farmers in high-potential regions and commodities, thus helping to drive transformation and inclusivity in the sector. In terms of this pillar, the Bank will directly help emerging commercial farmers address financing gaps in new farm development, land acquisition, and farm expansion. To this end, it will find and support local change agents who can help originate projects; provide access to value chains; offer training and support to emerging farmers; and provide them with financial intermediation. The Bank will also seek to act as a catalyst to ensure the appropriate use and allocation of capital allocated by the National Treasury to the agricultural sector.

Emerging commercial farmers include small-scale farmers with commercial ambitions (typically with backgrounds in agricultural or vocational employment); new, entrepreneurial entrants seeking to buy or lease commercial-scale land; and recently established farmers seeking to build their skill and impact.

In its support to emerging commercial farmers, the Bank will initially focus its efforts on six high-potential commodities – poultry, sheep, pigs, eggs, soybeans and avocados – in Limpopo, Mpumalanga, Kwazulu-Natal and the Eastern Cape. It will continue to review and accept applications from other commodities and regions.

Pillar 2: Increase funding for agro-processing: The focus of this pillar is on funding and developing the agricultural supply chain, with a particular emphasis on agro-processing. Target customers will include existing agro-processing enterprises that require capital expansion and commercial farmers moving up the value chain. The Bank will also seek to accelerate the participation of black entrepreneurs and investors in the agricultural economy.

The approach will be to increase the Bank's investment in agro-processing in 11 commodities across the country, selected because of their market attractiveness, national competitive advantage and development importance. The Bank will proactively finance expansion projects and convene public-private partnerships in these commodities. It will actively syndicate with other relevant institutions, including the Industrial Development Corporation and the Development Bank of Southern Africa.

Pillar 3: Product expansion and crop intensification: The focus of this pillar will be to support next-generation farming by expanding and intensifying existing agricultural production. The target customers for this pillar will be growth-oriented, large-scale, established commercial farmers, who have the potential for expansion or yield improvement. The Bank will focus on significantly improving its service levels to large commercial farmers.

The emphasis in terms of this pillar will be on capital projects with a high potential to expand outputs or increase yields, as well as on tailored production finance and specialised asset finance. For example, the Bank can finance farmers deploying new, higher-risk technology or start-up expansion projects for which commercial banks do not have an appetite.

Pillar 4: Boost agricultural innovation: The focus of this pillar will be on agricultural innovation, entrepreneurship and productivity. Its target customers will comprise agricultural innovation start-ups – enterprises that are developing and commercialising revolutionary agricultural technology or products. The Land Bank's approach will be to invest in high-potential agricultural innovation companies either directly or via venture capital funds, thus supporting the commercialisation of promising agricultural start-ups in the relatively underdeveloped venture capital market in South Africa. It could fill this financing gap by incubating and commercialising "ag-innovation" through a dedicated venture capital fund.

B. Capital Management

The Capital Management strategy of the Bank has been developed to support the Bank in its execution of its Corporate Strategy.

The Basel Capital Accord was intended to amend international standards that controlled how much capital banks need to hold to guard against the financial and operational risks banks face. These rules sought to

ensure that the greater the risk to which a bank is exposed, the greater the amount of capital the bank needs to hold to safeguard its solvency and economic stability.

Capital, or the amount of capital that the Land Bank holds, is retained as a buffer to absorb losses. The more capital the Bank retains, the lower the likelihood of any solvency concerns and the better the ability the Bank has absorb losses resulting from economic shock events.

The Bank is of the opinion that the current 20% Capital Adequacy Requirement / Gearing is inappropriate as it is a risk insensitive measure. The Bank therefore aims to change its capital management practices in line with Basel II principles to maintain sound capital to safeguard the Bank against financial and operational risk.

Calculating and reporting Basel II regulatory capital adequacy ratios would allow the Land Bank to:

- Provide funders and ratings agencies with relevant risk based reporting that is consistent and comparable to Land Bank's peers in the South African financial sector – resulting in enhanced transparency, and potentially improved funding rates; and
- Provide the opportunity for the Land Bank to negotiate shareholder and loan covenants that are more appropriate to a banking entity than currently exist.

Furthermore, managing capital benchmarks that are more in-line with SARB regulatory requirements should allow Land Bank to improve its market competitiveness by aligning its "regulatory" requirements, i.e. shareholder covenants, to those of its competitors, allowing it to compete on a level playing field.

The Bank therefore proposes a revised Capital Adequacy measurement in the form of a minimum total capital adequacy ratio (CAR), based on the standardised approach of Basel II, in section VI of the Borrowing Plan.

C. Funding and Liquidity

The Funding and Liquidity strategy of the Bank has been developed to support the execution of the Corporate Strategy with the Bank determined to further lengthen the funding profile of the organisation and thereby reducing the refinancing risk that the Bank is currently exposed to.

In response to the liquidity and funding mismatch during FY2015, the Land Bank and the National Treasury agreed to moderate the Bank's asset growth during FY2016 and revisit its funding plan.

Government provided a R4.0billion guarantee to the Bank, in recognition of recent events, including the organisational review, and the investments required to set a firm basis for a significant change in the organisation. This guarantee has been successfully utilised to raise a R2.7billion longer-term loan during the year. This guarantee will continue to be utilised to raise a further R1.3billion development facility from the World Bank.

During FY2017 the goals of the Treasury Division will be as follows:

- A well informed, diversified and increased investor base;
- Source affordable funding and diversify funding instruments;
- Source affordable funding to enable the development objective of the bank;
- Structure funding liabilities in line with the maturity distribution targets;
- Provide optimal liquidity for the Bank;
- Optimal investment and liability portfolio management in terms of cost and risk;
- Review Treasury Policies in line with National Treasury Guideline on Treasury Best Practise;
- Develop currency and interest rate risk hedging policies; and
- Develop a capital management strategy.

The strategy for FY2017 will therefore focus on:

- A stable, lower cost of funds over the next three financial years;
- Progressively term out along the yield curve to 5-10 years if there is market interest and/or demand;
- Using both financing and risk management transactions to achieve the desired portfolio structure and cost of funds over time;
- Structured cash flow forecasting for periods from 'end of today' forward to 30 days and the next 12 months to manage and anticipate accurately future funding requirements;
- Re-negotiate loan covenants based on standardised Basel III principles.

III. EXISTING FUNDING POLICY AND BORROWING PROGRAMME

A. Funding Policy

The Borrowing and Funding Policy as contained in the Treasury Policy Manual details the guiding principles that enable the Land Bank's Treasury function to operationalize the 3 year Borrowing Programme submitted for approval to the Minister of Finance.

The policy, inter alia, states the following;

- Treasury operations will be complying with the Bank's Corporate and Borrowing Programme and directives as approved by the Land Bank Board and the Minister of Finance;
- The policy will encapsulate instructions made by the Minister of Finance; and
- The policy will be reviewed annually to ensure that Treasury operations are in harmony with a dynamic South African financial market environment.

B. Borrowing Programme

This Borrowing Programme is oriented to meet the Bank's operational financing needs, striking a balance between diversified sources of debt that reduces funding cost while considering a long term horizon with a low risk level. To this end, it is important to maintain access to different funding sources and to continue to strengthen the Bank's visibility in the domestic debt markets.

