REPUBLIC OF SOUTH AFRICA
COMPETITION COMMISSION

Competition Act, 89 of 1998

MEETING WITH STANDARD BANK

OPEN SESSION

DATE: 2017-10-30

VENUE: PRETORIA CSIR CONEVENTION CENTRE

CHAIRPERSON: Ms L Mtanga

COMMISSION MEMBERS

Ms S Grimbeeck : Principal Economist
Mr T Khumalo : Senior Legal Counsel
Prof Halton Cheadle : Apology

ON BEHALF OF STANDARD BANK SOUTH AFRICA

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In the hearing of

COMPETITION COMMISSION AND STANDARD BANK

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PROCEEDINGS ON 30 OCTOBER 2017

CHAIRPERSON: Good afternoon ladies and gentlemen. I will now proceed to hear the presentation or the submission from Standard Bank.

We do understand that there were certain aspects that you did not, you required, that you said you are not prepared to address. We took note of those and also we noted the two aspects that you requested that you do the presentation on in a closed session.

We suggest that you cover everything else in this public hearing and then we deal with the closed session aspects at the end of the, after the public one. So if you are ready we are, let me just double check again. We had lots of technical issues earlier on. Are we all ready to start? Okay. Okay thank you, you may proceed then.

MR GARRET: Thank you. Good afternoon. I would like to up front just thank you for inviting Standard Bank to participate in the hearing and to provide our views on the factors we consider as financiers in providing financing for the development of retail property and the extent to which these factors may or may not facilitate the prevalence of long term lease, long term exclusive lease agreements between property developers and the anchor tenants of shopping centres.

I think just by way of introduction our panel is made up of members of our team from real estate finance which forms part of the corporate and investment banking pillar in Standard Bank and just to introduce the team. To my right is Karin Joubert, she is an executive in the real estate finance business. To my left is Genevieve Naidoo, she is the head of credit for real estate incorporate and investment banking. Directly behind me is Sharon Brighton she is the head of legal for real estate and then

I am Gary Garret, I am responsible for the real estate finance business incorporate and investment banking.

Thank you for, for addressing the letter that we sent through regarding certain questions and I think I would just like to create some context in forum for why we ask for them to be excluded.

Obviously in preparing for this we felt that some of these questions went beyond the initial scope as we understood it of the inquiry and I think as you would appreciate Standard Bank is a large organisation with many different businesses with varying mandate and I think to have got all of those people together at such short notice to cover all of those questions would have been fairly difficult given the timelines.

We did undertake in our, in the letter that we submitted to provide written responses in need.

So, so during our time today and in answering the questions we will explain the factors that we take into account in assessing finance for retail developments. I think at the outset it is important to highlight that we access each proposal for funding on a case by case basis and there is no simple formula that we apply.

So the factors that we are going to discuss or the principles and parameters that we generally access understanding that the level of analysis done on each transaction may be different and so if I can just try and highlight that by way of example.

If we fund a retail centre at a relatively high daring level where that centre is the only asset to which we have recourse for repayment we will do a much greater level of analysis on all of these factors on that particular transaction relative to for example where we lend into a company that, where we have a large portfolio of assets that we may have recourse to and where that entity may be very lowly geared.

The difference is being that in the first instance we rely purely on the specific property for repayment versus the second where we have a large pool of assets that generate cash flow to repay our debt.

Also as part of our opening comments I just like to re-highlight the factors that we consider when looking at funding for retail centres. These were set out in our correspondence dated 16 August and include the developer and the professional team, the property fundamentals and the commercial viability of the centre and we can get into each one of those in more details as required and we will obviously do that in answering the questions that were provided to us.

And perhaps finally in our opening comments just to provide clarity on Standard Bank's stance regarding exclusivity clauses in lease agreements. We do not request or require exclusivity clauses in lease agreements and nor are there a factor that we consider in assessing funding packages for retail centres.

That is probably all we wanted to say in opening. Just in terms of understanding the format of how you propose to run the session Madam Chair, we have obviously been through the questions and prepared on that basis and different members of our team are prepared to take different questions, so if we move around the order et cetera, you may just need to give us a few seconds to orientate ourselves and figure out who is answering. Thank you.

<u>CHAIRPERSON</u>: That is fine with us.

<u>MS JOBERT</u>: Madam Chair are you going to run through the questions, should we wait for you to prompt us?

<u>CHAIRPERSON</u>: Okay. I actually wanted to understand that, I was actually checking with my colleague. With the previous presentation they sort of had a longish submission where they gave us an overview to everything that we had asked but I see with you, you are doing an intro the way you have.

I just want to ask then on, just based on what you said Mr Garret, you say you do not... in deciding whether or not to fund a development retail, specific to retail development you do not consider, you do not take into account exclusive leases and you do not require them. Do their existence have any bearing whatsoever in how you would then fund a certain return development?

MR GARRET: No they do not, we do not consider them a positive or negative factor. We do not, we effectively ignore them in assessing whether or not we are going to provide a funding package on a particular retail centre, it is not something we consider at all.

CHAIRPERSON: Okay and then my next question was more of what our second question was in the list of questions which you have not taken out, number 2. I think we, you need to appreciate that we have not heard from any banker during the, this enquiry so we have no idea whatsoever how a bank operates when it starts an, who approaches whom in relation to a development.

So my first question would be, can you give us a sense of how does a bank ordinarily get involved? Is it you being approached by a developer seeking funding or is it also a case of a bank having identified sites that it thinks a development might be good for development and therefore you look for developers out there. How, how is that relationship initiated, that is the starting point.

MS JOUBERT: So we would normally as the real estate finance team we will be approached by a developer, so let us assume there is a new retail development that is going to take place, the developer will approach a number of banks usually and provide us with a finance pack.

