

# An analysis of finance as a barrier to entry and expansion for emerging farmers

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Paper presented at the Biennial Conference of the Economic Society of South Africa (ESSA)

Johannesburg, South Africa, 3-5 September 2019

## Abstract

This is the first paper of a series of research papers that examines the barriers to entry and expansion facing emerging farmers in the South African agricultural sector. The significant barriers to entry and expansion that this series examines include access to finance, inputs and infrastructure and routes to market. This paper focuses on the barriers to accessing finance by emerging farmers in the agricultural sector. The paper provides an overview of the funding landscape and the different forms of funding provided by the South African government, Development Finance Institutions (DFIs) and the Land and Agricultural Development Bank to emerging farmers. The paper examines the mandate of these institutions as well as the funding requirements and the use of incumbent intermediaries in the funding models. The trends of financing are also analysed to determine if the funding allocation is where it is needed. The authors observe that most of the funding is directed to commercial farmers and therefore the funding initiatives examined are not reaching emerging farmers. Recommendations are made to facilitate the entry and participation of emerging farmers in the agricultural sector.

**Keywords:** barriers to entry, emerging farmers, development finance, Land Bank, Department of Agriculture, Forestry and Fisheries.

**JEL classification codes:** Q13, Q14, Q28.

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## 1. Background

- 1.1. The National Development Plan (NDP) of 2011 reflects that after 1994 one of the main challenges for rural development has been to combat marginalisation of the poor. This required changes to facilitate access to resources such as land, water and skills as well as rural infrastructure. The NDP further recognises agriculture as one of the critical enablers to significantly grow the South African economy and for job creation.<sup>4</sup> The statistics show that the agricultural sector plays a significant role in contributing to the country's gross domestic product (GDP). For example, in the second quarter of 2017, agriculture was recorded to be the most significant contributor to GDP growth by 33.6% (seasonally adjusted and annualised) when compared to other industries. This economic contribution assisted South Africa in recovering from a recession during that period.<sup>5</sup>
- 1.2. With job creation, the sector is one of the biggest employers in the economy as it is more labour-intensive than other sectors.<sup>6</sup> The sector is also vital for food security.<sup>7</sup> The food security concerns are as a result of an increasing population, the gradual decrease of the world's natural resources and the consequences of climate change.<sup>8</sup> The agricultural sector also plays a prominent role in the economy not only for primary production but, for instance, estimates state that about 60% of agricultural output is used as intermediate inputs by various other sectors of the economy. This statistic indicates how important the sector is as an engine of growth for the rest of the economy.<sup>9</sup>
- 1.3. In light of this, the persistent high concentration in the agricultural sector remains a concern. This notwithstanding the regulatory interventions of breaking up cartels and imposing significant administrative penalties, some prosecution of abuse of dominance cases and vigorous merger regulation.
- 1.4. Engagement with various black and emerging farmers took place to understand the challenges they faced in participating in the agricultural sector. The authors engaged the African Farmers Association of South Africa (AFASA) and the National African Farmers Union (NAFU)

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<sup>4</sup> National Development Plan 2030, pg. 44. Accessed from: [https://www.gov.za/sites/default/files/NDP-2030-Our-future-make-it-work\\_r.pdf](https://www.gov.za/sites/default/files/NDP-2030-Our-future-make-it-work_r.pdf) last accessed on 09 October 2018. State of the Nation Address. 2018. Accessed from: <https://www.gov.za/speeches/president-cyril-ramaphosa-2018-state-nation-address-16-feb-2018-0000> last accessed on 09 October 2018.

<sup>5</sup> Statistics South Africa 'Agriculture and finance help lift SA out of recession.' Accessed from: <http://www.statssa.gov.za/?p=10426> last accessed on 09 October 2018.

<sup>6</sup> Farmers' Weekly (2016) "Agriculture is still creating employment in SA". Accessed from: <https://www.farmersweekly.co.za/agri-news/south-africa/agriculture-is-still-creating-employment-in-sa/> last accessed on 30 September 2018.

<sup>7</sup> Grain SA (2015) "A look at the contribution of the agricultural sector to the South African economy." Accessed from: <https://www.grainsa.co.za/a-look-at-the-contribution-of-the-agricultural-sector-to-the-south-african-economy> last accessed on 11 October 2018.

<sup>8</sup> Department of Agriculture, Forestry and Fisheries, accessed from: [https://www.daff.gov.za/doaDev/topMenu/StratPlan2011\\_12to2014\\_15.pdf](https://www.daff.gov.za/doaDev/topMenu/StratPlan2011_12to2014_15.pdf) last accessed on 7 October 2018.

<sup>9</sup> The Land Bank. Corporate Plan FY2019 – FY2021.

respectively and engaged some farmers on a one-on-one basis. Following these engagements, it was apparent that there are several barriers to entry and expansion facing black and emerging farmers in the agricultural sector.

1.5. Below is an outline of how this paper is structured and the themes to be covered under each section.

1.6. **Section 2** provides an overview of the agricultural sector in South Africa. **Section 3** introduces the research problem and lays out the problems as identified by stakeholders which the research will seek to test. **Section 4** will set out the research methodology used. **Section 5** discusses the funding landscape in the agricultural sector. This includes a review of the history, current development funding institutions (DFIs) and other funding initiatives and programmes by DAFF such as Micro Agricultural Financial Institutions of South Africa (MAFISA). **Section 6** analyses the trends of financing from the DFIs and DAFF's agricultural funding programmes. **Section 7** provides the authors observations on the barriers to entry and expansion identified. **Section 8** will provide a conclusion on the findings of the research project.

## 2. An overview of the agricultural sector in South Africa

2.1. The agricultural sector (primary production) can be classified into two main categories, namely, subsistence and market-orientated agriculture. Within the broad categorisation of market-orientated agriculture, there are various scales of farming, namely; small, medium-sized and large/mega farming. This research focuses on the market-orientated farmers. The different scales of farming vary as to the size(s) of participating farms, the share of farmers' land that is devoted to the crop, the extent of participation (number of farmers), the percentage of total farming population and the presence of rival contractors and/or markets, as well as the annual turnover.<sup>10</sup>

2.2. The research draws the definitions of different categories of farmers or producers from the Department of Agriculture, Forestry and Fisheries' (DAFF) draft National Policy on Comprehensive Producer Development Support, published for public comment on 30 May 2018.<sup>11</sup> The policy indicates that it will be the overall national policy for the agriculture, forestry and fisheries sector in South Africa that will regulate and guide interventions to various categories of producers by the government, such as accessing finance, land ownership, access

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<sup>10</sup> Smalley, R. 2013. "Plantations, Contract Farming and Commercial Farming Areas in Africa: A Comparative Review," pg. 10. Accessed from: [https://www.plaas.org.za/sites/default/files/publicationspdf/FAC\\_Working\\_Paper\\_055.pdf](https://www.plaas.org.za/sites/default/files/publicationspdf/FAC_Working_Paper_055.pdf) last accessed on 11 October 2018.