The Bank continued to expand funding sources beyond the usual money and capital markets. The Bank targeted the following alternative funding sources:

- Renew and increase commercial bank funding (dedicated credit lines);
- Loans and lines of credit from Development Finance Institutions;
- Debt and Capital market transactions;
- Shareholder funding to the extent to which it is available; and
- Repayment of facilities to clients (where the pricing of those facilities was aggressive).

The Bank will however, taking into consideration the above, continue to maintain a debt structure in line with its role as a primary agricultural development finance institution (DFI).

C. Funding Profiles

Land Bank Treasury continues to auction money market paper, inter alia, to remain visible and to use the auction process as a tool to assess demand for our paper.

As at 31 December 2015, short term debt (maturities up to one year and measured as original term to maturity) amounted to R19.0bn or 59.2% of total debt. Treasury's strategy is to continue lengthening the maturity profile by using the DMTN Programme and private placements to diversify sources of funding.

Figure 2 – Funding Maturity Profile FY2016

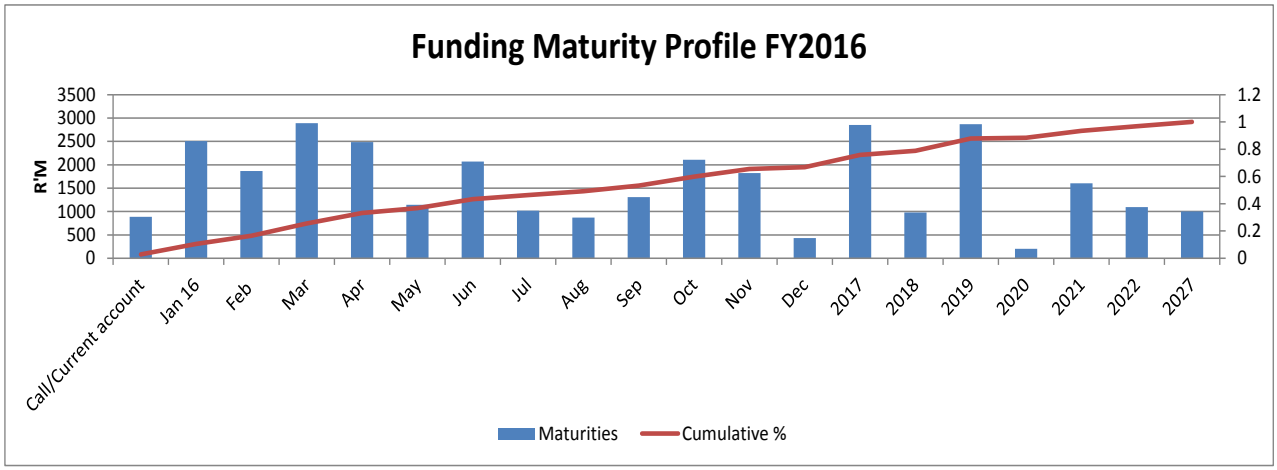


Figure 3 below shows that total average roll-over rates (Including PIC & CPD) stabilised around 83% for the period April 2015 to January 2016 with PIC and CPD agreeing to roll maturing debt one hundred percent. Total average roll-over rate for the same period prior year was 55%. The roll-over rate clearly shows a significant improvement during FY2016.

Figure 3: Maturing Debt – Roll-Over Rate

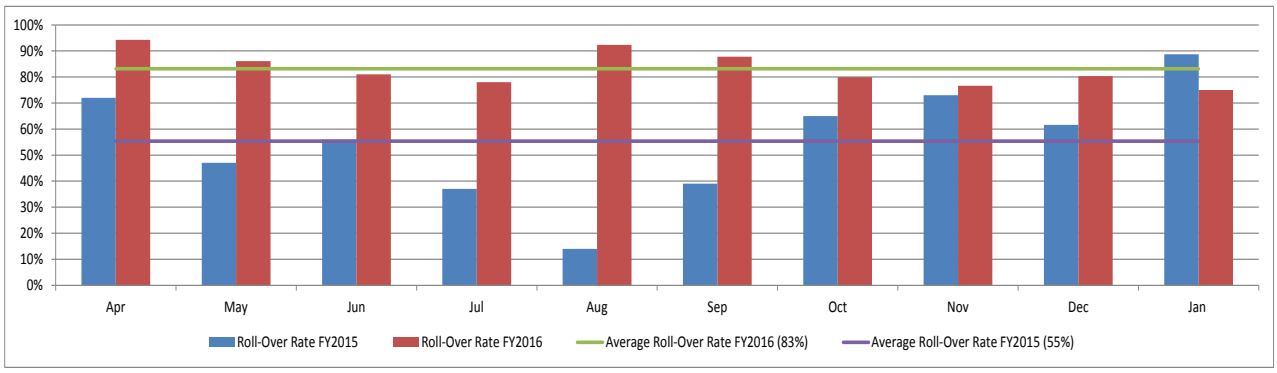


Figure 4 below features average roll-over rates (Excluding PIC & CPD) at 61% for the period April 2015 to January 2016. Average roll-over rate during the same prior year period was 42%. Although the roll-over rate shows an improvement during FY2016 compared to FY2015, it still requires the Bank to refinance on average 39% of other maturing debt not rolled-over.

Figure 4: Maturing Debt excluding PIC & CPD: Roll-Over Rate

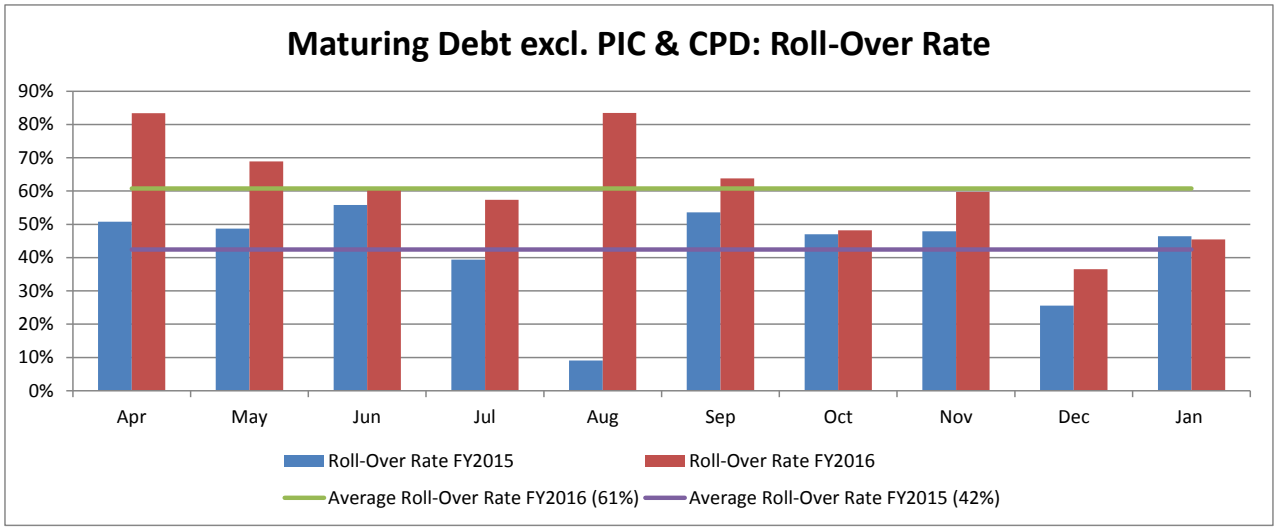


Figure 5 below depicts the funding mix on 31 December 2015. The figure shows that the composition of the Land Bank's funding portfolio is concentrated in the short term promissory notes (maturities up to one year) category. Concentration risk in promissory notes, as a percentage of total funding was 41.5% as at 31 December 2015. Concentration in short term promissory notes will be addressed further by way of terming out maturing liabilities, as well as issuing other instruments and loans through the R20bn DMTN Programme, private placements and loan/overdraft facilities from financial institutions. The Bank will

continue to address refinancing risk taking into consideration high cost of longer term funding and the risk associated with concentration of funding in the short term.

