



The Restructuring and Rescue of African Bank Limited – A Synopsis

With a transaction value of circa. ZAR66 billion, it represents to date the largest default, successful restructuring and rescue of a financial services provider in South Africa.



Deal Overview

African Bank Limited (“African Bank”), a wholly owned subsidiary of African Bank Investments Limited (“ABIL”), was placed into Curatorship by the South African Reserve Bank (“SARB”) and Minister of Finance on 10 August 2014 due to key concerns of possible severe impact of a bank failure on:

- Staff, customers and creditors of African Bank;
 - Banks, Money Market, Fixed Income and Other Funds in South Africa; and
 - Overall financial stability of and foreign investor confidence in South Africa – possible downgrade to “junk status” and increased borrowing costs.
- Tom Winterboer (a now retired PwC Partner) was appointed as the Curator, and PwC’s subject matter experts were appointed as advisors to the Curator to implement the Resolution Plan as initially proposed by SARB.
 - Curatorship was considered the best way to provide a legal framework within which the Resolution Plan could be implemented.
 - The Resolution Plan focused on creating an optimal outcome for creditors and staff of African Bank, and the South African banking and financial services sector as a whole.
 - Salient features of the transaction include:
 - Developing a detailed Resolution Plan which included a number of refinements and additions (as detailed below) to the Resolution Plan as initially proposed by the SARB;
 - Splitting of the “Good Bank” and “Bad Bank”;
 - Restructuring of senior unsecured and subordinated debt amounting to circa. ZAR56 billion;
 - New listings of the DMTN Programme (on the JSE) and EMTN Programme (on the LSE and SIX Swiss Exchange);
 - Amendments to the Banks Act which allowed the Curator to implement the Resolution Plan;
 - Introduction of the SARB, Public Investment Corporation (“PIC”), and a consortium of six banks being FirstRand, Standard Bank, Nedbank, Barclays, Investec and Capitec (the “Banking Consortium”) as shareholders of the Good Bank;
 - ZAR10 billion recapitalisation of the Good Bank; and
 - The Resolution Plan was successfully implemented on 4 April 2016 (20 months from the date of Curatorship) African Bank changed its name to Residual Debt Services Limited (“Residual Debt Services”), and Good Bank changed its name to African Bank Limited.
 - Services provided by PwC included corporate finance advisory, debt and equity capital advisory, restructuring advisory, due diligence, financial modelling, operational review, crisis management and stabilisation, deal integration, valuation, accounting, tax, banking and regulatory, stakeholder and overall project management

Innovation and creativity

Development of the Resolution Plan

- The Restructuring Plan as initially proposed by SARB was modified and further developed.
- Considered “bail-in”, “bail-out” and other alternatives.

Good Bank

- Sale of good business to Good Bank.
- Capitalised by ZAR10 billion, funded by the SARB (ZAR5 billion), PIC (ZAR2.5 billion) and the Banking Consortium (ZAR2.5 billion).
- All retail depositors of African Bank (circa. ZAR100 million) were unaffected and transferred to Good Bank.
- Trade creditors of African Bank were unaffected and transferred to Good Bank.
- All the staff of African Bank were transferred to Good Bank.

Senior unsecured creditors of African Bank

- Overall 90c/ZAR offer under transaction (as per the SARB announcement).
- Offered 80% of the claim as a new instrument in Good Bank.
- Offered 10% of claim as a cash settlement at transaction effective date.
- 90% of interest during Curatorship was settled at transaction effective date.
- 10% residual senior unsecured stub instrument offered by Residual Debt Services.
- Maturity extensions of up to 24 months.

Subordinated creditors of African Bank

- Offered ZAR1.4 billion new Basel 3 Tier 2 compliant subordinated debt instruments in Good Bank.
- 10% of the above offer was cash settled at the transaction effective date.
- Remaining balance offered as subordinated stub instrument by Residual Debt Services.

Residual Debt Services

- To remain in curatorship to optimise asset realisations, with Good Bank to provide most functions under a service level agreement.
- The SARB provided a senior secured loan of ZAR3.3 billion in order to facilitate the disposal of the good business to Good Bank, and a guarantee of ZAR3 billion to Good Bank to cover any claims that may arise as a result of the assets and liabilities transferred to Good Bank.
- Likely run-off of 3 to 5 years – designed as “self liquidating”.