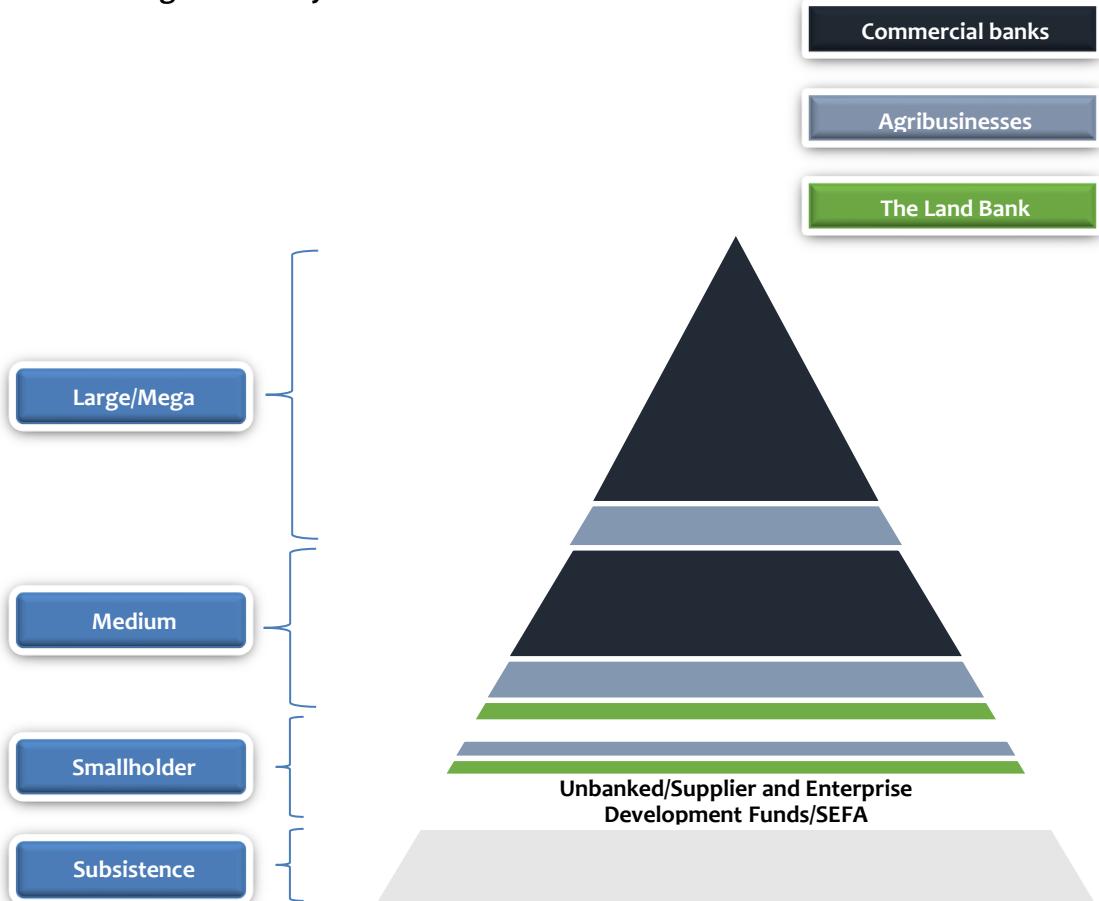
<sup>11</sup> Department of Agriculture, Forestry and Fisheries 2018. "National Policy on Comprehensive Producer Development Support: Draft 5 ver. 3", pg. vi-vii. Accessible at [https://www.daff.gov.za/docs/media/Draft%205%20ver%203%20Policy%20on%20CPDS\\_30May2018\\_accepted%20change.pdf](https://www.daff.gov.za/docs/media/Draft%205%20ver%203%20Policy%20on%20CPDS_30May2018_accepted%20change.pdf), last accessed on 4 March 2019.

to water resources, access to markets and compliance with market standards. The policy document differentiates between four categories of farmers, namely; household producer (subsistence farmer), smallholder producer/farmer, medium scale producer/farmer and large scale commercial producer/farmer.

2.3. There appears to be some level of alignment among industry players in terms of the categorisation of farmers. The Land and Agricultural Development Bank (the Land Bank) and the Bureau for Food and Agricultural Policy (BFAP) use a similar categorisation of farmers.

2.4. **Figure 1** below provides a schematic representation of the different farmer categories.<sup>12</sup> It is notable that the pyramid also depicts a representation of the number of farmers in each category. It is evident from **Figure 1** that there are less (in number, not value) of large-scale farmers as compared to subsistence farmers.