Figure 5: Funding Mix at 31 December 2015

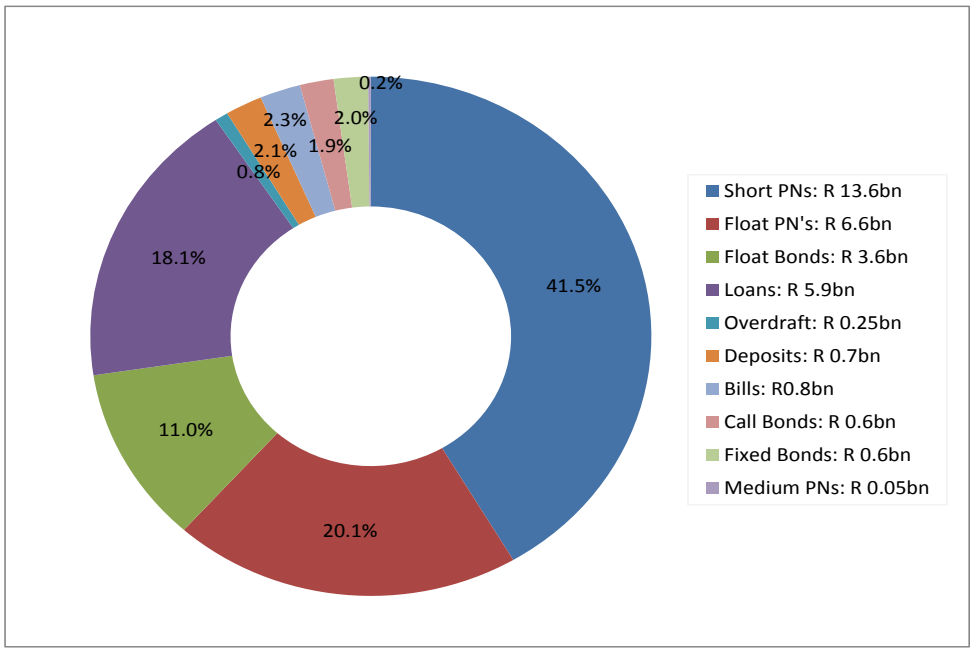
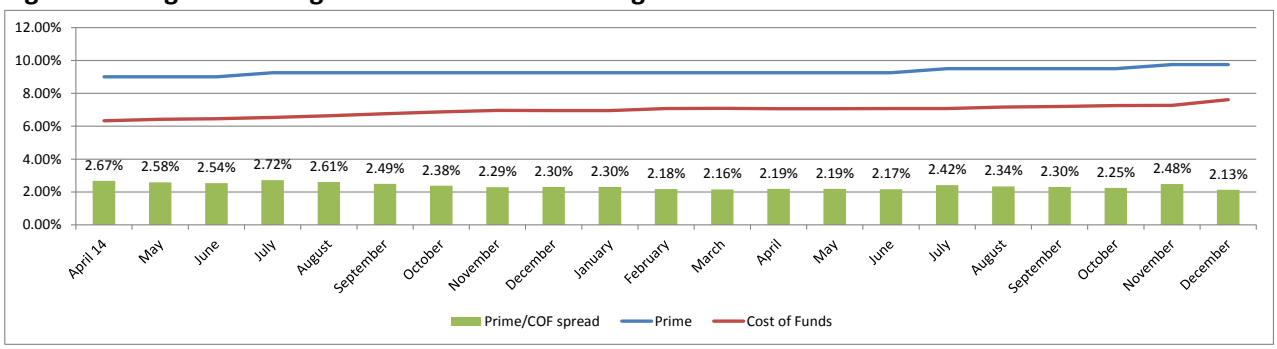


Figure 6 below depicts the Bank's weighted average historical cost of funding during the period April 2014 to December 2015. The spread to Prime Rate ranges between a high of 2.72% in July 2014 to a low of 2.13% in December 2015.

The Bank will therefore continue to refine its asset pricing strategy and develop an interest rate hedging strategy during FY2017 to manage the basis and re-pricing risks. Cost of funding increased 35 basis points as a result of the R2.7bn long term funding raised during December 2015 as well as the volatile interest rate environment. The cost of funding is expected to continue to increase due to the interest rate environment.

Figure 6: Weighted average historical cost of funding



D. Current Financial Government Guarantees

Table 1 below shows total Government Guarantees of R6.6bn as at 31 December 2015. During FY2016 a total of R3.2bn guarantees have been drawn down leaving an amount of R1.3bn available to issue government guaranteed debt.

Table 1 – Government Guarantees

Guarantee in respect of:	Original capital amount	Utilisation of guarantees			Remaining Portion of guarantee
		Opening Balance 1 April 2015	Drawdowns during the year	Closing Balance 31 December 2015	
Consolidation of debt	0.1	0.1	-	0.1	-
Financial sustainability	1.5	1.5	-	1.5	-
Financial sustainability	4.0	-	2.7	2.7	1.3
African Development Bank	1.0	0.5	0.5	1.0	-
Total	**6.6**	**2.1**	**3.2**	**5.3**	**1.3**

The R1.3bn remaining portion of the R4bn Financial Sustainability Guarantee has been earmarked for a World Bank facility.

IV. OBJECTIVES AND SCOPE FOR THE BORROWING PROGRAMME FY2017 TO FY2019

A. Revised Capital, Funding and Liquidity benchmarks

The current capital adequacy ratio was an imposed ratio that only took into consideration the amount of equity, divided by funding liabilities which is a measurement for gearing and is completely risk insensitive. Therefore it does not matter what the funding profile of the Bank is or whether the Bank grows its assets in a risk responsible fashion. For this reason, the Bank will adopt the Basel II Standardised Approach to determine the amount of capital needed to ensure solvency and liquidity. The Bank will target a minimum total capital adequacy ratio of 15%.

Basel requires that banks meet three minimum capital adequacy ratios, in order to ensure that banks have an acceptable mix between high quality, expensive capital and lower quality, less expensive capital, these are:

- Common Equity Tier 1 (CET1) minimum = CET1 / total Risk Weighted Assets (RWA);
- Tier 1 minimum = (CET1 + Additional Tier 1 (AT1)) / total RWA; and
- Total minimum = (CET1 + AT1 + Tier 2) / total RWA.

