

# Land Bank and Cadiz

On Thursday 23 April 2020, the 108-year-old, Land and Agricultural Development Bank of South Africa (Land Bank), which is the country's largest agricultural focused lender that supplies about 30% of loans in the agricultural industry, defaulted on debt due triggering a cross default on certain other notes and bonds that the Land Bank uses to fund their operations.

This culminated in the bank experiencing a liquidity shortfall and requesting all noteholders to consider a one-year deferral of interest and capital payments that are due in the next six months, while it engages in talks with various stakeholders to address its financial obligations.

National Treasury provided Land Bank with a R5.7 billion guarantee in February and is now considering further recapitalisation and additional guarantees to assist the Bank.

A Noteholder Steering Committee has been formed, under the Association for Savings and Investment South Africa (ASISA) which aims to engage with the Land Bank to find a workable solution due to the important role it plays in supporting farmers and ensuring food security.

Cadiz have for many years been a supporter of the state-owned bank with its key shareholder being the National Treasury. However, in light of the default the Cadiz team decided on 28 April to take swift action and write down the exposure in our funds.

## WHAT DOES THIS MEAN TO THE CADIZ FIXED INCOME FUNDS?

### **Cadiz Money Market Fund**

We have written down the difference between the book cost and amortised value of the Land Bank Promissory Notes by 25%, which resulted in a negative daily yield but only for that specific day. A positive daily yield has subsequently resumed for the fund.

Distributions for the month of April have therefore been impacted by the write down, but by adjusting the distributions your capital remains protected in the fund.

The diversified strategy employed by the Cadiz Money Market fund however lowers the risk of loss during times of unexpected defaults as in the case of the Land Bank. The Fund continues to invest strategically across the money market yield curve to maximise yield while remaining within the risk parameters defined for money market funds.

### **Cadiz BCI Enhanced Income Fund**

The Cadiz Enhanced Income Fund held ~4.45% exposure to Land Bank via Floating Rate Notes and the Cadiz team decided on the 28 April to writing down this exposure by 25%, which resulted in a drop of ~1.06% in the value of the fund for that day.

The diversified strategy employed by the Cadiz BCI Enhanced Income fund, however lowers the risk of loss during times of unexpected defaults and remains true to its objective of providing cash beating returns over the medium to long-term with low variability of returns even during times of crisis.

### **Cadiz Absolute Yield Fund**

The Cadiz Absolute Yield Fund held ~6.13% exposure to Land Bank Floating Rate Notes and Fixed Rate Bonds and this exposure was written down by 25%. This was done on the 29 April which resulted in a drop of ~1.5% in the value of the fund on that day.

Defaults are very difficult to predict and near impossible to forecast. The diversified and actively managed strategy of the Cadiz Absolute Yield Fund once again lowers the risk of loss during times of unexpected defaults, as in the case of the Land Bank.

The Cadiz Absolute Yield Fund remains true to its objective of providing positive returns over any rolling 12-month period with consistent returns above that of income type funds.

## WHY DID WE TAKE THIS ACTION?

It is important to note that this pre-emptive measure, executed by the Team, has been done as a measure to mitigate the risk of our holdings, while a resolution is being negotiated by all market and industry participants, and it is also important to note that the write down may not be permanent and exposure may be written back up once a resolution is found and capital and interest payments resume.

Under a normalised default cycle, credit spreads more than compensate for potential capital losses due to default risk. Should defaults occur, the sizing and impact of the default is limited, and should not be significant enough to derail the broad long-term strategy of the fund.

The Cadiz Fixed Income Team has experienced numerous severe market conditions since starting out in credit markets back in the 1990s, which have included the Russian default crisis, the Dot.Com bubble, the financial fallout from 9/11, the Global Financial Crises (GFC) and the European Sovereign debt crises and many valuable lessons have been learnt along the way. The Team has focused on building a robust, widely diversified portfolio of credit instruments and has built up an enviable, long-term track record of doing so.

The negative impact is therefore short term and we feel that this action was prudent as it protects clients invested in the fund and ensures that existing clients, new clients, and those clients that choose to exit the fund are treated fairly.