**Figure 1: Farmer Categorisation Pyramid**



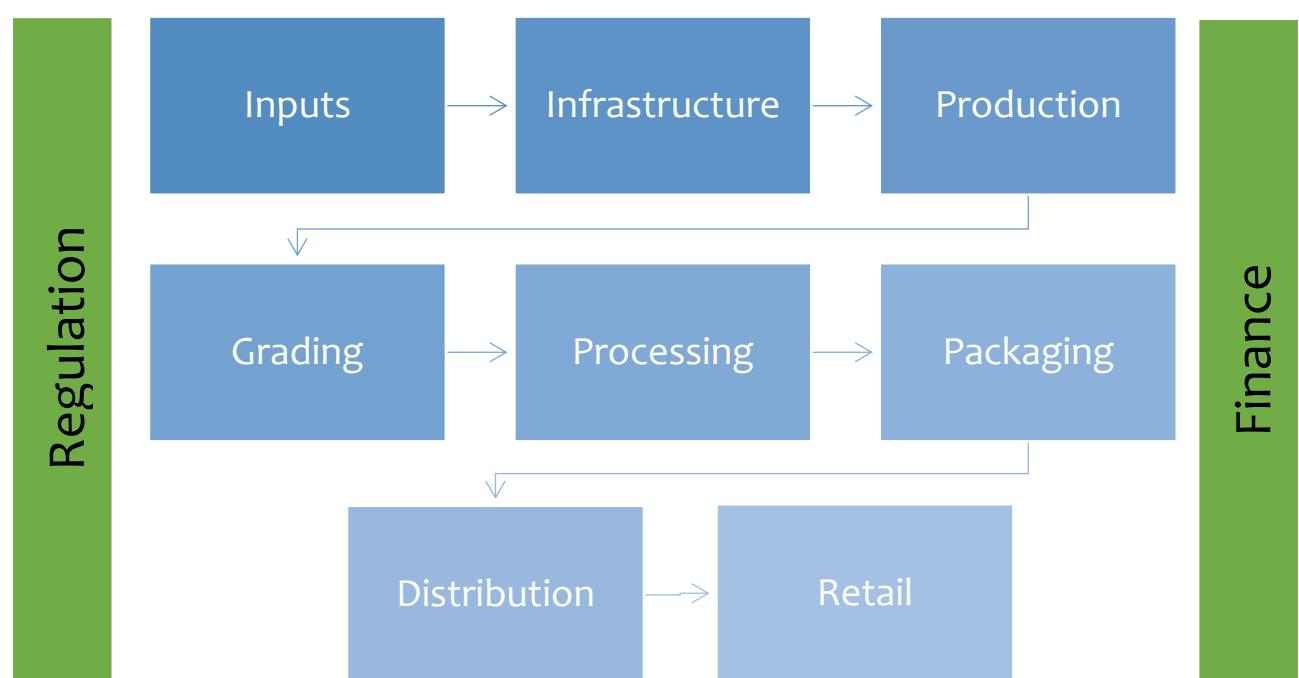
Source: The Land Bank's submission to the Commission dated 26 November 2018.

<sup>12</sup> Also refer to the BFAP potential architecture of a redesigned land reform and producer support framework, BFAP Baseline Agricultural Outlook 2018 – 2027 at page 13, accessible at <http://www.bfap.co.za/wp-content/uploads/2018/08/BFAPBaseline-2018.pdf> last accessed on 12 November 2018.

2.5. The review of the literature reveals a distinction between the commercial sector (represented mostly by medium and large farmers) and emerging sector (represented by smallholder and subsistence farmers) in terms of farmland hectares. For example, the total agricultural land in South Africa is about 93.5 million hectares.<sup>13</sup> The commercial sector is made up of between 30 000 and 35 000 farming units which equate to nearly 68.5 million hectares of farmland, from which more than 90% of South Africa's agricultural primary goods are produced.<sup>14</sup> Meanwhile, the emerging sector is farming on approximately 25 million hectares, producing lower levels of the country's primary goods.<sup>15</sup>

2.6. The common factors in most market-orientated value chains in the sector are illustrated in **Figure 2** below.

**Figure 2: Market-orientated agricultural sector value chain**



Source: Authors compilation

<sup>13</sup> AgriSA National Audit of the transaction of agricultural land in South Africa from 1994 to 2016 <https://www.timeslive.co.za/news/south-africa/2017-11-01-land-reform-is-showing-progress-audit/> last accessed on 20 February 2019.

<sup>14</sup> Community Household Survey <https://www.statssa.gov.za/publications/03-01-05/03-01-052016.pdf> last accessed on 20 February 2019.

<sup>15</sup> AgriSA National Audit of the transaction of agricultural land in South Africa from 1994 to 2016 <https://www.timeslive.co.za/news/south-africa/2017-11-01-land-reform-is-showing-progress-audit/> last accessed on 20 February 2019.

2.7. As shown in **Figure 2**, access to finance is an essential factor of the value chain which enables participants to purchase essential inputs and infrastructure (e.g. machinery and land) necessary for the production process, grading, processing, packaging and distribution of their produce. Finance is also required where there are specific regulatory requirements (such as licencing and certification) which a participant must adhere to and these may differ from commodity to commodity. With this in mind, it is clear that any farming enterprise that wishes to enter and participate in the agricultural sector will need access to finance to compete effectively. This paper will thus examine if access to finance is more difficult for emerging farmers thus creating a barrier to entry and expansion for them.

### **3. The research problem**

- 3.1. Stakeholders, including the Land Bank have raised the same concern regarding the ability to obtain finance for emerging farmers in order to ensure their entry and participation in the South African agricultural sector. The competition authorities have over the years tried to address issues of access to finance for new entrants and smaller players by establishing several developmental funds as part of conditions attached to mergers and abuse of dominance cases and penalties imposed on firms involved in cartels. These development funds include the Agro-Processing Competitiveness Fund (APCF), the Massmart Supplier Development Fund (MSDF), the Coca-Cola Supplier Development Fund and the AB InBev Fund.
- 3.2. The impact assessments of some of these funds have revealed their positive effects in improving competitive outcomes in markets mainly through new market entry and expansion of existing smaller players. Notwithstanding the positive impact of the developmental funds introduced by the competition authorities in addressing market entry and concentration levels, it is evident that these interventions and remedies alone will not address the issue of persisting high concentration in this sector. Further, as this is the mandate of other stakeholders, it is important to understand how financing in the sector operates and what the challenges faced are. The research seeks to identify if the concerns raised are valid and if so how they can be overcome to ensure an efficient funding environment that will cater for more competition in the sector. The following aspects will be examined:

- i. Lending models of development finance institutions

DFIs like the Land Bank are criticised for adopting a purely profit-oriented approach and imposing strict criteria for successful loan approval. It is also claimed that the Land Bank is run akin to a commercial bank rather than a developmental bank.