Basel II capital requirements are more onerous when compared to Basel II, and so a period of phasing-in is underway to allow banks to reach increased minimums by 2019. The SARB includes additional capital add-

ons and buffers specifically related to the RSA banking sector, over and above Basel minimum requirements. The 2019 SARB Basel III regulatory capital minimums are:

- CET1 ≥ 7.50%
- Tier 1 ≥ 9.25%
- Total ≥ 11.50%

The calculation for capital adequacy consists of the demand and supply of capital. The available capital or capital supply consists of three categories:

- Common Equity Tier 1 (CET1):
  - Shareholders' equity
  - Highest quality capital
  - Greatest capacity to absorb unexpected losses;
- Additional Tier 1 (AT1):
  - Preference shares
  - Only absorbs losses after ordinary equity is depleted; and
- Tier 2:
  - Subordinated-debt
  - Typically would only absorb losses in a "gone-concern" scenario.

Capital demand consists of Risk-weighted assets (RWA) which are based on five risk categories identified as mandatory. These are termed "Pillar 1 risks" and include:

1. Credit risk
2. Operational risk
3. Market risk
4. Equity risk
5. Other assets risk

Risk-weightings are risk sensitive, in other words, riskier assets receive higher weightings and Basel allows for basic and advanced approaches to determine RWA dependent on the sophistication of a bank.

Land Bank (Bank) capital adequacy was estimated based on the following Basel approaches:

- Credit risk: The Standardised Approach;
- Operational risk: The Standardised Approach;
- Equity risk in the banking book: The Simple Risk-weight Approach;
- Market risk: Assumed nil; and
- Credit and operational risk have been identified as the major risk types affecting the Land Bank.

It is the intention of the Land Bank to move towards more sophisticated approaches, such as the Advanced Internal Ratings Based (AIRB) approach for credit risk measurement.

The Bank will further seek to strengthen its capital management by adopting the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) as proposed by Basel III.

Currently the liquidity buffer of the bank is mainly determined by a liquidity ratio of 7.5% of liabilities maturing in the next six months. The major concerns with this ratio:

- *Promotes increased costs of funding:* Liquidity risk managers choose high cost short term funding in order to maintain the 7.5% ratio regardless of liquidity needs. Overdrafts are sought from the same banks who impose the covenant requirements, increasing funding costs;
- *Does not account for liquidity mismatches:* The current requirement does not take into account liquidity needs. The 7.5% held might be insufficient to meet short term cash flow demand or may be held without regard for low liquidity demand. This is both needless and costly;
- *Retrospective liquidity assessment:* The metric assesses past asset and liquidity balances rather than forward looking cash flow requirements. Without consideration for client behaviour or stress conditions it is not possible to ascertain the appropriate level of liquid assets required; and
- *Low return cash management encouraged:* The covenants currently require that cash balances are maintained, thus reducing the profitability of Land Bank as higher return near cash instruments such as corporate bonds are not acquired as part of the liquid asset mix.

The LCR aims to ensure that banks maintain adequate levels of unencumbered high quality assets (numerator) against net cash outflows (denominator) over a 30 day significant stress period. Adopting a variation of this ratio will have the following benefits for the Bank:

- Improved comparability with South African commercial banks;
- Basel approved measures more accurately reflect the capital requirements and liquidity demands than metrics currently in use;
- Metrics encourage examination of future and current risks, with a focus on promoting good risk management practices from a credit and liquidity management perspective;
- Basel measures promote long term, sustainable business rather than short term gains; and
- Basel methodologies are well embedded across the globe and are accepted as international best practice in risk management

The LCR is a measure of the bank's ability to meet cash outflows under stressed conditions using its available sources of cash or near cash instruments. LCR is calculated by dividing High Quality Liquid Assets (HQLA) by Net Cash Flows. High Quality Liquid Assets (HQLA) is split into three types, based on quality:

1. HQLA Level 1:
    + Cash
    + Government securities
    + Central bank liquidity facility (not available to Land Bank)

2. HQLA Level 2a:
    + Specific corporate bonds

3. HQLA Level 2b:
    + Specific high quality assets

While Net cash outflow over a 30 day period includes:

- Cash outflow:
  - + Maturing debt (weightings are applied to take into account funder behaviour, e.g. rollovers, re-investment)
  - + Off-balance sheet commitments (weightings are applied to take into account client behaviour, e.g. drawdowns)
  - + Cash inflow: are mainly client repayments.

The Bank will seek to target a minimum of 60% of the LCR ratio as is required by Basel III as shown in the table below:

Table 2: Liquidity Coverage Ratio

Liquidity Coverage Ratio (LCR)		**Basel Req.**	**FY2016**	**FY2017**	**FY2018**	**FY2019**	**FY2020**
Short-term liabilities	Assume no roll-over and maturing in the applicable year		18,917	19,608	19,381	21,046	23,499
Funding from PIC & CPD	Assume no further growth in funding obtained		9,010	9,010	9,010	9,010	9,010
Maturities of liabilities	Excluding funding from PIC & CPD		9,907	10,598	10,371	12,036	14,489
Unutilised facilities provision	Assuming 85% utilization	5%	112	118	125	132	140
Deposits rundown	545,545	3%	16	16	16	16	16
Total Outflows			**10,035**	**10,733**	**10,512**	**12,184**	**14,645**
Inflows	Basel (inflows max. 75% of outflows)	**75%**	**7,526**	**8,050**	**7,884**	**9,138**	**10,984**
Net Flows			**2,509**	**2,683**	**2,628**	**3,046**	**3,661**
Sinking Fund[1]	A 15% haircut is applied to the current market value of each Level ZA asset held in the stock of HQLA		-	420	970	1,553	2,169
LCR incl. Sinking Fund			55%	74%	97%	102%	105%

[1] A sinking fund is an annuity type investment with recurring monthly investments aimed at building sufficient contingent sources of cash and liquidity. The underlying investment instruments are very flexible and the Bank will ensure an appropriate investment strategy, investing only in "High quality liquid assets" as to ensure the "Sinking Fund" meets the qualifying criteria with regard to LCR.

The NSFR aims to establish a minimum acceptable amount of stable funding based on the liquidity characteristics of an institution's assets and activities over a one year horizon. It aims therefore to limit over-reliance on short term wholesale funding during times of buoyant market liquidity and encourage better assessment of liquidity risk across all on and off balance sheet items. The Bank will over the time horizon of the funding strategy aim to achieve a NSRF of higher than 100%. In order to allow for the implementation of the NSFR, the Bank targets an NSFR of a minimum of 80%.