Now that finance pack is just a document really and it sets out the proposed development, it sets out the location, it sets out the size of the retail development, the target market, it also sets out the tenants, the tenants that they have identified and who they would have engaged with already and obviously who they propose occupies the centre and it will also include an initial feasibility, not the final feasibility but the initial feasibility that they have put together in terms of the total development cost and the total return and that total return, would generally be determined by the developer in conjunction obviously with his professionals and after consulting obviously with all, engaging with the tenants in terms of the rental levels and base on that information we will, well we will then receive the pack and he will set out what his requirements would be for the debt application and we will assess each and every, one of those factors.

So we have previously outlined very comprehensively the main factors that we take into account when we look at a funding application but that is, that is how it reaches us. There is a funding pack presented to us and a developer will then ask us for a certain funding amount based on that funding pack information.

CHAIRPERSON: So that, that funding pack is the funding pack that could have been presented to a number of banks for example to self get different offers and see which offer would be better?

MS JOUBERT: Correct Madam Chair so it could be in some instances the client only banks with Standard Bank or Nedbank and they might only go to that bank or in other instances they will give it out to a number of banks to get a competitive offering if they believe they need a more competitive offering and options.

CHAIRPERSON: Okay. Just to link up to this, this, your assessment of that application then in relation to the last presentation that we heard we, and also how that relates to exclusive leases.

We heard a, there was a suggestion by Massmart for example that exclusive leases, leases should not contain any exclusive clauses, this is for us to decide not for you to decide obviously, however they said there may be an exception in instances where a development is, could be viewed as high risk development.

Are you able to take us through what would you consider as a bank to be a high risk development and then on high risk development what factors would fall under these two types of developments?

High risk, a high risk development, when you are presented with that pack.

MS JOUBERT: Sure. So as part of the assessment or the analysis that we undertake, so we, we do not, we would not obviously know if it is a, as you refer to it a high risk or a low risk assessment, so we will undertake our entire assessment in the usual way.

We will look at the location, is there a market, so you always have to obviously establish if there is a market, from a supplier and demand perspective and is there a, is there sufficient consumer spending in that marker to support a new retail development and then we will look at, and I am not going to go through all of them, we will look at the developer and professional team and then at the property fundamentals and commercial viability.

If we believe that there is no market then we would merely go back to the developer and confirm that we do not have any appetite to fund the development.

So we do not, we do not go back and say this is high risk or this is low risk, we just go back in terms of do we have appetite and what is our appetite level.

CHAIRPERSON: On, on the point of market, the existence or none existence of the market that is, that is a factor that a developer must present to you, so you look at the documents that they are presenting to you am I correct?

MS JOUBERT: We look at the documents that they present to us but we also do our own analysis so in most instances for, let us assume it is a large regional mall, they will undertake a demographic study.

That study is quite a lengthy document setting out obviously the extent of the target market and their spend power and the competing centres et cetera.

But if we feel that we, well we in any event supplement the assessment from experience in the market because we might have a centre that we funded next door so we can obviously supplement the analysis as well.

We do not necessarily just base our assessment on what the developer provides us.

CHAIRPERSON: Okay from, from the side of, from our part as the inquiry team, if for example we are to come across a development that has been funded by Standard Bank can we assume that it is a development that would have at least ticked that aspect of a market being in existence prior to the development being there?

MS JOUBERT: Sorry we are just conferring if you do not mind for 2 minutes.

CHAIRPERSON: Okay.

MR GARRET: So I think, I think to respond to that if we go back to the opening remark I made, I think if it is a standalone centre where that is the only collateral that we have and that is the only basis of us repaying our loan you can assume we have assessed all of the factors that we have set out in detail.

If for example we are lending to, let us call it one of the reeds on the, you know those listed on the stock exchange, often the gearing in that companies is very small and we have sizable collateral pool that we have access to.

So there are many properties within that portfolio that can generate cash to repay our debt.

The level of analysis we may do on a single new centre that they want to develop and want to purchase may be a lot less than if we were just relying on one asset for repayment and that is what I said we do not have a, simple formula for each and every transaction that we do, but these are broadly the factors that we would consider.

CHAIRPERSON: Yes Mr Garret I understand that, but what I also want to understand is, I just want to understand what would be the fundamentals or the basics that a development would have ticked if it does get funding from Standard Bank can we assume as this enquiry that that funding Standard Bank was happy with the existence of the market, with consumer spending, with the professional team of the development team, the professionalism of the development team, those because it is those factors that we want to see what, what is it that, what factors would you have been happy with in general terms because they will be the, the, the general ones that you know they are no brainer, without those you are not going to go into that funding, so that is what we are looking for.

So once you are presented with a pack what is it that you will, you first look for and then you go for the specifics of the area and all those, the gearing issues that you are mentioning, those would be very specific to that particular development but in general as Standard Bank what would you be looking for? The market, consumer spending, can we assume that those would be in existence at least when you do your funding?

MS JOUBERT: *Ja* so for a stand-alone transaction and we are specifically talking to larger retail developments. Remember the same level of analysis does not get or we do not do the full analysis for a small neighbourhood shopping centre. You are not going to have a full demographic study for a small convenience centre but you would ordinarily have one if you build a 30,000 m² regional mall. So I just want to make that point so that the detail that we have available would not be the same for every centre.

The assessment will however include a market analysis as far as, as far as we can determine the size of the market by various means, it could be, be a demographic study or it just can be simply by the details that we can give in terms of population size in the area and basically for smaller centres follow the roof kind of principle i.e. if there are enough households in the area to support a smaller convenient shopping centre that will give us a sense of will there be sufficient support for the centre or not.