There has also been an acknowledgement from stakeholders that the current agricultural funding system is not working optimally, as it involves different DFIs such as the Land Bank

and others which have different eligibility criteria for accessing funding and the funding amounts that are provided.

ii. Lifecycle and patient funding

Stakeholders have also raised an issue about the lack of lifecycle and patient funding. They have argued that while they obtain funding from DFIs and other programmes, this is ordinarily once-off funding.<sup>16</sup> Therefore, this is argued to be a barrier in the sense that, long-term investments are needed for some commodities before any returns are realised. Some instances will require constant capital investments, which emerging farmers will not have.

iii. Subsidised interest rates

According to stakeholders, the interest rates currently charged by DFIs such as the Land Bank is an obstacle and limitation for small businesses, as it increases running costs and overheads which impacts the financial sustainability of potential entrants in the market. For example, the fundamental problem for emerging farmers is that they borrow from DFIs to have capital and are expected to repay their loans on market-related interest rates, which sometimes results in them defaulting on their loans.

iv. Timeframes in the assessment of funding applications

Lengthy timeframes for the assessment of funding applications and the granting of funding are regarded as a significant challenge for SMMEs. Emerging farmers often require funding urgently and feel that the processes and turn-around times to access funding are long and too much information is requested from them.

Stakeholders have also critiqued the timeframes for the disbursement of funds by the DFIs, as the cycles in which funding is disbursed do not meet the needs of farmers. For example, a farmer will need funding to plant in February but will only receive funding in August.

v. The role of intermediaries

Stakeholders have further raised an issue regarding the role of intermediaries used by the Land Bank in influencing the funding made available to emerging farmers. The concerns raised relate to the fact that these intermediaries are more established players (e.g. mostly commercial farmers) competing with the emerging farmers. The allegation is that these intermediaries pursue their interests and may not necessarily be keen to provide adequate assistance to emerging farmers as they can potentially be their future competitors.

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<sup>16</sup> The Commission notes that the Land Bank's funding framework may include repeat approvals of funding applications.

vi. Views from the Land Bank

The Land Bank seems to confirm much of what the stakeholders have raised stating that access to finance is one of the main constraints in agriculture, particularly among new entrants. Constrained access to finance leads to limited production as producers and entrepreneurs are unable to acquire the necessary inputs for optimal production.

**Table 1** below summarises the issues raised by the Land Bank:

**Table 1: Barriers to access finance**

Activity	Constraint	Description
<b>Pre-investment/ Origination phase</b>	Inability to access suitable land for farming activities at an affordable cost and with secure tenure	<p>Constraints associated with available land:</p> <p><b>Private land:</b></p> <ul style="list-style-type: none"> <li>- cost often prohibitive</li> </ul> <p><b>Government land</b> through land reform programmes:</p> <ul style="list-style-type: none"> <li>- long process</li> <li>- beneficiary selection process not transparent</li> <li>- allocated land portions not necessarily suitable/adequate for farming intentions</li> <li>- cannot offer land as collateral</li> </ul> <p><b>Communal/tribal land:</b></p> <ul style="list-style-type: none"> <li>- allocated land portions not necessarily suitable/adequate for farming intentions</li> <li>- insecure tenure arrangements</li> <li>- cannot offer land as collateral</li> </ul>
<b>Structuring/Due diligence</b>	Inadequate business plans due to a lack of financial and technical farming knowledge, and no or limited track record	<ul style="list-style-type: none"> <li>- Prepared by consultants with little interest in the actual intentions of smallholder farmers; or</li> <li>- Prepared by farmers themselves with little knowledge of the content required by financial institutions</li> <li>- Unrealistic assumptions regarding both costs and income in the business plan</li> <li>- Misalignment in terms of the productive capacity of land to support domestic consumption versus commercial production requirements</li> <li>- Expected productive capacity often do not take into consideration the level of land degradation due to over-grazing and lack of investment in soil nutrition</li> <li>- Inadequate information to farmers on what they can offer to obtain finance and collateral</li> </ul>
<b>Financing</b>	Lack of own equity to invest in venture	<ul style="list-style-type: none"> <li>- Results in unacceptably high gearing ratios that equate to reckless lending and sets up the venture for failure</li> </ul>

Activity	Constraint	Description
		<ul style="list-style-type: none"> <li>- Agriculture cannot sustain high debt ratios due to the external risks related to climate/commodity prices, which must be factored into the operation</li> </ul>
	Lack of collateral	<ul style="list-style-type: none"> <li>- Sustainable DFIs and the Land Bank Act requires collateral and government, and communal land cannot be offered as collateral</li> <li>- Alternative sources of collateral such as equipment and livestock may be accepted but increase the cost of financing due to the limited value thereof</li> </ul>
	Unaffordable cost of finance/interest rates	The Land Bank raises money in the capital markets due to its funding model. Thus, it must lend at a rate that allows repayment of the funding and covers its operational costs to maintain financial sustainability. These interest rates cannot necessarily be carried by enterprises in the start-up phase and strain cash flows while the climate and business risks to the enterprise are high
<b>Post finance support</b>	Inadequate technical, managerial and/or operational experience	<p>The level of expertise of the farmers differs based on experience.</p> <p>Many smallholder farmers have solid technical skills, but little business skills.</p> <p>New-generation farmers who join the sector from a professional services background often have solid business skills, but few practical farming skills.</p> <p>However, commercialisation of smallholder farmers require both technical skills to meet higher standards from formal suppliers as well as business skills to manage the larger enterprise and formalise accounting, health and safety, labour and other practices.</p>
	Lack of access to formal markets	<p>Value-chain financing where farmers are included in strong value-chains offer several advantages including technical support and confirmed buyers of produce.</p> <p>Farmers are inevitably price-takers in the market, but lack of access to better-structured markets often result in waste and financial losses to smaller farmers.</p> <p>An alternative challenge is where smallholder farmers have strong access to informal markets but cannot use the arrangements to obtain finance.</p>
	Limited access to risk management tools such as insurance	Smallholder farmers cannot afford the premiums associated with crop insurance. South Africa is the only market globally where farmers carry the full cost of crop insurance premiums.

Activity	Constraint	Description
		As the risk increases to the insurer, both from climatic events and limited re-insurance capacity, premiums will continue to increase.
	Limited access to implements and equipment	Certain implements and equipment like tractors, harvesters require businesses to operate at a certain scale for the business to be able to carry the high capital costs. Smallholder farmers generally do not have the necessary scale and must, therefore, contract equipment. This creates dependencies for the farmer including availability at key times, the quality of the equipment. All of these may have a detrimental effect on the business.
<b>Monitoring</b>	Limited access to technology that improves risk management and productivity	The 4 <sup>th</sup> Industrial Revolution is providing many technological solutions that allow smallholder farmers to improve productivity through better monitoring of crop health, application of inputs.  However, the costs associated with these technologies are high, and smallholder farmers are often not aware of the possibilities due to lack of exposure.  Such solutions will also improve the risk to the bank and therefore improve the credit risk of the client if available and accessible.
	Limited ability to respond to regulatory compliance matters	Smallholder farmers are often unaware of regulatory compliance matters such as environmental and labour legislation.  Projects are delayed due to the unavailability of environmental impact assessments, water licenses and other certificates and permissions.  In some cases, farmers cannot afford the cost of compliance resulting in viable business plans being abandoned or reduced profitability as portions of projects cannot be implemented.