The NSFR is calculated by dividing Available Stable Funding by Required Stable Funding and the SARB requires this identity to be greater or equal to 100%. For the purpose of calculating the NSFR, the following were taken into consideration:

Available Stable Funding	Required stable funding
▪ Total regulatory capital (excluding Tier 2 instruments with residual maturity of less than one year) ▪ Other capital instruments and liabilities with effective residual maturity of one year or more	▪ Unencumbered level 1 assets, excluding coins, banknotes and central bank reserves
▪ Stable non-maturity (demand) deposits and term deposits with residual maturity of less than one year provided by retail and small business customers	▪ All other assets not included in the above categories with residual maturity of less than one year, including loans to non-financial corporate clients, loans to retail and small business customers, and loans to sovereigns and PSEs ▪ Deposits held at other financial institutions for operational purposes
▪ Less stable non-maturity deposits and term deposits with residual maturity of less than one year provided by retail and small business customers	▪ Unencumbered residual mortgages with a residual maturity of one year or more and with a risk weight of less than or equal to 35% under the Standardised Approach
▪ Funding with residual maturity of less than one year provided by non-financial corporate customers	▪ Other unencumbered performing loans with risk weights greater than 35% under the Standardised Approach and residual maturities of one year or more, excluding loans to financial institutions
▪ All other liabilities and equity not included in the above categories, including liabilities without a stated maturity (with a specific treatment for deferred tax liabilities and minority interests)	▪ All other assets not included in the above categories, including non-performing loans

Table 3: Net Stable Funding Ratio (NSFR) – R'm and %

Net Stable Funding Ratio (NSFR)	FY2016	FY2017	FY2018	FY2019	FY2020
Available stable funding					
Capital (Tier 1 and 2)	5 204	6 316	6 848	7 622	8 560
Long term debt (Maturity > 1 year)	12 713	16 705	20 055	21 165	23 765
Funds from PIC & CPD	9 010	9 010	9 010	9 010	9 010
Deposits	1	1	1	1	1
Less stable deposits (Call Bonds from other Public Entities)	427	457	488	520	520
Total	**27 355**	**32 489**	**36 402**	**38 319**	**41 857**
Stable funding required	**36 036**	**40 734**	**43 896**	**47 193**	**51 384**
Net Stable Funding Ratio (NSFR)	**76%**	**80%**	**83%**	**81%**	**81%**

B. Funding and Liquidity

The Land Bank's funding requirements are satisfied with reference to authorised money and capital market instruments listed in the Treasury's Borrowing and Funding Policy Manual. Funding is divided into three maturity buckets, namely short-term, medium and long-term. Short-term funds have maturities not longer than one year; medium-term funding has maturities longer than one year up to five years and long-term funding has maturities longer than five years.

During FY2017 efforts to source new funding will be intensified in the local financial market as well as the finalisation of a government guaranteed loan facility of R1.3billion with the World Bank subject to the finalisation of the organisational restructuring and National Treasury's approval to utilise the remaining R1.3billion portion of the R4billion government guarantee. Comprehensive feedback on the progress made by the Land Bank to comply with the conditions set by National Treasury to utilise the remaining portion of the guarantee is included in the Corporate Plan.

During the first week of February 2016 the executive management of the Bank embarked on a non-deal specific investor road show to update investors on recent developments at the Land Bank, introduce management to investors, the funding requirements of the Bank and to get feedback from investors with regards to the investor sentiment and appetite for Land Bank financial instruments. This roadshow should serve as a launching pad for our capital market funding activities during FY 2017.

The Bank has also increased its Domestic Medium Term Note Programme limit by R10billion from R10billion to R20billion and subject to investor appetite, the programme can be used to issue listed bonds during FY2017.

1) Baseline Assumptions

The gross Agro, Commercial and Corporate loan books is projected to grow at a rate of 9.1%, 7.4% and 6.9% for the next three years from current R37.2 billion to R46.6 billion in FY2019 an average rate of 7.8%. This amounts to an average increase in these loan books of R3.1 billion per annum.

Table 4: Loan Book growth excl. "Sector Growth" – R'bn

Financial Year	Agro Processing	Commercial	Corporate	Total	Growth	Growth %
FY2016	2.3	5.1	29.8	37.2		
FY2017	2.8	5.1	32.7	40.6	3.4	9.1%
FY2018	3.2	5.5	34.9	43.6	3.0	7.4%
FY2019	3.5	5.9	37.2	46.6	3.0	6.9%
					9.4	**7.8%**

The development loan book is projected to grow at a rate of 74.1%, 18.7% and 15.1% for the next three years from the current R1.4 billion to R3.5 billion in FY2019, at an average growth rate of 35.9% per annum. This amounts to an average increase in the development loan book of R0.7billion per annum.

Table 5: Loan Book Growth – "Sector Growth"- R'bn

Financial Year	REM	Commercial Development	Corporate Development	Total	Growth	Growth %
FY2016	0.6	0.8	-	1.4		
FY2017	0.6	0.9	1.0	2.5	1.1	74.1%
FY2018	0.9	1.0	1.1	3.0	0.5	18.7%
FY2019	1.2	1.1	1.2	3.5	0.5	15.1%
					2.1	**35.9%**

The Bank's funding liabilities are expected to grow in parallel with loan book from current R31.8 billion to R43.0 billion over the next three years at an average rate of 10.6%. This amounts to an average increase of R3.7 billion per annum.

Table 6: Funding Liabilities – R'bn

Financial Year	Sector Growth	Agro Processing	Commercial	Corporate	Total	Growth	Growth %
FY2016	1.3	1.9	4.2	24.4	31.8		
FY2017	2.2	2.3	4.3	27.4	36.3	4.5	14.2%
FY2018	2.7	2.7	4.7	29.6	39.7	3.4	9.3%
FY2019	3.1	3.0	5.0	31.9	43.0	3.3	8.4%
						11.2	**10.6%**

During FY2017 new funding of approximately R4.5 billion needs to be sourced to fund expected loan book growth. Debt totalling R19.6 billion is projected to mature during FY2017 and it is assumed that 10% of maturing debt will not be rolled over by investors. An additional amount of R2.0 billion will therefore be needed to fund the maturing debt not rolled over. Total funding requirement for FY2017 is R6.5 billion calculated as follows:

Table 7: Total Funding Required

Financial Year	Maturing Debt	Maturing Debt not rolled (10%)	Funding of Maturing Debt	New Funding for "Sector Growth	"New Funding for "Commercial/ Corporate	Total new funding required
FY2017	19.6	2.0	2.0	0.9	3.6	4.5
FY2018	23.6	2.4	2.4	0.5	2.9	5.8
FY2019	26.3	2.6	2.6	0.4	2.9	5.9
Total	**69.5**	**7.0**	**7.0**	**1.8**	**9.4**	**18.2**

2) Funding Structure

Due to the dynamic nature of the financial markets, the supply and demand characteristics of funding instruments change on a continuous basis. Demand for funding instruments can change due to the market development, and these changes are effected and operationalized in the monthly funding strategy document submitted to the Asset and Liability Committee of the Bank (ALCO) for approval. The authority to determine the tenor, yield and amount to be issued is delegated according to the existing delegation of powers.

In line with the strategy to lengthen the debt maturity profile the Bank would endeavour to raise the funding requirement in the loan, money and capital market. The envisaged structure of the funding requirement for FY2017 to FY2019 will be as follows:

Table 8: New funding structure FY2017/ FY2018/ FY2019 – R'bn

Structure of Liabilities	Funding Instrument	FY2017	FY2018	FY2019
< 1 year	Promissory notes	3.6	2.9	3.0
3 years	Floating rate notes	1.6	1.7	1.8
5 years	Floating rate notes	1.0	0.6	0.6
7 years	Floating/ Fixed rate notes	0.3	0.3	0.3
10 years	Fixed rate notes	-	0.3	0.3
Increase in funding		**6.5**	**5.8**	**5.9**

Given the volatility and nature of the Capital Market, the tables above represent targets and the actual structure could be different. The Bank has to be flexible in its execution and may opportunistically make use of small windows of opportunity to take advantage of available appetite.

