



Relationship Banking

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The Competition Commission
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(See Form CC7 and Attachment)

By email: MawaboN@compcom.co.za / IanM@compcom.co.za / RuanM@compcom.co.za

Dear Mawabo

REQUEST FOR INFORMATION RELATING TO THE FRESH PRODUCE MARKET INQUIRY (CASE NUMBER: 2022APR0051)

We refer to the Competition Commission's (**Commission**) letter dated 23 June 2023 requesting information from Absa Group Limited (**Absa**) in relation to the market inquiry into the South African Fresh Produce Market. We thank the Commission for the time indulgence.

As we understand, the Fresh Produce Market Inquiry seeks to examine whether there are any features in the fresh produce value chain which lessen, prevent or distort the competitiveness of the South African fresh produce market and the Commission has identified Absa as a relevant stakeholder in the Inquiry. We set out below Absa's responses to each of the Commission's questions which have been repeated for ease of reference.

1. Provide a description of the role played by Absa in relation to the fresh produce sector. In your answer, indicate the process which emerging farmers need to go through to receive funding/ startup capital?

1.1. Absa is a fully-fledged commercial bank and provides financing in the agricultural sector. Absa does not have a dedicated focus on fresh produce and does not measure advances according to commodities. Accordingly, the responses and comments provided relate to general agricultural financing and not specifically to fresh produce.

1.2. [REDACTED]

financing and to repay the loan. Applicants are assisted and offered support by Absa's Agri-Specialists where a business plan requires improvement.

- 1.3. Once the business plan is presented [REDACTED]
bsa
considers the application and decides whether or not to approve the application.

2. Describe Absa's funding approach for emerging farmers in fresh produce farming operations and the difference in the approach, if any, when considering funding for established farmers for purposes of expanding their operations?

2.1.

2.2.

3. Explain in detail the criterion used for evaluating funding applications, in your answer indicate the type of security which farmers should have prior to being granted funding by Absa.

The following criteria are used to evaluate funding applications:

- 3.1. **Repayment ability** – The applicant must prove that the enterprise will generate enough income to cover all associated costs as well as to service the loan. Absa Agri Specialists are able to assist applicants with this process, using information that is provided by the applicant as well as industry norms, for example for yields and prices.
- 3.2. **Capacity of the owner or borrower to run the business** – The ability and capacity of the people in charge to run the business is assessed based on historical performance, for example, yield, quality, access to markets, income realised of agri-enterprises that they have managed previously.
- 3.3. **Security** – The type of loan dictates the security type that is applicable, for example:
- 3.3.1. for loans to acquire commercial assets, the asset is the security;
- 3.3.2. in the case of loans to acquire land, the covering mortgage bond is the security; and
- 3.3.3.
- 3.4. **Industry and/or economic environment** – Enterprises in industries that are performing well are considered favourably. Applicants have to demonstrate that they understand the strengths, weaknesses, opportunities and threats that are relevant to the relevant industry. They have to show how they exploit the strengths and opportunities and overcome the weaknesses and threats.

4. **From Absa's viewpoint what are the contributing factors to low level of access to finance by small-scale farmers/emerging farmers? In your answer, indicate what measures you think small-scale farmers/ emerging farmers can take to ensure that they attract the interest of commercial banks to fund their operations?**

The ability to produce a bankable application is key -

- 4.1. **Compiling audited financial statements:** audited financial statements which show historical performance of the enterprise is a challenge for most small scale or emerging farmers. Absa uses its ED funds as well as development funds provided by external providers to assist developing farmers with proper record keeping. Farmers and other SMEs are encouraged to utilise the [REDACTED] account, which is linked to a book-keeping programme so that they have the required financial records available and accessible when they need to apply for a finance.
 - 4.2. **Track record/capacity of management:** where possible, Absa uses ED funds to support capacity building. Absa also partners with corporate companies that offer enterprise and supplier development programmes to help develop farmers within these corporate companies' value chains and lends to such farmers on the strength of the technical support and access to market (offtake agreement).
 - 4.3. **Access to proper security:** where there is a shortfall on security, Absa may accept alternatives such as credit guarantee facilities. Refer to our response at 3.3.3 above.
 - 4.4. **Pricing:** Absa [REDACTED] offer subsidised prices to developing farmers.
 - 4.5. **Own-contribution:** where there is a business case, Absa may use ED funds to subsidise own contribution. The bank is currently engaging with the Department of Land Reform and Rural Development (**DALRRD**) on a Memorandum of Agreement (MOA) for the Blended Finance Scheme.
5. **What are the elements of the funding evaluation procedure used by Absa that mostly results in the rejection of emerging farmers applications? In your response, provide a list of at least 10 entities, whose applications were rejected due to the identified elements in the past five years.**