Source: The Land Bank's compilation dated 12 February 2019

#### 4. Research Methodology

4.1. The information contained in this paper was sourced through desktop research and by means of questionnaires and interviews with relevant stakeholders such as the Land Bank, DAFF, the Department of Rural Development and Land Reform (DRDLR), National Treasury, Department of Planning, Monitoring and Evaluation (DPME), BFAP,<sup>17</sup> the National Agricultural Marketing

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<sup>17</sup> BFAP is a non-profit organization that informs and supports decision making by stakeholders in the agro-food, fibre and beverages sectors of Africa. It provides research-based market and policy analysis. For further information on its mandate refer to the BFAP Baseline Agricultural Outlook 2018 – 2027, accessible at <http://www.bfap.co.za/wp-content/uploads/2018/08/BFAPBaseline-2018.pdf> last accessed on 12 November 2018.

Council, AgriSA, the Institute for Poverty, Land and Agrarian Studies (PLAAS), the Institute for Market Agents of South Africa (IMASA), the South African Local Government Association (SALGA), and the Agricultural Research Council (ARC). In this context, the authors are conducting this research to expose the barriers further and to bolster efforts from industry players to address them.

## 5. The Funding Landscape

### 5.1. Pre-deregulation of the Agricultural Sector

- 5.1.1. The Marketing Act No. 26 of 1937 established marketing boards with extensive powers to regulate the production and marketing of agricultural products. Other vital institutions were the Land Bank that channelled much of the finance to farmers in the sector, co-operatives that acted as agents for the Land Bank and the marketing boards as suppliers of inputs to farmers. The Land Bank was established in 1912 as the primary lender to the agricultural sector. The Land Bank took over the assets and liabilities of some colonial the Land Banks and was subsequently funded through a combination of low-interest loans from the government, direct appropriations, deposits and reinvestment of its profits. In the 1950s, the Agricultural Credit Board (ACB) was established to give loans to farmers who could not access credit from commercial banks.<sup>18</sup> The ACB and the Land Bank provided financial assistance to farmers at subsidised interest rates and on preferential terms.
- 5.1.2. The marketing boards had powers to determine which individuals could produce, handle, process and trade agricultural commodities and at what price.<sup>19</sup> They were the sole buyers from producers and the sole sellers for processing. The co-operatives were central to this process. The co-operatives received agricultural produce delivered by farmers, graded the produce and paid out the delivery price and despatched it to the buyer.<sup>20</sup> The co-operatives would then claim back the amount they had paid out to farmers, including the cost of financing. These input supply co-operatives became effective regional monopolies, which enabled them to become the preferred suppliers of credit to farmers. Another reason for the expansion of the number of co-operatives was the cheap source of finance from the Land Bank. The co-operatives generally used the Land Bank as their source of funds. This was because, in the past, the Land Bank

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<sup>18</sup> Refer to <http://www.nda.agric.za/docs/Policy/policy98.htm> last accessed on 14 November 2018.

<sup>19</sup> The marketing system was characterized by state control, concentrated ownership and the exclusion of black and smallholder farmers. Policy Brief No. 2 31 March 2000 ‘Should the Competition Commission be concerned about the agricultural sector in South Africa?’ at page 3.

<sup>20</sup> Ibid at page 2.

obtained low-interest loans from the government which it then on-lent to the co-operatives.

### **5.2. Deregulation of the agricultural sector**

- 5.2.1. In 1994, the government ushered in a new era of policy changes. In the same year, South Africa ratified the Marrakesh Agreement, which for the first time, brought international trade in agricultural products under the World Trade Organisation.<sup>21</sup> The main objectives of the agreement were to increase market access and to lower export subsidies. These regulatory changes impacted on the structure and performance of the sector, thus presenting a complex set of interrelated issues that form the subject of this research series.
- 5.2.2. The government realised that, agricultural industries had to improve their productivity to become competitive internationally. Farming enterprises had to change their emphasis on international trade. Hence, the emphasis moved from production towards marketing and organisation of the value chain.<sup>22</sup> In order to achieve this, the government introduced several structural changes during the latter half of the 1990s.
- 5.2.3. Changes took place in terms of labour legislation, marketing arrangements and government support. Most notable of these was the promulgation of the Agricultural Product Marketing Act No. 47 of 1996 which changed the face of marketing of agricultural products in South Africa.<sup>23</sup> It made provision for the establishment of the National Agricultural Marketing Council (NAMC).<sup>24</sup> The main objectives of this legislation were to place less of a burden on government finances, achieve more efficient use of agricultural resources, increase market access for smallholder farmers to become internationally competitive, promote efficiency in the marketing of agricultural products and optimise export profitability.<sup>25</sup>
- 5.2.4. While marketing used to be the function of the marketing control boards, it became the responsibility of producers and agribusiness to manage the marketing of their products. Thus, producers were to have companies bidding for their produce. All price support measures under the control boards were abolished. Role players currently must

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<sup>21</sup> The Chair in International Agricultural Marketing & Development Competition Issues in the South African Agricultural Sector (2001) at page 1. It imposed new disciplines on the domestic agricultural policies of member countries, including South Africa aimed to create a level playing field for international trade in agricultural products by improving market access, reduced domestic support and a lowering of export subsidies.

<sup>22</sup> Ibid at page i.

<sup>23</sup> Ibid at pages 1 and 12.

<sup>24</sup> Ibid.

<sup>25</sup> Ibid at page 13. Policy Brief No. 2 31 March 2000 ‘Should the Competition Commission be concerned about the agricultural sector in South Africa?’ at page 3. Griffiths, A ‘The Domestic Politics of Agricultural Trade Policy Making in South Africa’ (2003).

compete in the market to realise a price that would make their operations sustainable and profitable.