3) Cost of Funding

Table 9 below shows Land Bank projected cost of funding for FY2016 to FY2019. It shows that projected cost of funding is expected to increase from an average of 8.19% during FY2016 to 8.41% and 8.71% respectively during FY2017, FY2018 and FY2019. The percentage increase in cost of funding is expected to exceed the percentage increase in repo rate due to the higher cost of extending the Land Bank maturity profile further to achieve target funding mix target of less than 50% reliance on short-term funding.

Table 9: Average cost of funding - %

	FY2016	FY2017	FY2018	FY2019
Average Repo Rate %	7.06	7.56	7.99	7.95
Average Cost of Funding (COF) %	8.19	8.41	8.71	8.71

4) Borrowing Programme

The Land Bank intends to borrow its funds in the domestic market. Foreign borrowings will only be considered where the Bank can issue the instruments at cheaper rates than in the local market and with prior approval from the National Treasury. But, this will be hedged (converted into rand) to eliminate foreign exchange risk.

The Funding requirements for the financial year 2017 are the aggregate of maturing current debt plus the expected loan book growth.

Borrowings are broken up into short, medium and long term buckets as required by the National Treasury and borrowings dovetail with the proposed corporate plan of the Bank.

The maturity profile and proposed domestic borrowings for FY2017 to FY2019, based on the expected loan book growth forecast, is shown in Table 10.

Table 10: Net Borrowing Programme – R'bn

				DOMESTIC PORTION		
Financial Year	**Funding: Maturing Debt not rolled**	**Funding: Loan book growth**	**Total Net Borrowing**	**Short Term (≤12 MTHS)**	**Medium Term (1-5 YRS)**	**Long Term (> 5 YRS)**
FY2017	2.0	4.5	6.5	3.6	22.6	0.3
FY2018	2.4	3.4	5.8	2.9	2.3	0.6
FY2019	2.6	3.3	5.9	3.0	2.3	0.6
TOTAL	**7.0**	**11.2**	**18.2**	**9.5**	**7.2**	**1.5**

Table 11 below features gross borrowings. Any funding longer than one year is expected to be sourced from diversified sources of funding, through the R20 billion DMTN programme, loan market and private placements. Shortfalls will be funded (bridged) with short term borrowings.

Table 11: Gross Borrowing Programme – R'bn

				DOMESTIC PORTION		
Financial Year	**Gross Borrowings**	**Maturing Debt to be Rolled**	**New Funding**	**Short Term (≤12 MTHS)**	**Medium Term (1-5 YRS)**	**Long Term (> 5 YRS)**
FY2017	36.3	29.8	6.5	3.6	2.6	0.3
FY2018	39.7	33.9	5.8	2.9	2.3	0.6
FY2019	43.0	37.1	5.9	3.0	2.3	0.6
TOTAL	**119.0**	**100.8**	**18.2**	**9.5**	**7.2**	**1.5**

5) Funding Pipeline

The table below shows the Bank's current funding pipeline.

Table 12: Funding Pipeline – R'bn

Funding Institution	Funding Purpose	Funding Term	Government Guarantee	Funding Amount	Current Status	Expected Disbursement
World Bank	Sector Growth	15yrs	Yes	R1.3 bn	Negotiation phase	June 2016
PIC	Sector Growth	8yrs	No	R5.0 bn	Finalising loan requirements	In tranches of next 2 financial years
AfDB	Sector Growth	11yrs	Yes	R0.5 m	Concluded	FY2017
DMTN Programme	Corporate/ Commercial	3-5yrs	No	Up to R5.0 bn	Market sounding to be performed by arrangers	Dependent on outcome of market sounding
Syndicated Loans	Corporate/ Commercial	> 5yrs	Yes	Up to R5.0 bn	Motivation for government guarantees included in FY2017 Borrowing Plan	FY2017 – December 2016
Money Markets	Corporate/ Commercial	≤ 1yr	No	Up to R2.0 bn	On-going	On-going
Foreign Banks	Corporate/ Commercial	> 5yrs	No	Up to R2.0 bn	On-going	On-going

During FY2017 the Bank would continue negotiations for funding with the following institutions:
The Bank will only approach local branches of foreign banks subject their South African status being the following:

- Is a locally registered branch;
- A local taxpayer;
- Its local funding is in ZAR;
- Is registered with and regulated by the SARB; and
- It is an authorised dealer in foreign exchange under exchange control regulations.

Given the spectacular success of the R2.7billion Government guaranteed syndicated loan, where the appetite expressed for the transaction by investors exceeded the available amount by more than 2.5 times, the Land Bank will formally apply for further support from our Shareholder in the form of a R4billion Government guarantee to raise long term debt (exceeding an original maturity of more than five years for a bullet repayment profile and a weighted average maturity profile of 4 years for an amortising repayment profile) over the next 3 years.

6) Maturity Profile

The projected maturity distribution of funding liabilities over the next three years is as follows:

Table 14: Maturity distribution of Funding Liabilities – in %

	Maturity distribution of liabilities %			
Structure of liabilities	**FY2016**	**FY2017**	**FY2018**	**FY2019**
< 1 year	60	55	50	50
3 years	20	25	30	30
5 years	15	15	10	10
7 years	5	5	5	5
10 years	-	-	5	5
	100	**100**	**100**	**100**

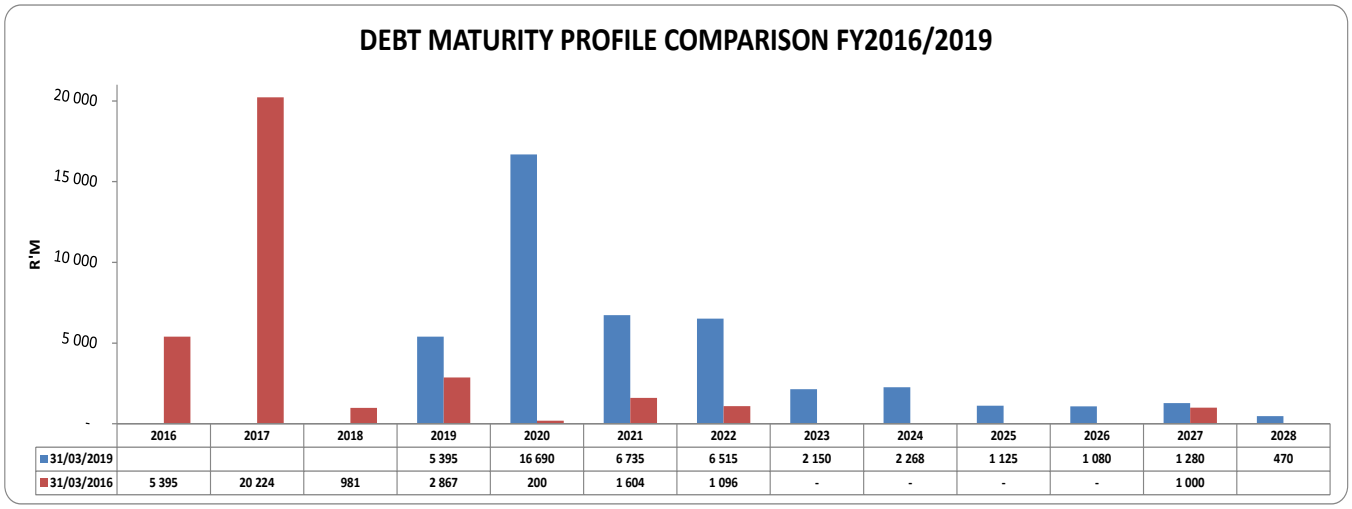
Table 15 below features the total debt maturity profile from FY2016 to FY2019. Total debt is expected to increase by R11.2 billion from R31.8 billion at 31 March 2016 to R43.0 billion at 31 March 2019. This maturity profile is based on the assumption that favourable market conditions would prevail to enable the Bank to increase funding by R11.2 billion over three years.