We will obviously take into account competing centres, so if there are two convenience centres right or planned for, right next each other we will obviously take into account the size of the existing and of the new and whether we believe in our experience if the market is big enough to support both.

So that is the type of analysis we will undertake from a location perspective and we will not proceed if we do not believe in our opinion that the market would be there for a, for a centre where it is a standalone debt transaction, I just want to make that point as well.

We then, so as soon as we have location, the demographics or the spent confirmed we will also look at the proposed tenants and that will obviously occupy the centre, we will look at the layout is it appropriate, are we happy with the flow, line of sites, we can get very technical here, so we look at that and that basically covers the property fundamental side of it.

We then also look at the developer from a perspective of what experience does he have in terms of putting up the specific retail offering that he is proposing in terms of size, the location, is it kind of what he is used to in terms of what he has developed before and also his financial standing.

If there is costs overruns, can he chip in and fund that during the development period.

We also look at the professional team members to make sure that they have the necessary experience so we, and those would be the main professional members, it would not necessarily include a landscaper or some of the smaller guys but the main professional members we do look at and their experience and then the commercial viability, does it actually make sense based on the net rental that can be generated by that centre can that service and support the proposed debt facility and those would be the main categories that we look at.

That is not an exhaustive list by no means but it would cover the main ones [intervened]

CHAIRPERSON: The general ones.

MS JOUBERT: *Ja*.

CHAIRPERSON: Sure. Just looking specifically at the profile of the tenants in the mall, what exactly would you be looking for?

MS JOUBERT: So it is dependent on again the retail offering. You would need an anchor normally, we also obviously have strip retail that you do not need necessarily an anchor for so but generally if you look at a convenience centre or a regional mall, community centre, value centre you will have anchors so we will look at the anchors, are they strong enough to draw tenants to the centre because it is the consumer that is, that needs to spend at the centre and if they are not drawn to the centre obviously the centre is not going to generate cash flow so we will look at those tenants and their ability to actually draw consumers to the centre based on experience of other centres.

CHAIRPERSON: Okay. On the point, on anchor tenants. I do understand that we cannot go into specifics here, but I just want to understand as Standard Bank, do you have a list of anchor tenants that you consider to be strong enough at all times, irrespective of where the development is and therefore if they are present in that tenant profile, you are happy and then if a developer comes up, that is one, on the one hand and then on the other hand do you have a list of anchor tenants, that you will always be in doubt when they are presented to you and then you probably require a probe, more on the viability of that development.

How does this play out? And maybe in the closed session would you be able to delve into that clause, on the list of the anchor tenants that you consider strong enough and why you consider them to be strong enough, those you consider questionable and those that you think they are wishful, they wish they could be but they do not actually make the mark for you and why, would that be considered for a confidential, we want, now we would want know the specific names which anchor tenants have been put forward to Standard Bank in this way and you made these conclusions but do you make this decision beforehand and, and, and make a decision as to whether or not this is going to fly or not. This development can fly or not, from your perspective.

MS JOUBERT: Okay, so just from your, based on your or further to your first question, we do not have a list so we do not have a list of good, bad, not so good tenants.

So we look at when we get the finance back what are the proposed tenants by the developer, who he has engaged and we will evaluate it accordingly.

CHAIRPERSON: You do not have al list, you do not have [intervened].

MS JOUBERT: No we do not have a list that sets out these are anchor tenants that we like and these are anchor tenants that we do not like because of financial standing or, or not good financial standing.

CHAIRPERSON: So how would you then determine the strength of an anchor tenant?

MS JOUBERT: Well so from an anchor, so we would know from experience obviously in other centres how they trade, there is public information available on a number of tenants in the open, well obviously in the open market because they are publically listed entities but it is mostly from experience in terms of other centres, how are they operating in terms of that demographic study and will they also do well in, in the centre proposed but it does not mean we will, there is, *ja* so that is basically what we look at, we look at our experience of centres.

CHAIRPERSON: Okay again based on your, because I would [indistinct] based on your experience actually you would have that answer, you would know that a certain anchor tenant would be strong enough for a certain market because my next question for you would be for example if you have a development that goes into a township which anchor tenant would you consider strong enough for that market and which anchor tenant would you consider not strong enough for that market?

MS JOUBERT: I think Madam Chair it is going to be difficult for us to obviously talk about actual individual anchor tenants so you know we can obviously look at some of the question *in camera*.

CHAIRPERSON: Yes.

MS JOUBERT: And as you have said you know we only obviously represent a certain portion of the bank and we do not necessarily have the mandate to discuss some of the, you know the detail of that question. So what I will do is I will take of the question, we can discuss parts of it *in camera* and alternatively we can come back to you by written submission.

CHAIRPERSON: Okay.

MR KHUMALO: So based on what you, what you said earlier when you considered the funding package, one of the things you have mentioned is the developer and the professional team. Can you elaborate as to what is it about that developer that you are looking at? You mentioned their financial viability but can you give us a complete picture as to what do you look at?

MS JOUBERT: Sure, so from a developer perspective we look at their financial position, so if it is an individual it would be their normal assets and liabilities and if he has a company it would be the company's financial statements that we look at to see if there is, if he has the ability, obviously depending on the, the size of the development.

If it is a small development you are not going to require as much or the level of comfort that you would if you are looking at a R500 million or a billion rand development when there is cost overruns because cost overruns is a reality and there can be unforeseen circumstances, ground conditions that they did not know about or delays and the development need to, to fund that so we will normally look at his financial position t cover that cost overruns.

MR KHUMALO: Is it only the financial position that you look at?

MS JOUBERT: So for the, for cost overruns that is the, that is what we look at to see if he can carry the, the development.

MR KHUMALO: *Ja* but [intervened]

MS JOUBERT: But.