- 5.2.5. In 1970, there were about 23 control boards administering the various schemes under the Marketing Act of 1968, but with the promulgation of the Agricultural Product Marketing Act of 1996, this reduced to 14 boards, which were eventually phased out.<sup>26</sup> NAMC was tasked to manage the phasing out process. Some of the boards had assets at the time of closure, which were transferred to industry trusts.<sup>27</sup> After deregulation, some large-scale producers established voluntary co-operatives to facilitate their access to capital, silos for storage and to continue with the marketing of their products.
- 5.2.6. Before deregulation, agricultural credit was a significant policy instrument. Agricultural policy was characterised by extensive government subsidies to farmers, usually in the form of drought aid and other disaster payments, as well as industry subsidies to, amongst others, the wheat, maize and dairy industries.<sup>28</sup> The deregulation process had wide-ranging implications for agriculture in South Africa, including significant changes in the level of direct subsidies paid to farmers by the South African government before deregulation.<sup>29</sup> With deregulation, commercial banks were able to expand their share for the provision of financial products in the sector.
- 5.2.7. At the turn of the century, the co-operatives were not a significant force in agriculture.<sup>30</sup> The ACB was closed in 1999, and following its closure, the private finance sector increased its lending role with capacity largely directed to commercial farmers.<sup>31</sup> This followed the establishment of the Presidential Commission on Rural Financial Services Chaired by Mr CB Strauss in 1996 (Strauss Commission).<sup>32</sup> The Strauss Commission was a committee which was appointed to investigate the state of funding farmers in the

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<sup>26</sup> This included the Deciduous Fruit Board, Citrus Board, Canning Fruit Board, Dried Fruit Board, Wool Board, Meat Board, Milk Board, Lucerne Seed Board, Maize Board, Mohair Board, Oilseeds Board, Sorghum Board, Wheat Board and Cotton Board, among others. Ibid at page 14.

<sup>27</sup> Ibid.

<sup>28</sup> MF Viljoen ‘South African Agricultural Policy 1994 to 2004: Some reflections (March 2005) at page 3 accessible at <https://core.ac.uk/download/pdf/6551113.pdf> last accessed on 4 March 2019.

<sup>29</sup> The Chair in International Agricultural Marketing & Development Competition Issues in the South African Agricultural Sector (2001) at page 1. See <https://www.farmersweekly.co.za/tax-and-management/global-farming/farming-without-government-support/> and <https://pmg.org.za/committee-meeting/14884/> last accessed on 4 March 2019.

<sup>30</sup> For further information on the breakdown of agricultural debt see

<https://www.daff.gov.za/Daffweb3/Portals/o/Statistics%20and%20Economic%20Analysis/Statistical%20Information/Abstract%20018.pdf> last accessed on 14 February 2019.

<sup>31</sup> Qwabe, N ‘Lending to small-scale farmers in South Africa : A case for best practices in formal institutions’ (May 2014) University of Pretoria accessible at

[https://repository.up.ac.za/bitstream/handle/2263/43227/Qwabe\\_Lending\\_2014.pdf?sequence=1](https://repository.up.ac.za/bitstream/handle/2263/43227/Qwabe_Lending_2014.pdf?sequence=1) last accessed on 11 October 2018.

<sup>32</sup> The Chair in International Agricultural Marketing & Development Competition Issues in the South African Agricultural Sector (2001) at page 22.

rural areas and also to provide recommendations to the Land Bank following the change of government in 1994.<sup>33</sup> It made recommendations to improve rural financial services and that the state should assist the market for agricultural finance. The Strauss Commission uncovered both public and private lending institutions were orientated to fund largely commercial farmers and small-scale farmers remained underserved. The Strauss Commission recommended that the Land Bank configure itself to be the main lending agent in agriculture. Previously, it had seen the Land Bank's role as a significant development agent.<sup>34</sup>

- 5.2.8. Interest rate subsidies from the Land Bank were reduced because of monetary policy reforms, which re-orientated financial services to the market. Changes to the reserve requirements of the banking sector made it impossible for the Land Bank to continue subsidising farmers' interest rates. The use of interest rate policy by the South African Reserve Bank (SARB) led to a rise in interest rates to very high levels, which resulted in interest payments becoming the single largest cost of production in agriculture at that time. Another notable change because of deregulation is taxation. The sector had traditionally received differential tax treatment from the South African Revenue Service (SARS). It has been estimated that income tax concessions to farmers amounted to 70% of their theoretical tax bill from 1981 to 1984. In 1986, the tax treatment of agriculture changed, for example, by the extension in the period within which capital purchases could be written off from one to three years, thereby reducing the subsidy available to farmers.<sup>35</sup>

### **5.3. The current landscape for agricultural funding**

- 5.3.1. Since 1994, the South African government has implemented various funding initiatives targeted for the agricultural sector, through DAFF and other departments such as the Department of Trade and Industry (DTI), DRDLR and National Treasury, while overall agricultural policy remains the mandate of DAFF.
- 5.3.2. Over and above the Land Bank, the country has various other DFIs with clear mandates that are all targeted for economic transformation and job creation. They differ in terms of the weight of their financial resources and the nature and scale of the projects they

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<sup>33</sup> Mandisa Dlamini 'The Case of The Land Bank's Retail Emerging Markets (REM) Funding Model for Emerging Farmers' (December 2016) The Graduate School of Business UCT accessible at [https://open.uct.ac.za/bitstream/handle/11427/25096/thesis\\_com\\_2017\\_dlamini\\_mandisa.pdf?sequence=1](https://open.uct.ac.za/bitstream/handle/11427/25096/thesis_com_2017_dlamini_mandisa.pdf?sequence=1) last accessed on 24 October 2018 at page 14. The Report of the Strauss Commission is accessible at [https://www.ecsecc.org/documentrepository/informationcentre/rural\\_financial\\_services\\_commission.pdf](https://www.ecsecc.org/documentrepository/informationcentre/rural_financial_services_commission.pdf) last accessed on 23 November 2018.

<sup>34</sup> Ibid at 23.

<sup>35</sup> Vink N & Kirsten J 'Deregulation of agricultural marketing in South Africa: Lessons Learned' (2010).

finance. DFIs that provide financing to entrepreneurs and farmers engaged in the agricultural sector include the Industrial Development Corporation (IDC), The Development Bank of Southern Africa (DBSA), the National Empowerment Fund (NEF), and the Small Enterprise Finance Agency (SEFA). There are also other provincial and regional DFIs in the country.

- 5.3.3. There are also several non-governmental organisations, producer and other organisations and associations as well as private companies that have started funding initiatives in agriculture. The commercial banks (First National Bank, ABSA, Standard Bank and Nedbank) for instance are the main funders for agricultural finance. **Table 2** shows the various categories of funding initiatives in South Africa based on the type of funding provided to farmers

**Table 2: Examples of loan financing and grant funding institutions**

Type of institution	Institutions	Type of finance	Target recipient
Government	DAFF the DTI Jobs Fund, a National Treasury initiative DRDLR	Soft loan programmes such as MAFISA Grant funding such as the Comprehensive Agricultural Support Programme (CASP) and Agricultural Broad-Based Black Economic Empowerment (AgriBEE Fund)	Emerging farmers
Development Finance Institutions	The Land Bank IDC SEFA Provincial DFIs like Ithala Bank	Loan financing It is notable that the Land Bank can play the role of administrator of some grant funding	Emerging and commercial farmers
Commercial Banks	Absa FNB Nedbank Standard Bank	Loan financing Masiszane Fund <sup>36</sup> Limited grant financing through enterprise development programmes	Commercial farmers
Private sector input suppliers and produce buyers		Grants and loans through enterprise and supplier development programmes e.g. Old Mutual, RCL Foods, Massmart, VTB Group and AFGRI.	Emerging farmers

Source: Authors compilation

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<sup>36</sup> The Masiszane Fund is an Old Mutual initiative that was established in 2007 in consultation with the National Treasury of South Africa. For further information refer to <https://www.oldmutual.co.za/masiszane/about.html> last accessed on 14 February 2019.

#### **5.4. Government funding through grants and soft loans**

- 5.4.1. There are different funding requirements applied by loan financing, grant and concessional funding institutions. This is primarily because grant funding does not need to be repaid, is often once-off and therefore the risk of the transaction is minimal. The authors examined DAFF's funding criteria, for the AgriBEE fund and Comprehensive Agricultural Support Programme (CASP) which are grant initiatives. The standard prerequisites for funding observed include a clean credit record, FICA verification documents, a market/business plan, off-take agreements, undertakings from external suppliers for inputs, the applicant must be a South African citizen with a valid identity document and produce a certificate of incorporation for the legal entity to be funded.<sup>37</sup>
- 5.4.2. An applicant for grant funding from the AgriBEE fund must source the portion required from any funding source of its choice.<sup>38</sup> This is required to 'demonstrate the level of commitment from applicants'.<sup>39</sup> The management of the applicant entity must present proof that it is skilled in financial and project management before it can start to receive the funds from DAFF.<sup>40</sup> For equity deals, applicants may only be assisted to acquire up to 49% in the initial investment.<sup>41</sup> This is to ensure that there is a skills transfer over some time and that the business continues to be viable.<sup>42</sup> Applicants who are not directly involved in the sector in terms of farming, fishing and forestry activities are excluded.<sup>43</sup> The applicant must be directly involved in the commodity or industry where investment is sought and should have been operating for at least three consecutive years.<sup>44</sup> Proposals must be linked to the elements of the B-BBEE sector codes, and the entity must comply with BEE-rating and verification processes.<sup>45</sup> However, the maximum grant that each applicant can apply for is capped at R5 million, unless DAFF exercises its discretion and approves the application with a 20% own contribution.<sup>46</sup>
- 5.4.3. The CASP grant also targets smallholder farmers and small agribusinesses and farmers transitioning from subsistence to smallholder. The requirements for this programme

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<sup>37</sup> AgriBEE Fund Criteria For Funding at paragraphs 4.2, 4.3, 5.1.2, 5.1.3, 5.1.5, 5.1.6 and 6.2.

<sup>38</sup> Ibid at paragraph 6.8.

<sup>39</sup> Ibid at paragraph 6.6.

<sup>40</sup> Ibid at paragraph 7.2

<sup>41</sup> Ibid at paragraph 7.3.

<sup>42</sup> Ibid.

<sup>43</sup> Ibid.

<sup>44</sup> The AgriBEE Fund criteria and application form is accessible at <https://www.daff.gov.za/daffweb3/Resource-Centre> last accessed on 22 November 2018. Refer to page 4.5 of the AgriBEE Fund criteria for funding. This criteria applies to all applicants including those that wish to apply for new equity deals or start-up agro-processing activities.

<sup>45</sup> The applicant must be black and the project 100% black-owned. Ibid at paragraphs 5.1.11 and 6.1 on page 5.

<sup>46</sup> Ibid at paragraph 6.7 on page 6.

are that applicants must be South African citizens, from a historically disadvantaged group, provide proof of managerial and technical skills, access to land, security of tenure and access to water and electricity.<sup>47</sup>

- 5.4.4. Beyond the grant funding, DAFF had soft loan funding in the form of MAFISA which was introduced in 2004.<sup>48</sup> MAFISA's focus was on providing short to medium term production loans to historically disadvantaged smallholder farmers and small agribusinesses, with an annual turnover of less than R5 million.<sup>49</sup> Its maximum loan amount payable to each person is R500,000. The applicant can be an entity representing some individuals in which case each one could be entitled to R500,000. Collateral is required to access the loans that exceed R50 000.<sup>50</sup> However, loans valued up to R50 000 do not require collateral.
- 5.4.5. MAFISA's products and services are accessed through a network of institutions which are accredited by DAFF as retail intermediaries for MAFISA. This is intended to ensure the expansion of Small, Medium and Micro Enterprises (SMMEs). However, analysts have reported that DAFF faced challenges in terms of the implementation of the programme. Stakeholders confirmed that the MAFISA programme was cancelled in 2013 due to irregularities in how the funds were being allocated, among other reasons. In 2015, the DPME conducted an impact evaluation on MAFISA. The findings reveal that although MAFISA loans offered a positive incentive to attract new entrants into farming, the absence of on-site technical assistance and mentorship contribute to its challenges. Also, the extent to which it reached its target population (smallholder farmers) was limited.