Challenges and complexity

Viability of Good Bank

- Poor credit behaviour of existing customers would impact asset values, high risk of moral hazard.
- The current state and further deterioration of the South African economy impacts customers and may reduce credit worthy business for Good Bank.
- The Good Bank needs to diversify its business activity to reduce risk, improve financial performance and create a longer term viable and more attractive investment proposition.
- Increases in interest rates may impact affordability of loans, increase default rates and impact core lending business.
- The volatility of ZAR to international currencies has the potential to increase interest costs of Good Bank (as existing hedges unwind and costs to hedge in future increase).
- Reduced appetite for South African debt, sovereign rating (possibly downgrade to “junk status”) and possible increases in interest rates likely to increase costs of and ability to refinance.
- Capital adequacy considerations, including modelling of Good Bank future state and reaching agreement on regulatory capital requirements.
- Extensive engagement and negotiations with the SARB, PIC and the Banking Consortium. Engagement with numerous local and international creditors
- Extensive engagement with lenders and creditors (local and international).
- Public consultation documents needed to be published (to comply with the Promotion of Administrative Justice Act since the Curator was performing a public duty).
- Exchange Offer launched and creditors voted thereon. Failed acquisition of The Standard General Insurance Company Limited (“Stangen”)
- Stangen is an insurance company owned by ABIL which primarily provided credit life cover for customers of African Bank.
- A group of BEE shareholders launched an urgent application to the court to seek an interdict to prevent the disposal of Stangen to the Good Bank – which was granted in their favour.
- The acquisition of Stangen was no longer seen as viable given the legal process that had to be followed – resulted in increased execution risk and a potential delay in implementing the Resolution Plan.
- A cell captive arrangement with Guardrisk Limited was instead considered and introduced. Business Rescue of ABIL, Ellerine Holdings Limited and Ellerine Furnishers (Pty) Limited
- Extensive engagement and negotiations with the business rescue practitioners.

- Business rescue plans needed to be considered, negotiated and approved by African Bank as creditor.
- Primary objective of maximising recoveries for African Bank.

Regulatory

- Curator did not have the powers to implement the Resolution Plan – the Banks Act needed to be amended to allow the Curator to implement the Resolution Plan.
- Continued tightening of regulations by the National Credit Regulator (“NCR”) which negatively impacted unsecured lenders.
- Extensive engagement with regulatory authorities to resolve a number of issues, and obtain regulatory approvals and relevant licences (including banking, insurance, competition authorities and applicable securities exchanges) needed to be obtained to implement the Resolution Plan.

Value Created

Financial stability

- There were limited cash resources available to African Bank at the date of Curatorship.
- Daily cash monitoring, liquidity assessment and decision making.
- The cash position of African Bank significantly increased due to improved and strong collections of the loan book.
- New agreements were concluded to retain currency and interest rate hedging.

Operational stability

- The workforce and bank operations were stabilised.
- Improved credit and lending policies were introduced – strong performance against new criteria has been experienced.
- Responsible increases in customer loans.
- Operational turnaround and restructuring resulted in ZAR250 million in annual savings.
- Annual financial statements for 2014 and 2015 were finalised.

Management and Governance

- Key management were retained – executive committee and top 50 employees.
- Appointment of new CEO and CFO for Good Bank.
- Appointment of directors to the board of Good Bank.

Successful implementation of the Resolution Plan

- Exchange Offer accepted by more than 95% of creditors.
- The Resolution Plan was successfully implemented on 4 April 2016 as the first “bank bailin” in South Africa.

- Considered to be the best outcome for staff and creditors of African Bank, the South African banking, and financial services sector as a whole with systemic risk successfully mitigated.
- More than 5,000 jobs were saved.
- African Bank continues to provide unsecured lending available to a key segment of the market that does not meet lending criteria imposed by traditional banks.
- The Resolution Plan has been recognised internationally with much interest from bodies dealing with bank resolutions.

SARB exposure to Residual Debt Services

- The senior secured loan of ZAR3.3 billion was repaid in full on 1 September 2016.

Key Parties to the Transaction

- Minister of Finance
- South African Reserve Bank
- Public Investment Corporation
- Banking Consortium (FirstRand, Standard Bank, Nedbank, Barclays, Investec and Capitec)
- National Treasury
- Tom Winterboer (Curator)
- Advisors to the Curator
 - PwC (various roles)
 - Webber Wentzel (legal and tax)
 - Linklaters (legal)
 - Prinsloo, Tindle and Andropoulos (legal)
- Management and staff of African Bank
- Creditors (including their advisors) of African Bank
- Securities Exchanges (JSE, LSE and SIX Swiss Exchange)
- Competition Commission of South Africa
- Financial Services Board
- National Credit Regulator
- Rand Merchant Bank (corporate finance advisor to the Banking Consortium)
- ENS (legal advisor to the Banking Consortium)
- Werksmans (legal advisor to SARB)
- Deloitte (reporting accountant)

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