MR KHUMALO: But [intervened]

MS JOUBERT: So that is not all that we look at from a developer perspective, we look at the developer's experience as well in terms of retail development, has he done similar retail developments before, does he have the experience to develop and this type of retail and asset management, that type of development because it is one thing to put it up, it obviously has to also be asset managed afterwards and *ja* so we look at his experience in the retail environment.

MR KHUMALO: How critical is that factor in the analysis of the, of whether or not you grant the loan?

MS JOUBERT: It is very important to us because retail is not a, as vanilla as a normal office property would be. It is easier for, if you look at a multi let office building and to just replace a tenant with another tenant, but from a retail development you sometimes have to move tenants around to get the right tenant mix, the right flow of consumers so it is important for us that the developer does have experience.

MR KHUMALO: Okay so if someone is, someone has one successful say what did you mention $30m^2$ regional mall and they have been running that for 5 years would that be sufficient experience for Standard Bank?

MR GARRET: I think, I mean what is important here is we look at a variety of factors and we look at each deal on a case by case basis, so to simply ask is running one centre for 5 years with a centre size of $30{,}000m^2$ sufficient experience, I think that is a very difficult question to answer given that we look at a multitude of factors in deciding whether or not to provide funding to a development.

I think it is an important point too to say that you know like in, in anything typically developers of retail centres build up their businesses over time so the, you know I think for, for us it would be difficult for someone straight off the bad, first development to want to build a super regional mall which is complex, it is expensive, it could cost you know a billion rand or more and then run that without you know having been able to run smaller centres as a start.

So I think it is like any business. You tend to, you know our clients have tendered to start small and build themselves up over time.

So I think it is difficult to answer you know what is sufficient experience.

MR KHUMALO: *Ja* I mean we, we also, you have to understand like my colleague said we are not in the banking industry. Now we did I think say that you could present for 30 minutes in the beginning right, so you have elected not to do so and you are saying when we ask questions well we consider a number of things but you are not really telling us what those number of things are.

So, so we can only mention the ones that you have mentioned, so you have mentioned experience and financials. From thereon I mean we can only ask about those.

Can you maybe elaborate, what are these multitude of factors that you look at?

MR GARRET: Sure so, so I think they were outlined in our submission dated I think 16th of August and I think we recover them in the first question that you ask.

So perhaps we can go to that question 1 and just talk through that in detail.

CHAIRPERSON: Okay.

MS JOUBERT: *Ja* so we set out in, our answer in question 1 that we do have due diligence and we categorise the due diligence into three categories and again I just want to stress that this is not an exhaustive list, it would depend on the deal by deal basis.

We look at, the first category is the developer and the professional team. Second is the property fundamentals and the third would be the viability of the proposed retail property and as Gary pointed out in his intro the level of analysis will vary from client to client depending if we do a standalone transaction or whether it is part of a portfolio of assets.

If we move on to the development and professional team we look at as discussed the financial strength of the developer or the borrowing entity should this not be the developer and we look at the relevant experience in relation to retail property.

Generally including inter alia previous retail properties developed i.e. the size, the location and the complexity of such retail properties.

We do a further analysis on all the members of the professional team who will be responsible for the build of the retail property and specifically enquiries made on whether each member has the relevant experience in relation to retail property generally including previous retail properties where they have acted as professionals.

Again we consider the size, the location and the complexity of such retail properties. From a property fundamentals perspective we consider the below factors *inter alia*, a summary of what we consider for each development in determining whether it demonstrates the correct property fundamentals.

We consider the location of the proposed retail property, whether it is sound and whether there are any competing retail properties in the area that will be in direct competition to the proposed retail properties.

We look at, we inquire into the demographics of the shopper, households in relation to the proposed location and we also ask our project management team and/or the legal team if there are any encroachments, incumbencies, town planning and zoning issues that may need to be addressed with the developer or the professional team.

We then move on to the functional, review the functional layouts of the proposed retail property in terms of its access points, the entry and *egress* of the proposed retail property, the general flow of the proposed property, the parking and the size of the retail property.

Finally as part of the property fundamentals we will consider the tenant mix and the placing of the tenants within the retail property, the proposed rental amounts that the developers put forward, an escalations and whether the rentals being asked are comparable in the market for similar retail properties in similar locations.

From a commercial viability perspective we will fundamentally need to know whether the retail property will generate enough income on a sustainable basis in order to service and ultimately repay the loan from the bank. We will consider the level and quality of the rental income that would be a key factor in the funding decision including the level of equity that will be required by the client and the level of debt that could be supported by the proposed property.

At this stage we obtain information on all proposed tenants and establish the financial strength of each proposed tenant, what the gross lettable ratio will be per proposed tenant and whether overall the tenant mix generally will sustain the proposed retail development.

We would analyse the material lease terms and understand what rental would be paid.

We ask for a detailed reschedule on all tenants and ensure that the cash flow generated from such leases will ultimately sustain the underlying loan held with the bank.

It is also critical to ensure that the tenants presented to the bank during the assessment process as well as the material terms of their leases are not changed without the prior consent of the bank for the duration of the loan.

Upon conclude a full due diligence a financing structure will be proposed to the developer.

CHAIRPERSON: Okay. Sorry, I am going to take you back to… Sorry, that is Karin?

MS JOUBERT: Yes.

CHAIRPERSON: I just want to take you back to the question I asked about, about the profile of the tenants in the development. I have listened to you what you have given us as a list of what you would consider for a developer itself.

Would you say based on the factors that the bank, Standard Bank specifically takes into account in looking at a development pack that is put before it specifically on that profile tenant, tenant mix that a bank, a bank's decision or a bank's perception of the peers in the market has a bearing who ends up making it as a tenant in a mall or in a centre, what is your view?