Table 15: Maturity Profile – in billions

Financial Year	TOTAL DEBT				
	31 Dec 15	FY2016	FY2017	FY2018	FY2019
FY2016	21.4	5.4	-	-	-
FY2017	2.9	18.6	5.5	-	-
FY2018	1.0	1.0	13.9	5.5	-
FY2019	2.9	2.9	5.5	13.6	5.5
FY2020	0.2	0.2	3.9	5.0	15.4
FY2021	1.6	1.6	3.2	7.4	6.7
FY2022	1.1	1.1	2.4	2.7	6.5
FY2023	-	-	0.3	1.4	2.1
FY2024	-	-	0.6	1.1	2.3
FY2025	-	-	-	1.0	1.1
FY2026	-	-	-	0.3	1.1
FY2027	0.9	1.0	1.0	1.3	1.3
FY2028	-	-	-	0.4	0.5
FY2029	-	-	-	-	0.5
TOTAL	**32.0**	**31.8**	**36.3**	**39.7**	**43.0**

Figure 7 depicts the change in the expected Debt Maturity Profile between FY2016 and FY2019. It demonstrates the efficiency of implementing the maturity distribution strategy as presented in table 15 above. It shows an expected decline in short-term debt of R3.5billion from R18.6billion in FY2016 to R15.1billion in FY2019.

Figure 7 – Debt maturity profile comparison FY2016/ FY2019



	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	2027	2028
31/03/2019				5 395	16 690	6 735	6 515	2 150	2 268	1 125	1 080	1 280	470
31/03/2016	5 395	20 224	981	2 867	200	1 604	1 096	-	-	-	-	1 000	

7) Funding Mix Comparison

Figure 8 and Figure 9 below depicts the expected change in the funding mix from FY2016 to FY2019. It shows an expected decline in short term promissory notes from 41.5% in FY2016 to 25.7% in FY2019 in line with the Bank's strategy to reduce refinancing risk and to lengthen the maturity profile.

Figure 8: Funding Mix FY2019

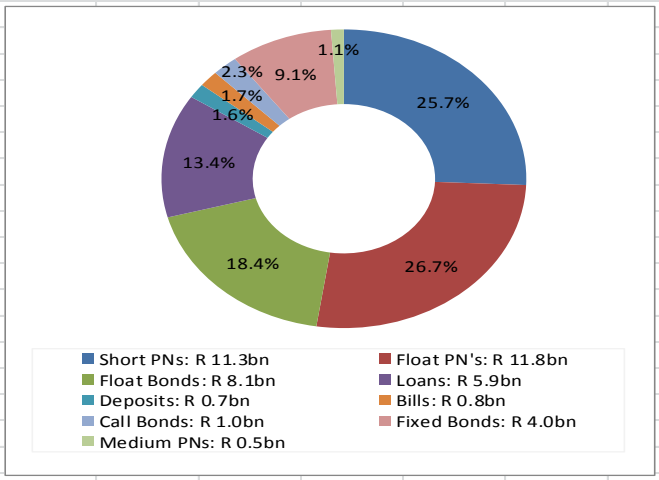
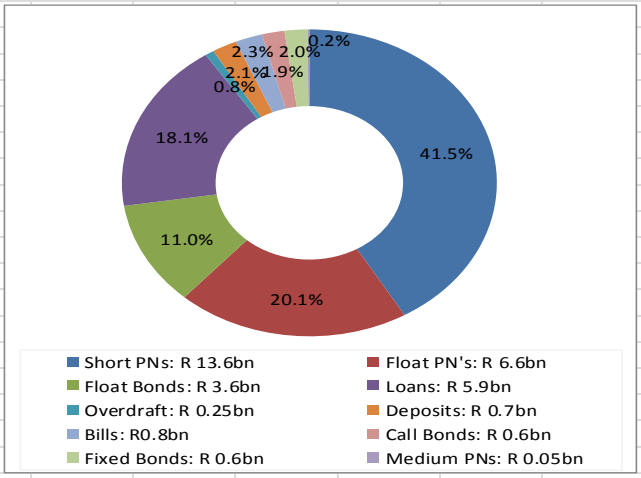


Figure 9: Funding Mix FY2016



V. CAPITAL INJECTIONS

As noted earlier in the document, the Bank aims to adopt the Basel II Standardised Approach to determine the minimum Capital Adequacy ratio that the Bank wishes to maintain. Based on these principles, Table 16 below features the minimum demand for capital (as risk-weighted assets), which takes into consideration credit and operational risk associated with the projected growth in the loan book, whilst Table 16 details sources of Capital available to the Land Bank.

Table 16: Demand for Capital (Basel Standardised Approach) – R'm

Risk Weighted Assets – Standardised Approach	FY2016	FY2017	FY2018	FY2019	FY2020
Credit Risk	35 896	40 542	43 763	47 012	51 308
Cash	313	314	313	337	355
Guarantees	320	366	395	423	468
Loans and Advances	35 263	39 863	43 055	46 252	50 485
Operational Risk	2 092	2 182	2 390	2 771	3 215
Equity Risk in Banking Book	12	12	12	12	12
Other Assets	87	87	87	87	87
Threshold Items	500	500	500	500	500
Total	38 587	43 324	46 753	50 383	55 122

Risk Weighting (Standardised Approach for Credit Risk)	
Credit Risk	
Cash held at RSA Banks	20%
Guarantees Issued	100%
Loans and Advances	
Performing Loans – Risk Weighting	
Corporate	100%
Retail/ Commercial	75%
Non-Performing Loans – Risk Weighting	
Corporate	150%
Retail/ Commercial	150%
Operational Risk	
Gross Operating Income	188%
Equity Risk in the Banking Book	
Listed Investments	100%
Unlisted Investments	100%
Other Assets	
Property and Equipment	100%
Threshold Items	
Significant investments in Financial Entities	250%

