Explaining the impact of African Bank on your investments

Focused Investing

STANLIB

14 August 2014

Last week Wednesday, 6 August 2014, African Bank Investment Limited (ABIL) issued an announcement forecasting a loss of at least R6.4 billion in the 2014 financial year, the resignation of their long-time CEO and the need to raise at least R8.5 billion in additional capital. This in turn raised questions around the future of African Bank as a going concern.

The share price reacted negatively and moved from R6.86 at the close of business on 5 August 2014 (i.e. right before the announcement) to R0.31 as at close of business on Friday 8 August 2014.

On Sunday, 10 August 2014 the South African Reserve Bank (SARB) issued a statement to say that African Bank has been placed under curatorship and the stewardship of Tom Winterboer of PricewaterhouseCoopers.

While the recent news flow surrounding African Bank has been unsettling, the SARB has responded to calm the market concerns and the clients of the bank through the provision of significant financial support. African Bank will essentially be divided into a “good” bank and “bad” bank and these two sections will be financed separately.

The “good” vs the “bad”

During the global financial crisis, one of the methodologies adopted by the authorities to deal with troubled banks was to split them into a “good” bank and a “bad” bank. While the difficulties within African Bank are completely unrelated to the global financial crisis, the SARB has adopted the same principle in providing assistance.

The “bad” bank portion of African Bank, which has a net loan book of around R17 billion, will be ring-fenced and effectively “sold” to SARB for R7 billion. Within the “bad” bank, the curator will endeavour to collect all outstanding loans. This means that existing customers will have to repay their credit facilities in line with their legal obligations. This portion of the bank will eventually cease to exist.

The “good” bank, which has a net loan book of around R26 billion, will continue to operate as African Bank, but with certain conditions and oversight from the SARB.

To support the “good” bank, there is a commitment of R10 billion from the consortium of commercial banks (namely ABSA, Standard Bank, Capitec, Investec, Nedbank, and FirstRand) and Public Investment Corporations to underwrite its capital raising in the market. The financial support from the consortium will bolster the capital base of the “good” bank.

Impact on the investor

All investors in African Bank either direct or through their unit trust portfolios, will feel some impact. The impact on individual investors in the STANLIB funds will vary depending on the exposure of their chosen funds.

Certain STANLIB funds have exposure to either shares in African Bank or fixed interest instruments issued by African Bank or both.

Portfolios with equity exposure have experienced a market-related loss due to the decline in the share price. At this stage, trading in these shares has been suspended on the Johannesburg Stock Exchange on SARB’s instructions.

This is the list of STANLIB's funds with equity exposure to African Bank:

Funds affected through their equity exposure	Exposure as at close of business on 5 August* (%)	Exposure as at close of business on 8 August (%)	Impact on the market value of the fund as at 8 August (%)	Year to date performance to 8 August ** (gross) (%)
STANLIB Balanced Fund	0.45	0.01	-0.42	6.42
STANLIB Balanced Cautious Fund	0.18	0.01	-0.17	4.92
STANLIB Equity Fund	0.75	0.02	-0.71	7.66
STANLIB Financials Fund	5.34	0.26	-5.10	8.69
STANLIB Growth Fund	2.23	0.10	-2.13	9.94
STANLIB Inflation Plus 5% Fund	0.85	0.00	-0.48	3.86
STANLIB Medical Fund	0.86	0.00	-0.46	5.50
STANLIB SA Equity Fund	1.04	0.03	-0.99	9.61
STANLIB Value Equity Fund	6.11	0.15	-5.79	3.25

* as at close of business on 5 August, the ABIL share price was at R6.86.
** On Monday 11 August the company was placed under curatorship and trading on the JSE was suspended. Therefore the last known price for the ABIL share was at close of business on Friday, 8 August, which is why we show returns up to that date. These returns account for the impact of the share price decline.

The portfolios with exposure to fixed interest instruments are impacted by a write-down in the value of those fixed interest instruments, referred to as the "haircut". The senior debt has been written down by 10%, while the subordinated debt and preference shares have been written off altogether. This is as per the recapitalisation agreement and the guidelines issued by the SARB on 10 August 2014.

This is the list of our funds with the fixed interest exposure to African Bank:

Funds affected through their fixed interest exposure	Exposure before write-down on 8 August (%)	Exposure post write-down on 11 August (%)	Impact on the market value of the fund effective 11 August (%)*	Year to date performance to 11 August*** (gross) (%)
STANLIB Absolute Plus Fund	0.23	0.00	-0.23	7.56
STANLIB Aggressive Income Fund	6.79	5.48	-1.38	5.59
STANLIB Bond Fund	1.30	0.90	-0.41	4.25
STANLIB Enhanced Yield Fund	6.06	5.54	-0.61	2.65
STANLIB Extra Income Fund	4.40	3.98	-0.44	4.62
STANLIB Flexible Income Fund	8.43	7.66	-1.84	3.39
STANLIB Income Fund	6.47	4.94	-1.66	2.66
STANLIB Inflation Plus 5% Fund **	6.10	3.50	-2.60	2.76
STANLIB Institutional Money Market Fund	0.71	0.68	-0.07	3.08
STANLIB Money Market Fund	1.72	1.56	-0.16	2.98
STANLIB Prudential Bond Fund	0.55	0.43	-0.12	4.09

* Please note that this is not an arithmetic difference, but a weighted difference.
** Returns for this fund are an estimate only, due to the nature of the underlying instruments.
*** The write-down of ABIL's fixed interest instruments was effective on first trading day after the SARB announcement, which was Monday 11 August. This is why in this table, we show returns up to that date, to account for the effect of the write-down.

Looking forward

The SARB announcement has brought some stability to the debt market and a measure of certainty for the future of African Bank. The write-down and its impact have been fully accounted for in the affected funds. African "good" Bank will continue its operations as "business as usual".

Last week's events reinforce the benefits of a well-diversified investment portfolio. All investments carry a risk to some degree; however, investing across many different shares, sectors and asset classes spreads the risk and diminishes the impact of an adverse event, such as we have seen with African Bank. So while the impact on African Bank's share price and debt instrument has been significant, the impact on your STANLIB portfolio is marginal.

We will continue to engage with all the relevant stakeholders and will keep our investors informed regarding any significant new developments.

Regards

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