MS JOUBERT: I do not fully understand that question, would you just rephrase it?

CHAIRPERSON: Would you say your, your, the factors that you take into account in considering whether there is a good profile tenant, a good profile, a good mix of tenants for a specific development that is presented for funding to Standard Bank, when that is presented before you and then you make a decision. Specifically on the tenant mix would you say the bank, the bank's decision as to who make it as a tenant in a, in a shopping mall has a bearing on the market and generally who ends up being considered a tenant?

MS JOUBERT: Madam Chair can [intervened]

CHAIRPERSON: Or the extent of, okay sorry?

MS JOUBERT: No I was just going to say could you just give us a minute to confer?

CHAIRPERSON: Sure.

MS JOUBERT: Thank you. Okay to answer your question, so as outlines initially we are presented with a pack, so we are, it is confirmed to us who would be the anchors line shops or what we call the moms and pops and the nationals. We do not decide who makes it and who do not make it as you put it, we are given the info, or the tenants and the tenant mix.

CHAIRPERSON: You know the reason I am asking this question is that in the, in the, on the, in the one on ones we have had with some property developers it has been mentioned to us that banks tend to have a preference for certain types of tenants to be in the mix and those to be, that lease agreements be entered into with them prior to the bank considering the, whether or not, whether or not it is going to fund a development.

So that is why I was asking that question but I was asking it in an indirect way to ask you if do you have a, do you think your decision on approving and not approving certain tenant profiles actually has a bearing on who ends up making it as a tenant, that is why I was asking that question in that fashion.

MS JOUBERT: Ja just a general market principle, so in a centre you would need an anchor.

CHAIRPERSON: Yes.

MS JOUBERT: Okay so let us assume it is a normal convenience regional, whatever. So there is a, a requirement that there must be anchors to draw clients to the centre obviously, so there would be a general acceptance that you would have an anchor, whether that is a X, Y or Z.

As long as they have the ability to draw tenants, so if that anchor is a food anchor we are going to be, we will obviously consider do they have the ability to draw tenants to that centre based on our experience of other centres with similar demographic and spending power et cetera.

So *ja* and the developer would, I am assuming, would know that as well and would also look at sustainability of his cash flow because he is ultimately responsible for that loan so they do not, they do not engage with us up front if that is kind of what you are alluding to, to prepare the pack and include a certain name. We are given a set financial pack and which generally have most of the tenants on there, except obviously for the smaller... well not all of the tenants but it will have the main tenants on there and then obviously as they develop they would fill the space up to point of completion.

CHAIRPERSON: Okay. My last question on this point, all the tenants that are in the pack for, when you look at it, is there any, any preference or, I will say, I will call it preference for Standard Bank that this is before, offers a duration a short or long, let us say if he is an anchor tenant you would want a lengthy lease entered into with the tenant and then if it is a relatively new tenant where you require maybe two years, three years what, can that be influenced by a banking decision or is that solely within the decision and discretion of the property developer as to how long the lease agreements are with the tenants in the mall or in the centre?

MS JOUBERT: Madam Chair just give us a minute to confer.

MR GARRET: I think, I think our response to that and I will try and take it in a few ways is that when we look at a proposal we generally can fund it on particular basis or we elect not to. It is, it is very difficult for us to influence ultimately who the tenants are.

The developer has already entered into negotiations very often with some of the bigger tenants, the anchors or the sub-anchor tenants in the centre before we get the funding pack to know that there is, there is retailer demand for that, for that particular product.

If we look at, at a tenant make up and we do not like it, our decision is generally going to be, we probably not going to want to fund that centre. If we do like it then we are happy to fund it. It is very difficult for us to, to say that you know we want this retailer to fund it, that, I do not think that is our business.

We could provide reasons to the developer that we do not like the tenant mix and he may relook at that but we, we, we do not generally, actually we do not tell the developer that it has to be tenant A or tenant B for us to be able to fund it.

I think you will, your second question around duration of leases and perhaps if I could, if I could just talk through that because one of the questions, I think question 11 referred to how long on average it take a developer to repay a retail property development and what is the appropriate duration of a lease agreement.

So perhaps just to talk through that the length of time that it would take a developer or an owner of a retail property to repay us is dependent on the level of gearing typically that is in there, the higher the gearing the longer it is going to take them to repay us.

So it is very difficult to say you know what is the average duration but I will try, I will use an example and say that if we make an assumption that a centre is geared at 70%, so that means if a centre is worth R100 and we put in debt of 70 and there is equity of 30, it would typically take around 11 to 12 years for that centre to fully repay its debt down to zero.

And so you know, in trying to comment on what is an appropriate lease duration what we typically see is that anchor tenants would sign leases for around 10 years but your sub-anchor is going to sign leases for between 3 and 5 years and that your line shops would sign leases of between 2 and 3 years and that is, that is a generalisation but that is typically what we see in, in the development proposals and I think important to highlight here what we can see is that the duration of all of those leases is, is, is shorter than the typical repayment period of a centre that is geared at 70%.

And so what is absolutely critical over the life cycle of that centre is that those, is that those leases are continuously renewed or that you know if they are not renewed that substitute tenants are put in to be able to ensure that there is sufficient cash flow that is generated by the centre to repay the debt.

So hopefully that answered the question in the two parts around how we think about tenant mixes, we do not influence and then just to give you a sense of what we typically see as the average duration of leases.

CHAIRPERSON: Okay. Just on that last point, so would it be, would we be correct in our understanding that you also do not influence the duration of the lease in any way of form?

MR GARRET: We do not influence the duration, we can take a decision on whether we believe that the tenant of those leases is appropriate for us to be able to fund against.

Ja and that is pretty much what we do. I think what I have highlighted though is that what we typically see in the market, so this is very much market practise and this is what we would generally see in proposals that are put to us.

CHAIRPERSON: Okay and can you just give us a sense on, we just want to understand what happens because we are sitting here in a very difficult situation. When we ask questions, when a property developer comes in - we have got two that are coming tomorrow and we have met with a couple - they push back their answers to banks and then you are here saying we actually are presented and, so we want to understand whose, whose responsibility it is to make these decisions because it is decisions that are being questions by other players in the market.

One of them is declaration of the leases for smaller players for example. If I may be clearer on why I am asking this question, the critical question that has come to this enquiry is that most anchor tenants, anchor tenants have longer duration leases and these kind have favourable terms for anchor tenants.

This is what happens in a development and then when you, when you are a smaller player even when you are in the township and you are a smaller player that has been operating outside you had a standalone business that was profitable prior to the development and you, you have even financial statements to show that you were actually profitable in a township environment and you are still going to operate.

To be operating in a township mall in the township and the, the, you suddenly you come into this mall that is being funded and the, the 10 year of your lease is now shortened to 2 years, 3 years and every time there is a renewal the terms increase, it becomes better some... they become... it becomes more expensive.

Three to five years down the line you will find all those smaller players exiting the market slowly and we want to understand who, who has a bearing on that decision so that is why, that is why I was asking this question but I did not want to go into this background but I feel I must.

If you can just maybe comment on that, who has a bearing on, on the tenure of these leases?

MS JOUBERT: Okay so to specifically answer your question around the smaller tenants and the impact that could have i.e. renegotiations, high rentals, whatever.

So, when we presented obviously with a pack as I alluded to you before we, they, we normally see the anchor tenants already and your anchors would typically have 10 year leases because that is what anchors your centre and kind of brings the lease period in line with the repayment period because remember it is a long term asset.

So they would typically have longer dated, we, we almost never see an anchor with a lower than a 10 year lease period and then your sub-anchors generally 5 years and then your smaller moms and pops lower than that, but we in most instances will not even see those tenants at that stage so for a regional mall because they get fold in as you let out so that is a question that should be posed directly to the developer to understand kind of the dynamics around why they go for shorter periods.

Or may, *ja* you need to ask them maybe the tenant only wants to commit, because remember it is a long dated commitment also to commit for 10 years.

It is very difficult to take a view over 5 years so it could be driven from, by both parties so I would suggest you kind of direct that question between who negotiates the terms and that would be the developer and the tenant.

CHAIRPERSON: Okay. Before we proceed to the close session I just want to understand do you, are you aware of the concept of a bankable lease and what is meant by a banker bankable lease?

MS JOUBERT: A banker bankable lease in terms of what [intervened]

MR KHUMALO: Lease, lease.

MS JOUBERT: Oh lease?

CHAIRPERSON: Lease, lease, a bankable lease.

MS JOUBERT: I mean I think what is important from a bank's perspective is that we just, for us we look at essential terms.

That being who is the landlord, who is the tenant, what is the actual rental that is being charged, where in the shopping centre are they located and fundamentally the only other important question that we look at from a bank's perspective is are there any extra clauses that we are concerned about.

I do not know if you have heard of this concept of extra clauses but just to give you a sense some, we see in some leases certain tenants will have provisions that there needs to be a certain percentage let up and if they do not let it up they can actually exit without there being any penalty.

You can understand from a bank's perspective we would be concerned with provisions like that and we do discuss that with our clients you know should those extra clauses not be appropriate.

That is what a bankable lease is, it is whether those essential terms work and are existent, more than that we do not look at, we do not ask for specific clauses to be included in leases.

MR KHUMALO: Okay just to follow up from what you said, why, why is it important for the bank where a particular tenants are located within the mall?

MS JOUBERT: It is important because if they are not located in the right spots, so let us assume you have a retail centre that is an L shape and you have your anchors which are now the draw cards, they draw, that is the reason why the people go and shop there, so they draw the people to the shops, if they are all located on the one side of the L and there are no draw cards on the other side of the centre most of the activity will happen on this side and there could be dead spots created on the other side of the, of the centre.

So from a sustainability perspective we would consider where they are located and that it will have an appropriate spread of consumers throughout the mall.

MR KHUMALO: So you are only concerned with the location of the draw cards not, not all tenants?

MS JOUBERT: No sir, we look at the placing of all tenants, it is just an example that I am giving.

So if you have all your anchors on the one side obviously you do not have the same pull then to the other side of the centre and that could jeopardise that side of the centre, but we will look at overall placing of the tenants to make sure that it is appropriate.

MR KHUMALO: Okay so in one of the examples that Mr Garret used is you mentioned the store that is, I am not sure of the terminology you used, again this should give you an indication of who we are when it comes to these bank terms, where you said I do not know if you fund it 70% and there is 30% equity can you explain what that example would look like?

CHAIRPERSON: 70, the 70% *be at* the 30% equity

MR KHUMALO: I accept you guys are a bit ahead of me when [laughing] but I would like to hear it from the experts.

MR GARRET: So what this means is if and again each centre would have a different level of gearing that we put on it and therefore different requirement for equity but let us assume that a centre costs 100 to build, if we are prepared to lend that developer R70 in debt he is going to need to produce R30 in equity to fund the completion of that development.

If we are only prepared to put in R50 he has to find R50 worth of equity, if we are prepared to give him R80 he is going to need to find the balance as equity, that is his, his equity that he injects into that centre.

MR KHUMALO: I think... I am, sorry I think I am seeing the whispers from my colleagues, they are wondering what these things mean like, I am asking you know, what is, what is gearing and what is equity right. So if you can explain it to a lay man what that means?

MR GARRET: Alright so it is, it is, let us assume we are working in rands, it is all rands, gearing is the amount of debt that a bank like ourselves is prepared to give to the developer for his particular asset and equity is the amount of rands that he has to come up with himself to inject into that, that centre, so if it is, so that, that is really what it is.

The gearing is debt coming from a financial institution like ourselves and equity is what he has to put in himself, his cash contribution or his contribution to that centre.

MR KHUMALO: I suppose this is then the right time to ask these questions, how does the bank determine the level of equity required by a client?

Maybe, maybe talk to the level of debt that can be supported by the retail property as well.

MR GARRET: *Ja*.

MS JOUBERT: Okay so the first question I am referring to question 19, the level and quality of a rental income for a retail property because that is important to actually get you obviously the level of debt.

So the level of rental is generally determined by the market whilst the quality of the rental income is determined by the profile and financial standing of the tenants.

The level of equity required by clients it is questions 19.2 and 3 are interlinked, the level of equity and the level of debt that can be supported by the retail property. So we will answer that as one.

In general we would need an equity injection in a transaction by the developer. When we think about the total cost of the development, so the R100 million that Gary was referring to, it is funded by the two components, debt and equity. The level of debt is determined by the level of cash flow which I have just referred to, the net rental generated by the retail centre which will service and repay our debt facility over that 10 to 12 year period so it kind of, will show you based on what the interest rate is today and what the return is or the net rental is up to what level you can, you can gear or up to what level you can provide debt to the client therefore the level of debt is structured around the level of cash flow generated by the centre.

So the net rental actually is a very important component to determine the debt level ultimately so that you can get repaid within that 10 to 12 year period and once you have determined the level of debt the level of equity is then the residual piece that the developer will actually inject into the development.

MR KHUMALO: Okay, and then you, you mentioned now the net rental.

MS JOUBERT: Yes.

MR KHUMALO: What, what, what other type of rental is there?

MS JOUBERT: No it is just a, so how you get to net rental it would be gross rental, so the, the basic rental payable by a tenant and that could just be a rate per square metre or it could be a combination of basic rental plus turnover rental as determined between the developer and the tenant and then there would be other smaller components you know like contributing to marketing campaigns, contributing to the rates and taxes so the operating costs components and that would give you the total gross rental income and then from that you will deduct the property related expenses and that would be the rates and taxes, the security, the cleaning, the normal stuff to get to your net rental and that net rental is what is left obviously to service the debt facility and that net rental kind of drives the level of debt.

MR KHUMALO: Okay. And if we, okay before maybe we go there. These components are calculated the same for similar type of developments regardless of where they are located?

MS JOUBERT: So the different retail offerings will generate different rentals, so and but the mechanics are exactly the same, there will be a gross rental dependent on the retail offering and then the expenses get you to the net rental and that net rental then determines then the level of debt.

MR KHUMALO: And the other considerations that you take as a bank are they also similar regardless of whether or not the development is in an urban area or a township area?

MS JOUBERT: *Ja* so we as set out initially do the, a similar assessment of every development taking the same factors into account. Obviously the circumstances can be different or every retail development is really different but we do the same level of, well same analysis.

MR KHUMALO: How big a factor is the location?

MS JOUBERT: So … *Ja* so can you maybe give a bit more clarity what you are after in terms of how important is locations?

MR KHUMALO: *Ja* so I mean the, say that everything else is, you know you are happy with the tenant mix, you are happy with the experience of the developer and professional team and he is just going to, he wants to build this big 30,000m² mall in Tembisa. How important is the location, I mean? Okay let me put it the way it is put there. What constitutes a sound location? And, sorry and is the answer the same or different given whether or not it is in a township, a rural area or the city?

MS JOUBERT: Sir it is actually, I am referring back to question 12, what constitutes a sound location for retail property development?

Primarily dependent on the supply and demand principle okay, so supply and demand in the market and the spending power of the target market.

So the demand and spending power are driven or determined by the consumers, the target markets that reside that in the area and the supply is driven by the existing and future proposed retail offering in the immediate area.

If the demand for a new specific retail offering outstrips supply then the location would be considered as sound location.

MR KHUMALO: So the answer is the same regardless whether it is in the city of a township?

MS JOUBERT: Yes we, we take into account the same factors and as we said initially the property fundamentals which includes location is one of the three categories, the main categories that we look at to answer your question.

CHAIRPERSON: Ms Joubert just to go back to that example you gave of an L shaped centre.

MS JOUBERT: Yes?

CHAIRPERSON: Let us say you then, as a bank have, you, you have satisfied yourself on the anchor tenant type that you have on the one end of the L and the other end of the L, you then said, what do you do with the rest of the tenant mix, what, what decision do you make in relation to the rest of the tenant mix or the tenants that are there other than these two once you are happy with the two tenants.

MS JOUBERT: Sure, so we will consider the tenancy schedule that is provided to us so the, the developer would normally have anchors and he will confirm in the funding pack that he is planning to put in food anchors and services, well let us assume it is a convenience centre, take-aways et cetera, and we will look at that to see is the mix correct for a convenient centre, that you do not have destinational centre, for example in a convenient centre.

So we will take that into consideration and if he does have names to kind of, like you mentioned before tick a box to say okay well it will include a pet shop for example that is fine we will review it, if it does not have, we will review, we will consider the tenant name but not as much detail goes into… because it is normally moms and pops at that level, so it is very difficult to do the same analysis in terms of financial standing and profile of the tenant.

We will just look at okay the make-up of the centre is going to be X, are we happy, does it compare favourably with other successful centres.

CHAIRPERSON: In doing that comparison you will therefore be looking at certain types of shop to [intervened]

MS JOUBERT: Jip correct.

CHAIRPERSON: Is it, is it the product or is it the name, or is it the actual operator who is operating that shop?

MS JOUBERT: The actual operator would probably not be identified at that stage yet because it would be the smaller, you know that is the infill part of the centre that will happen [intervened]

CHAIRPERSON: Let us say brand, would you be looking for a certain, specific brands?

MS JOUBERT: No that is what I am referring to so the brand as you referred to it will probably not be known at that stage because the, typically a developer will not bring your proposal showing 100% let centre.

They would want to fill the centre as they obviously go on, as they develop it, the centre. So it is not typically fully let by the time we get it, so we will look at the type of tenant and we will make sure that we are happy with the type of tenant and the mix of those tenants in the centre and that we are happy with that.

So we will consider it on that basis. Oh *ja* so, sorry so type of tenant would be so for a convenient centre we would expect food anchors to typically take out 25% of the centre, we will look at your take-aways, taking up a certain percentage, we will take at health and beauty taking up a certain percentage so that is kind of what we mean about, regarding type.

CHAIRPERSON: Type, okay.

MS JOUBERT: *Ja* not brand.

CHAIRPERSON: So you would not be looking for example a national operator, a national brand, a brand that is recognised nationally, would that [intervened]

MS JOUBERT: For the smaller tenants?

CHAIRPERSON: Amongst the smaller tenants other than the anchor tenants, when you look at that mix there what, what would satisfy, in satisfying yourselves as to that other mix, we are not talking anchor tenants anymore we are just talking about the rest of them.

MS JOUBERT: Okay, so we have to look at then what type of centre, because it is different each [intervened]

CHAIRPERSON: For each type of centre.

MS JOUBERT: Retail offering, so for a convenience centre you could in some instance only have one anchor and a lot of line shops, you do not need more than one anchor if it is a small centre, whereas if you have a regional mall you could have two to three to four anchors, you can even have sub-anchors, which could include fashion retailers et cetera and we would then take, into account those brands because if it is a large centre.

Let us assume it is a 30,000m² centre and the food anchors, only take up a third of it the sustainability of the income is obviously not going to be that strong so we will look at your sub anchors as well or your national tenants and who the developer has identified or who he has engaged to take up space.

CHAIRPERSON: Okay. You also mentioned that with, with regard to the anchor tenant you have a certain space allocation that you prefer that they take, say 25%?

MS JOUBERT: It is not our preferred space, it is a typical ratio that you see in the market for a convenient centre that they would typically take up 25%.

CHAIRPERSON: If it is less what happens?

MS JOUBERT: It is not prescribed by us so...

CHAIRPERSON: No, no, no, how does it affect your decision in funding that, that development if, if the anchor tenant is getting a lesser space, less than 25%?

MS JOUBERT: Ja so if we consider the anchor too small to really draw tenants to the centre, then we would rather not fund the development from that perspective.

CHAIRPERSON: Okay my last question on this, have you, have you experienced from a Standard Bank point of view and in this tenant, when you consider this tenant mix where you have an anchor tenant and then you have... and considering the size, have you come across a centre where there is a competitor of an anchor tenant that is offered significant size in a mall, in that centre or mall and have you, in your experience have you come across a pack that, that shows a competitor to an anchor tenant? Let us say, let us talk about that L shaped mall.

MS JOUBERT: *Ja*?

CHAIRPERSON: On one end of the L we have got an anchor tenant we are happy so you think there is a drawing card and on the other hand you have got your other drawing card.

MS JOUBERT: *Ja*?

CHAIRPERSON: A food outlet so there is a balance.

MS JOUBERT: *Ja* .

CHAIRPERSON: And then, what happens then if there is another player, big, a bigger player with a significant space, would that also satisfy you as the bank, would you be happy or would you be concerned that it detracts from the sales that these two anchor tenants will be making in that L shaped mall?

MS JOUBERT: It is a difficult one to answer because you are going to have to have specific details.

CHAIRPERSON: Okay.

MS JOUBERT: Does it strengthen the centre or does it weaken the centre? So I cannot tell you based on a hypothetical kind of two anchors and this one, does it complement it or does it strengthen it or does it weaken it? So it is on a deal by deal basis that we will analyse it.

CHAIRPERSON: Okay.

MS JOUBERT: But it is not uncommon for more than, to have one or two [intervened]

CHAIRPERSON: To have more than *ja*.

MS JOUBERT: Or three, you can have four anchors.

CHAIRPERSON: Okay.

MS JOUBERT: And if they could be in the same industry well [intervened]

CHAIRPERSON: *Ja*, no we, here with this question I am trying to understand where an anchor tenant imposes terms on that developer to allow its competitors to compare in size and I wanted to understand if [intervened]

MS JOUBERT: Oh.

CHAIRPERSON: If that has any bearing on the funding of the mall or is it just solely a decision of the anchor tenant that just wants competitors to be of that size.

MS JOUBERT: You are going to have to again direct that question to the developer, so by the time we get it the sizes and the retail [intervened]

CHAIRPERSON: Had already been allocated.

MS JOUBERT: Have already been laid out and most of the anchors would have been secured by then, so it is best you direct that to the parties that actually is, will be involved.

CHAIRPERSON: Okay. I think we can proceed to the closed session. Let me, can I just check? Okay we would like to now proceed to the close session.

I am not sure if you have got any members of the public, when we have a close session we will only allow members of Standard Bank or employees of Standard Bank to be part of this session as well as those of the commission and the transcribers and then we also request that any media streaming be cut off please for this coming session.

So can we then adjourn for 5 minutes just to allow for people to leave and to also the, to do the cutting off, of the media streaming?

[End of open session…]

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