- 5.1. Applications are usually rejected for the following reasons:
 - 5.1.1. Greenfield enterprises where the applicant does not have farming experience.
 - 5.1.2. The level of required lending is too high with little experience.
 - 5.1.3. The applicant is listed with a credit bureau for outstanding bank debt.
 - 5.1.4. Lack of own contribution.
 - 5.1.5. Insufficient or no repayment ability, usually compounded with little experience.
 - 5.2. Refer to the excel spreadsheet marked **Annexure A** for a sample of entities, whose applications were rejected based on the failure to satisfy some of the criterion indicated at 5.1 above.
6. **Explain in detail Absa's viewpoint on the blended finance model recently launched by the Land Bank wherein a portion is grant and the other is interest bearing finance? In your answer, indicate whether this blended finance may facilitate access to finance by farmers, especially small-scale/ emerging farmers?**

Absa supports the blended finance model and is currently negotiating a Memorandum of Agreement with the DALRRD. The grant that is provided by the DALRRD would resolve some of the identified substantial weaknesses of applications from developing farmers, such as lack of own contribution (provided for in the 40-60% grant from DALRRD), technical assistance (provided in the provisions to support access to technical skills with the grant funding, where necessary), and security (provided for in the insurance grant).

7. From Absa's viewpoint, what are the challenges that are facing emerging farmers in South Africa and how do you think Absa can assist in ensuring that these challenges can be removed?

- 7.1. **Providing security for loans:** Most of the farmers are either leasing state land, or communal land with permission to occupy or land acquired through restitution programmes, which they cannot encumber as security. This makes it difficult for the farmers to access loans, particularly term loans. Absa uses credit guarantees where feasible.
- 7.2. **Own contribution:** Most developing farmers do not have any or enough savings to make the contribution that may be required for some loan facilities, for example, purchasing farms, farm machinery & equipment. Absa uses ED funding to subsidise clients' own contribution, however this pool of funding is limited and cannot cater for all needs. We hope to finalise the MOA with the DALRRD for the Blended Finance Scheme
- 7.3. **Access to reputable mentorship programmes:** As a consequence of limited experience and skills related to commercial agriculture farming, many developing farmers could benefit from mentorship programmes – farmers may not be able to access reputable programmes targeted at improving the necessary skills. Absa relies on ED programmes of corporate clients, with offtake agreements. These programmes often include a capacity building/mentorship programme.
- 7.4. **Pricing:** Commercial banks typically apply risk-based pricing models when evaluating applications for finance. Financing developing farmers is often considered a higher risk because of challenges such as limited history of optimal production, lack of security, etc. The high risk often attracts higher interest rates. Where a client is rated as high risk and qualifies for funding at high interest rates, Absa uses internal funding to subsidise the pricing that the client qualifies for.
- 7.5. **Access to markets:** This is compounded by a number of factors such as small volumes, which do not attract buyers, limited income and expertise which affects the ability to produce a quality crop. Other factors include the inability to use traceability systems, limited access to formal markets for products that do not meet aesthetic quality requirements of high value markets but are still edible (e.g. mottled fruits, irregular shaped fruits and vegetables).

8. Provide a full description of all funding instruments and financial support that Absa avails to the farmers operating in the fresh produce sector.

- 8.1. Absa is impartial to any agricultural commodities and offers its basket of products to qualifying applications. These products include the following:
- 8.1.1. overdraft facility for working capital.
- 8.1.2. term loans for the purchase of land and livestock. The tenor for the acquisition of land is [REDACTED] and the tenor for the acquisition of livestock [REDACTED], depending on the species; and
- 8.1.3. commercial asset finance for vehicles, machinery, equipment and other assets. The tenor in this category ranges [REDACTED] depending on the type of asset.

Financial support

- 8.2. **Consumer Financial Literacy training**, which is part of Absa's Socio-Economic Development programme in line with the B-BBEE codes of good practice. The training enables smallholder farmers [REDACTED] to learn how to manage their income, save and raise more money.
- 8.3. **Capacity development using ED Funding** – this includes training, mentorship, business coaching and other capability development activities to empower beneficiaries.
- 8.4. **Grant funding** from ED Funding which can subsidize part of a loan and cost of borrowing.
- 8.5. **Pricing concession** [REDACTED]
- 8.6. **Ability to link up with corporates** (such as mines, agro-processors and input suppliers) and partner with them in their enterprise and supplier development programmes.
- 8.7. **Use of credit guarantees** provided by third parties to de-risk Absa's lending to farmers and other clients, and thus open up access to funding.
- 8.8. We are seeking partnerships for blended finance with various institutions, including the DALRRD.
9. **Does Absa have policies/support mechanisms to assist SMEs and/or firms owned and controlled by historically disadvantaged persons? If yes, provide documentation which details the support provided. If no such documentation exists, please describe the nature of the support provided**

9.1. Absa has several programmes/products to support SMEs, and these include:

- 9.1.1. the Business Evolve account referred to above which is linked to a book-keeping platform in the background and enables SMEs and other clients to generate financial management information which is required at the loan application stage. [REDACTED]
- 9.1.2. at the height of the energy crisis, Absa set a renewable energy subsidy for SMEs, which could cover up to [REDACTED] of the cost of installing solar energy per client; and
- 9.1.3. Absa contributed extensively to the development of Agriculture and Agro-processing Master Plan (AAMP), which was led by DALRRD. The plan has holistic programmes for sector growth and transformation, including the Blended Finance Scheme.

10. **Has Absa undertaken, commissioned or is aware of any research that identifies the problems faced by SME/HDP farmers and provides policy recommendations on how to address these issues? If yes, kindly provide a list of the relevant research and copies of the reports.**

Issues pertaining to SMEs, including SME funding, are well researched and documented. Absa has not undertaken targeted research in this regard but uses available information to develop client value proposition for SMEs.

11. **From Absa's viewpoint, does the current design of funding models (funding markets and financial support), promote entry and economic participation of small-scale farmers? Briefly explain and provide evidence where applicable.**

As a bank, we endeavour to complement our funding model with solutions that cater for the developing sector, for example:

- 11.1. reliance on offtake agreements as mitigants for price risk;

16. In terms of development funding/finance, what is the uptake rate of small-scale farmers? Provide evidence where applicable.

Lending to the developing sector is increasing but uptake of bank loans is not a 100%. We estimate that the uptake is currently approximately [REDACTED] because developing farmers have other options of funding that may not cover the full production costs but are cheaper and less onerous for them (for example, government grants and enterprise development funding).

17. In Absa's view, is the cost of finance/funding prohibitive or discriminatory to small-scale farmers in any way? Briefly elaborate on your answer and provide evidence where applicable.

Pricing is allocated according to the risk. To determine the client's level of risk, banks apply a pricing risk model which is applicable to all clients. Higher risk attracts higher prices. Absa has a transformation facility [REDACTED] to subsidise pricing to developing farmers. We can also use Absa ED funds to enhance the application (through grants, pricing subsidy, etc.). However, this is a limited pool of funds servicing all sectors in which the bank finances.

18. What is Absa's view on small-scale farmer treatment by funding and financing institutions? Kindly provide evidence, if any.

Once a client approaches the bank, Absa assists where possible. We share information with developing farmers where possible on how to access available loans (i.e. during farmer information days and in industry publications and to farmers who approach the bank). Absa is inclusive in client engagement - developing farmers are also invited to webinars and functions to ensure that there is fair representation. Absa also offers training in financial literacy and business coaching to developing farmers.

19. Provide a list of all loans advanced to farmers operating in the fresh produce sector in the past 5 years. In your response, list the names of entities, loan amount, purpose and interest rate applicable. Kindly distinguish the loans advanced to small scale producers and commercial producers.

[REDACTED]

20. General comments

The fresh produce market extends beyond municipal markets and includes smaller and online markets that also cater for small scale producers, for example Freshling Direct, Freshling Markets and Khula! facilitate direct offtake arrangements. Some of these markets assist clients to manage some of the risk associated with fresh produce production and marketing and hence make it easier for banks to lend to farmers. As an example, offtake agreements guarantee a market and a price. Some offtakers and input suppliers may provide technical advice to producers to help them with farming practices. They may assist farmers to obtain the appropriate certification relevant to the markets that they supply (for example, local/global GAP), input procurement and controlled payment systems. The holistic support programmes are in their infancy but where they exist, they help to manage risk and thus enhance the chances of bank lending to developing farmers.

21. This letter contains confidential information and a Form CC 7 is accordingly attached.

Dr Langa Simela
Absa Group - Business Development Manager
(Unsigned due to electronic submission)