Table 17: Supply of Capital (Basel Standardised Approach) – R'm

Qualifying capital & reserves	FY2016	FY2017	FY2018	FY2019	FY2020
Common Equity Tier 1 (CET1) Capital: Instruments and Reserves	5 520	6 655	7 179	7 947	8 879
Common Equity Tier 1 Capital: Regulatory Adjustments	(315)	(338)	(331)	(325)	(319)
Goodwill and Intangible Assets	(32)	(55)	(48)	(42)	(36)
Defined benefit pension fund assets	(283)	(283)	(283)	(283)	(283)
Significant investments in banking, financial and insurance entities (above 10% threshold)	-	-	-	-	-
					-
Total available Common Equity Tier 1 Capital					
					-
Tier 2 Capital					-

General allowance for credit impairment	450	508	548	589	642
Portfolio provisions	2 724	2 898	3 136	3 374	3 685
1.25% of Credit RWA	450	508	548	589	642
					Total available Tier 2 Capital
Total available Capital	5 654	6 824	7 396	8 211	9 202
Guarantee					
Total RWA	38 587	43 324	46 753	50 383	55 122
Capital adequacy ratios – Standardised Approach	-	-	-	-	-
Excl. Guarantees					
Tier 1	13.5%	14.6%	14.6%	15.1%	15.5%
Total	14.7%	15.8%	15.8%	16.3%	16.7%
Incl. Guarantees					
Total	21.9%	19.2%	19.0%	19.3%	19.4%

To optimise its developmental impact, the Bank projects that it will require support from the shareholder in the form of either a direct capital injection or of financial sustainability capital guarantees amounting to:

FY2018 : R2.25 billion
FY2019 : R2.25 billion
Total : R4.5 billion

Should direct capital injections not be feasible, capital (sustainability) guarantees, which are off-balance-sheet capital instruments, would still be deemed "qualifying" capital under the Basel II Standardised Approach.

In the event of capital support in the form of a direct capital injection, or a capital guarantee from the shareholder, the table below outlines the scenario which details the financial impact.

Table 18: Scenario Analysis with/without Capital Support – R'm and %

	Base Case – No Support		**Scenario – R4.5bn Support**	
	FY2016	**FY2020**	**FY2020**	**Impact**
Total Loan Book	38,618	54,499	60,241	+10.5%
Sector Growth Loan Book	1,440	4,023	6,630	+65%
Funding Liabilities	31,782	47,156	47,530	(0.1%)
Net interest Income	1,067	1,891	2,230	+17.9%
Net Profit/ (Loss)	(146)	932	984	+5%
Retained Earnings	1,721	4,347	5,226	+21.2%
Total Equity	5,520	8,879	14,250	+60.5%
Basel II CAR % incl. Guarantee	21.9%	19.4%	22.8%	+3.3% ABS
Cost-to-income	55.0%	37.2%	33.8%	(3.4%) ABS

It is evident that capital support will result in a more sustainable business model, increased contribution to expanding the agricultural industry, especially in providing support to emerging farmers and increased profitability.

Strategically, the Bank foresees the following impacts:

- Increased loan book growth (R5.7 billion more)
- Significantly increased development investment (by 65%, or R2.6 billion)
- No real impact on overall funding liabilities, but a significant decrease in funding liabilities relating to assets of which a portion could be "free funded" through capital
- Increased net interest income (by 17.9%, or R338 million)
- Decreased cost-to-income ratio (by 3.4% in absolute terms)
- Improved profitability (by 5%, or approx. R50 million)
- Improved levels of retained earnings and therefore higher capital and reserves (by 21.2%, or R0.9 billion)
- Improved capital adequacy ratio (3.3% improvement in absolute terms).

The Bank will therefore formally apply for Capital adequacy support amounting to R4.5 billion from FY2018 – FY2019 in due course. Furthermore, subject to approval from the National Treasury, the Bank will target a minimum total CAR (including government guarantees not utilised to secure funding lines) of 15% under the Basel II Standardised Approach.

Additional capital injections will ensure that the Land Bank:

1. Can execute its Corporate strategy;
2. Maintain a sound and sustainable Capital Adequacy position;
3. Have sufficient capital as a buffer to absorb potential losses, mainly due to the expected deterioration in the overall credit risk as a result of increased investments to encourage commercial development growth; and
4. Maintain its credit rating

VI. SHAREHOLDER AND LOAN COVENANTS

As highlighted in the Borrowing Plan, the Bank is in process of adopting a number of new credit risk, liquidity and capital management frameworks, it is anticipated that the outcome of the quantitative analysis will result in certain shareholder and loan covenants being revised. Affected covenants include:

- Capital adequacy ratio – from existing "gearing" covenant to a minimum CAR of 15% in terms of the Basel II Standardised Approach;

- Liquidity Ratio – from existing Cash Levels of 7.5% of Short Term Funding (defined as those maturities less than 6 months), to a LCR of 60%;
- A NSFR of 80%; and
- Non-performing loans ratio ("NPLs") – from existing "customised" Land Bank definitions to a standardised 90 days in arrears type definition in terms of IFRS 9. A NPL ratio of 12% for FY2017 and 10% thereafter is proposed.

The Land Bank formally requests the approval of these target ratios and levels.

VII. RECOMMENDATIONS

It is proposed that the Honourable Minister of Finance approves this Borrowing Programme, with specific reference to the following:

Commercial/ Corporate lending:

- To issue Land Bank authorised money and capital market instruments to fund budgeted loan book growth and maturing debt not rolled over during FY2017;
- To arrange and renew overdrafts, overnight facilities, term loans, syndicated loans and revolving credit facilities with commercial and other banks and financial institutions;
- To issue financial instruments through the R20billion Domestic Medium Term Note Programme;
- Engage with the qualifying South African branches of international banks to access new pockets of liquidity that can potentially support Land Bank; and the tenor, interest rate and amounts to be issued be authorised in accordance with existing delegation of powers.

Development lending:

- To enter into direct loans and credit lines with DFI's and Multilateral Funding Institutions.
- The tenor, interest rate and amounts to be issued be authorised in accordance with existing delegation of powers.

Foreign currency:

- To borrow up to an equivalent ZAR amount of EUR50m from German Development Bank (KfW).
- The tenor, interest rate and amounts to be issued be authorised in accordance with existing delegation of powers.

Shareholder covenant ratios:

- Minimum Capital Adequacy Ratio of 15% in terms of the Basel II Standardised Approach;
- Liquidity Cover Ratio of 60%;
- Net Stable Funding Ratio of 80%; and

- Non-performing loans ratio of 12% for FY2017 and 10% thereafter

The Honourable Minister of Finance is also requested to note the intention of the Land Bank to formally apply for:
Government guarantee to support funding activities:

- Issue a R4billion Government guarantee to support the raising of long term funding by the Land Bank.

Direct Capital injection / Government guarantee to support solvency and Balance sheet growth:

- Issue a R4.5billion Government guarantee over the next 3 years to support Balance Sheet strength of the Balance Sheet of the Land Bank.

Compiled by:

_____

Land Bank Treasury Division

Date:

Recommended/Not Recommended

_____

Chief Financial Officer

Date:

Recommended/Not Recommended

_____

Chief Executive Officer

Date:

Recommended/Not Recommended

_____

Chairman of Land Bank Board

Date:

Approved/Not Approved

_____

Minister of Finance

Date: