

**Residual Debt Services Limited (in curatorship)**  
**Statement by C Du Plessis, curator of Residual Debt Services Limited**  
**24 May 2018**

## Introduction

This is the fourth half yearly update by the curator following the successful implementation of the transaction on 4 April 2016, in accordance with an Offering Information Memorandum (“OIM”) issued on 4 February 2016. The OIM, inter alia, created a new bank (African Bank Limited) and transferred the core assets and business to African Bank Limited, which received an injection of R10 billion from its new parent, African Bank Holdings Limited (the “Transaction”).

The material liabilities of Residual Debt Services Limited (“RDS”) were exchanged, as part of the Transaction, for new instruments held in African Bank Limited, together with certain residual claims on the assets of RDS – “senior stub instruments” and “sub-ordinated stub instruments” and a partial cash settlement.

The reader is referred to the Transaction documents. Nothing in this statement should be considered to alter legal terms and conditions agreed to and detailed in the Transaction documents.

The aspects related to RDS covered in this statement are the following:

<b>Topic .....</b>	<b>Page No</b>
<b>Unaudited Condensed Interim Financial Statements as at 31 March 2018 .....</b>	<b>2</b>
<b>SARB indemnity guarantee .....</b>	<b>2</b>
Claims against the indemnity .....	2
<b>Asset recoveries .....</b>	<b>3</b>
<b>Valuation of stub instruments .....</b>	<b>3</b>
Scenario 1: Full claim against the indemnity reserve .....	4
Scenario 2: No claim against the indemnity reserve .....	5
<b>NCR and legal proceedings.....</b>	<b>6</b>
<b>SARS related matters.....</b>	<b>7</b>
<b>Conference call.....</b>	<b>7</b>
<b>Next Update.....</b>	<b>7</b>

C Du Plessis replaced T Winterboer as curator of RDS effective 1 April 2018. This follows T Winterboer’s resignation as curator effective 31 March 2018, who was appointed as curator of Residual Debt Services Limited ((the “Company”) previously named African Bank Limited (the “Bank”)) on 10 August 2014 by the then Minister of Finance of the Republic of South Africa and pursuant to the Banks Act No. 94 of 1990 (as amended) to manage the affairs of the Company subject to the supervision of the Registrar of Banks.

## Unaudited Condensed Interim Financial Statements as at 31 March 2018

At the time of this statement, the unaudited condensed interim financial statements of RDS have been issued for the six months ended 31 March 2018.

Highlights include:

- Cash on hand totalling R3 994 million (FY2017: R3 675 million) consisting of an operational cash float of R500 million, indemnity reserve of R3 000 million and surplus cash of R494 million (which includes accrued interest on cash investments totalling R137 million);
- Assets at 31 March 2018 of R4 715 million, with unsubordinated liabilities of R5 338 million (including the senior stub instruments of R5 144 million), and subordinated liabilities of R4 606 million representing the contractual value of the subordinated stub instruments, resulting in negative equity of R5 229 million;
- A loss from operations of R27 million (H1 2017 loss from operations of R450 million); and
- Credit Impairment reversal of R604 million (H1 2017: R225 million).

The unaudited condensed interim financial statements for the six months ended 31 March 2018 can be accessed on [www.residualdebtsservices.co.za](http://www.residualdebtsservices.co.za).

### SARB indemnity guarantee

As part of the Transaction, RDS provided a R3 billion indemnity to African Bank Limited in respect of assets transferred, with such indemnity expiring on the 8<sup>th</sup> anniversary of the Transaction, effectively 4 April 2024. The South African Reserve Bank (the "SARB") provided to RDS a matching supporting guarantee for this indemnity, so that the indemnity could be honoured to the extent that RDS does not have sufficient funds to cover any claim arising.

Having settled the SARB Loan in September 2016, RDS built up an indemnity reserve which was fully funded to the value of R3 billion on 1 September 2017. Any excess free cash in addition to the operational cash float of R500 million will be utilised to make payments to the holders of the senior stub instrument according to the agreed cash flow waterfall.

### Claims against the indemnity

At the date of this statement, the curator has not received notice of any identified claim against the indemnity provided to African Bank Limited.

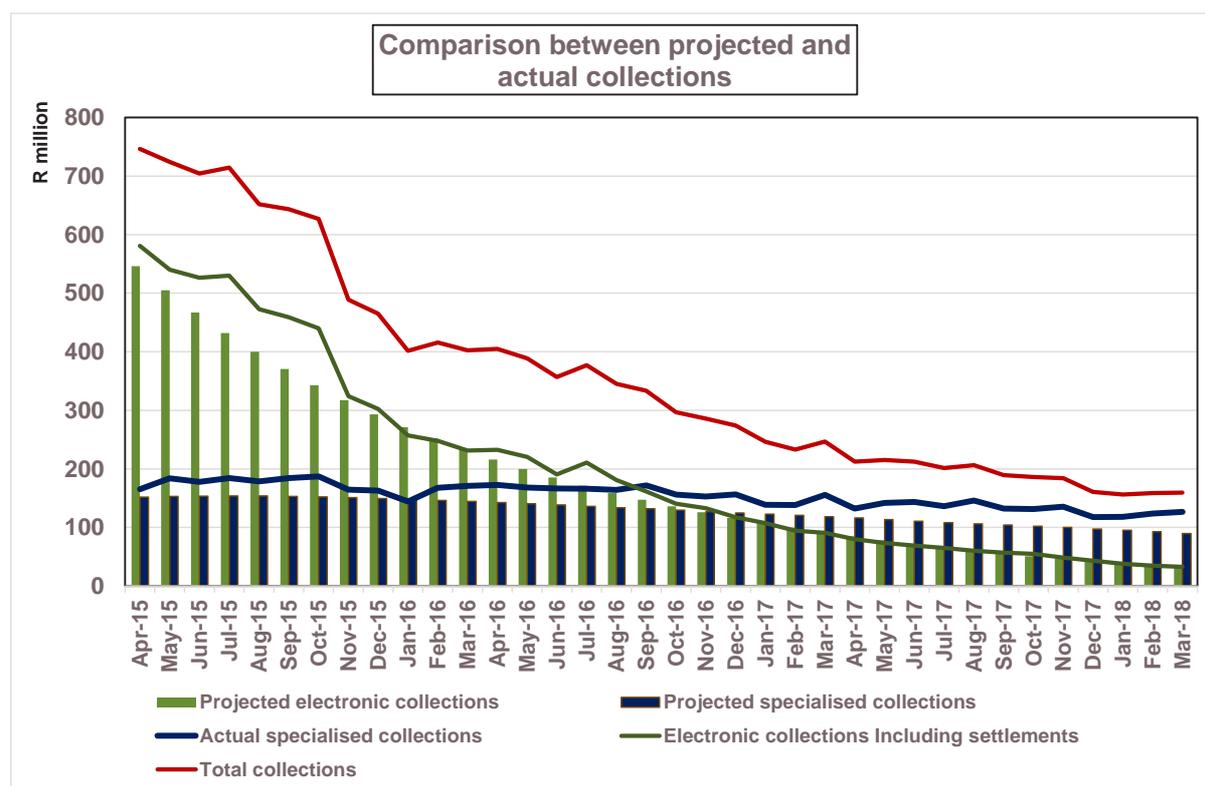
If, at the date of expiry of the indemnity (being 4 April 2024), no notice of claim has been received, then the reserve would be available to make payments to holders of the stub instruments according to the agreed cash flow waterfall.

## Asset recoveries

RDS continues to focus on recovery of the remaining assets held following the Transaction. The principal assets are loans made by RDS (prior to the commencement of curatorship) that were not transferred to African Bank Limited.

The monthly collections performance from 30 April 2015 to 31 March 2018 is presented below:

### Monthly collections – projected vs. actual (R million)



African Bank Limited is contracted to lead the recovery of such assets for which it charges a fee based on a service level agreement entered into between RDS and African Bank Limited. Additionally the curator has retained the services of another independent service provider to conduct an assessment to ensure that approaches to recoveries are optimised.

## Valuation of stub instruments

In estimating the fair value of liabilities, the Company made a number of assumptions that gave rise to a range of projected outcomes in respect of the SARB Indemnity.

Two scenarios together with the associated interest rate sensitivities are presented below. Under the first scenario it is assumed that there is a full claim against the indemnity reserve, while under the second scenario it is assumed that there is no claim against the indemnity reserve. In practice, it is possible that a combination of outcomes would materialise and that

these potential outcomes may be different from the ranges projected.

The expected future cash flows have been modelled based on the two scenarios. A discounted cash flow valuation has been applied to estimate the projected outcome under each of these scenarios.

### Scenario 1: Full claim on indemnity reserve

The key assumptions the Company has made in deriving the expected cash flows in this scenario are as follows:

- The expected cash flows derived from the remaining advances for a 60 month period;
- Using the expected cash flows derived from the remaining advances, application of the Distribution Waterfall are applied to the free cash flows;
- With regard to the indemnity reserve, it is assumed that 100% (R3 billion) will be utilised and paid out over a three year period;
- As the cash of R3 billion has built up to satisfy any potential indemnity reserve claim as detailed above, it is assumed that all surplus cash in excess of the R500 million operational float (to the nearest R50 million) is then paid to the holders of the senior stub instrument every 6 months. The first payment totaling R500 million was made on 29 January 2018, and it is anticipated that the next payment (of approximately R500 million) will be made in July 2018 and so on (based on forecasted surplus cash balances at the applicable points in time) until the end of the 60 months period mentioned above, when the operational float of R500 million will also be paid to the holders of the senior stub instrument;
- The model assumes that holders of the subordinated stub instrument will not receive any cash as the senior stub holders are not settled in full;
- An additional cash outflow totaling R200 million for potential future closure and associated costs is included; and
- The base case discount rate used to present value the expected future cash flows is 14.0% NACM; which represents a modified weighted average cost of capital (“WACC”) for the Company.

The table below illustrates the stub instruments’ fair values under *Scenario 1* as at 31 March 2018, together with the sensitivity if the discount rate is increased and decreased by 1%. In addition, the contractual carrying values of the stub instruments have been disclosed for completeness.

## Fair values and sensitivities overview (Scenario 1)

R million	31 March 2018			30 September 2017		
Stub instrument	Fair value @ 14.0% NACM	Fair value @ 15.0% NACM	Fair value @ 13.0% NACM	Fair value @ 14.0% NACM	Fair value @ 15.0% NACM	Fair value @ 13.0% NACM
Senior	2 606	2 550	2 664	2 820	2 760	2 882
Subordinated	Nil	Nil	Nil	Nil	Nil	Nil
<b>Contractual carrying values of stub instruments</b>						
Senior	5 144			5 380		
Subordinated	4 606			4 340		

## Scenario 2: No claim against the indemnity reserve

An additional sensitivity scenario has been presented where it is assumed that no amount is claimed against the indemnity reserve during the indemnity period, and thus the full R3 billion plus the operating float of R500 million is paid to holders of the senior stub instrument at the end of the indemnity period (being April 2024).

The key assumptions the Company has made in deriving the expected cash flows in this scenario are as follows:

- The expected cash flows derived from the remaining advances for a 60 month period;
- Using the expected cash flows derived from the remaining advances, application of the Distribution Waterfall are applied to the free cash flows;
- As the cash of R3 billion has built up to satisfy any potential indemnity reserve claim as detailed above, it is assumed that all surplus cash in excess of the R500 million operational float (to the nearest R50 million) is then paid to the holders of the senior stub instrument every 6 months. The first payment totaling R500 million was made on 29 January 2018, and it is anticipated that the next payment (of approximately R500 million) will be made in July 2018 and so on (based on forecasted surplus cash balances at the applicable points in time) until the end of the 60 months period mentioned above;
- The model assumes that holders of the subordinated stub instrument will not receive any cash as the senior stub holders are not settled in full;
- An additional cash outflow totaling R200 million for potential future closure and associated costs is included; and
- The base case discount rate used to present value the expected future cash flows is 14.0% NACM (which represents a modified WACC for the Company). However, the R3.5 billion cash flow mentioned above is not discounted using the WACC of 14.0% NACM, but is discounted using the 6 year risk free rate as at 31 March 2018 of 7.319% NACQ. This is

considered more appropriate as the full R3.5 billion has been collected to date and held on deposit with the major South African banks.

The table below illustrates the stub instruments' fair values under this *Scenario 2* as at 31 March 2018, together with the sensitivity if the discount rate is increased and decreased by 1%. In addition, the contractual carrying values of stub instruments have been disclosed for completeness.

### Fair values and sensitivities overview (Scenario 2)

R million	31 March 2018			30 September 2017		
Stub instrument	Fair value @ 14.0% NACM	Fair value @ 15.0% NACM	Fair value @ 13.0% NACM	Fair value @ 14.0% NACM	Fair value @ 15.0% NACM	Fair value @ 13.0% NACM
Senior	5 159	5 097	5 222	5 308	5 238	5 381
Subordinated	Nil	Nil	Nil	Nil	Nil	Nil
<b>Contractual carrying values of stub instruments</b>						
Senior	5 144			5 380		
Subordinated	4 606			4 340		

### Fair value summary

A substantial recovery for holders of the senior stub instrument is expected, albeit that the timing of payments and quantum will be reliant on future performance of recoveries and the extent of any claims against the indemnity reserve.

No payment to holders of the subordinated stub instrument is expected.

No distributions to the shareholder of RDS (being African Phoenix Investments Limited - previously known as African Bank Investments Limited) is expected.

### NCR and legal proceedings

The NCR had announced an investigation into certain activities of the Company prior to curatorship, focussed on reckless lending allegations. The Company co-operated fully with the NCR, whose review has been concluded.

An independent audit firm appointed by the NCR found that 2.61% or 19 285 credit agreements of a total population of 738 483 credit agreements were identified as having negative affordability in respect of their interpretation of the National Credit Act. These credit agreements were granted prior to the issuance of the affordability assessment regulations which came into effect in 2015.

The outstanding balances in respect of these credit agreements have been consequently written off by RDS. The 19 285 credit agreements that were affected resulted a financial write off of R730 million and a simultaneous release of the impairments provision amounting to R663 million. The overall impact was a R67 million loss for the Company. All credit bureaus have been requested to amend the records of the individuals concerned. The effect of the write offs means that RDS will not collect on them.

There are currently no material ongoing legal proceedings.

If a liability were to arise from any legal proceedings, such claims would rank *pari passu* with claims by the holders of the senior stub instruments.

### SARS related matters

RDS has open tax matters with SARS which primarily relate to the deductibility of historical impairments provisions. Due to the uncertainty relating to this matter, no deferred tax asset or liability has been raised in the financial statements.

### Conference call

A conference call is being held today at 12h00 SAST. Interested parties are requested to pre-register for this conference call at <https://goo.gl/v8DSUX> and follow the instructions provided. The call is being recorded and will be available via the company website [www.residualdebtservices.co.za](http://www.residualdebtservices.co.za) on 25 May 2018.

### Next Update

It is expected that the audited annual financial statements for the year ended 30 September 2018 and a further update will be provided by the curator in November 2018.

ENDS