## 5.5. *The Land Bank Model*

- 5.5.1. Understanding that there are other DFIs in the country, the analysis will focus primarily on the Land Bank as the only specialist DFI focused on agriculture. Since its inception in 1912, the Land Bank has undergone various phases of transformation. With the recommendations of the 1997 Strauss Commission's report, the Land Bank has a new

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<sup>47</sup> CASP and Illima/Letsema Flyer accessible at [http://www.gauteng.gov.za/Document%20Library/Agriculture%20and%20Rural%20Development/CASP%20and%20limma-Letsema\\_flyer.pdf](http://www.gauteng.gov.za/Document%20Library/Agriculture%20and%20Rural%20Development/CASP%20and%20limma-Letsema_flyer.pdf) last accessed on 22 November 2018.

<sup>48</sup> MAFISA is still providing finance to small players. For further information, see <http://www.daff.gov.za/daffweb3/Branches/Administration/Development-Finance> last accessed on 11 October 2018.

<sup>49</sup> MAFISA Information pamphlet 2016 at paragraphs 2,4 and 6., accessible at <http://www.daff.gov.za/doaDev/AgricDevFinance/MAFISA%20Flyer%202016.doc> last accessed on 22 November 2018.

<sup>50</sup> Ibid at paragraph 8.

mandate to deracialise the agricultural sector and bring on board farmers from previously marginalised groups.<sup>51</sup>

- 5.5.2. The Land Bank's objectives now flow from the Land and Agricultural Development Bank Act No. 15 of 2002 (The Land Bank Act) and are aligned with government policies and the country's socio-economic needs. Its broad mandate, as expressed in the Land Bank Act, covers 11 objectives.<sup>52</sup> These are the equitable ownership of agricultural land, in particular the increase of ownership of agricultural land by historically disadvantaged persons (HDIs), agrarian reform, land redistribution or development programmes aimed at HDIs, access to land for agricultural purposes, agricultural entrepreneurship, removal of the legacy of racial and gender discrimination in agriculture, enhancing productivity, profitability, investment and innovation, growth of the agricultural sector and better use of land, environmental sustainability of land and related natural resources, rural development and job creation, commercial agriculture and food security.
- 5.5.3. It is apparent that the Land Bank has classified its mandate into three themes; transformation, growth and integration.<sup>53</sup> The Land Bank does not receive any financial subsidy from the government; instead it receives its funds from the financial markets and guarantees from the National Treasury.<sup>54</sup> The State is its major shareholder.
- 5.5.4. The Land Bank has segmented its clients based on the turnover of their enterprises.<sup>55</sup> The model is based on the category or scale of the farmer concerned. For instance, the Land Bank handles mega-operators through its Corporate Banking and Structured Investments Unit. It has a transformation focus to facilitate the entry of black agri-entrepreneurs through the creation of equity investment structures.<sup>56</sup> This category of farmers is usually considered for credit as they meet the lending criteria required by the banks, such as a strong balance sheet which increases their ability to provide collateral for the capital they require and the management skills and technical expertise to operate their farming enterprise efficiently.

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<sup>51</sup> <https://www.nda.agric.za/doaDev/sideMenu/strategicPartnerships/Parastatals/LandBank/AboutLandBank.html> last accessed on 23 November 2018. See also the Preamble to the The Land Bank Act of 2002 which recognises its mandate to promote greater participation of historically disadvantaged persons and an increase in ownership of agricultural land by such persons.

<sup>52</sup> Preamble to the The Land Bank Act (2002).

<sup>53</sup> The Land Bank Income Investor Roadshow August 2018 Presentation accessible at

<https://www.landbank.co.za/Investor%20Presentations/Land%20Bank%20Roadshow%20August%202018.pdf> last accessed on 11 October 2018.

<sup>54</sup> Submissions from The Land Bank at a meeting held with the authors on 5 October 2018.

<sup>55</sup> Ibid.

<sup>56</sup> The Land Bank Presentation 2018 at page 20.

### **5.5.5. Steps in the Funding Process**

- 5.5.5.1. The first stage of the funding process is the application phase. After the application is received the process is followed by risk analysis and the allocation of funds by the Land Bank. The Land Bank offers the following products and services to the commercial farming sector: long-term loans, medium-term loans, short-term loans, guarantees, establishment loans, large livestock, instalment finance and special mortgage loans.<sup>57</sup> The funding must be repaid after a specific period.
- 5.5.5.2. To qualify for a loan from the Land Bank, farmers must meet specific criteria to demonstrate a sustainable agribusiness. The loan application and approval process include an assessment of creditworthiness, collateral requirements, authenticity checks, and property and asset evaluation and submission of a business plan indicating the financial viability and economic, social merits of the project or enterprise.<sup>58</sup> Further criteria include proof of assets or income and bank statements, cash repayment ability and the technical experience in agriculture development.<sup>59</sup>
- 5.5.5.3. Smallholder applicants must also demonstrate that they have secured off-take agreements. Without the necessary off-take agreements, the Land Bank views the transaction as riskier and thus would require a defined programme to cover the risk.<sup>60</sup> The Land Bank also considers a range of supply-side factors such as the technical support, business management skills and marketing capability of the farming enterprise. This is all required to determine if the funded business would be able to break even or earn profits and be sustainable.
- 5.5.5.4. The principles of sound credit applied are essentially the same across the different categories, but some of the requirements will be more onerous for emerging farmers to access loans. The Land Bank submits that it gives more risk tolerance to emerging farmers. The Land Bank further submits that its requirements are not as stringent as the commercial banks. It is, however, noted, that some of the commercial banks would already have credit facilities (such as a cheque account,

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<sup>57</sup> The Land Bank provides establishment loans to farmers for establishing perennial crops. These loans are typically used for establishing sugar cane plantations, citrus and deciduous fruit orchards, timber plantations and vineyards for table and wine grapes. This loan may be accessed by individual farmers, groups or any legal entity from large-scale commercial farms to small-scale farms. [For more information on these types of loans refer to https://www.fundingconnection.co.za/funding-agencies-in-south-africa/land-bank](https://www.fundingconnection.co.za/funding-agencies-in-south-africa/land-bank) last accessed on 4 March 2019.

<sup>58</sup> Submissions from The Land Bank at a meeting held with the authors on 5 October 2018.

<sup>59</sup> Qwabe, N ‘Lending to small-scale farmers in South Africa: A case for best practices in formal institutions’ (May 2014) University of Pretoria accessible at [https://repository.up.ac.za/bitstream/handle/2263/43227/Qwabe\\_Lending\\_2014.pdf?sequence=1](https://repository.up.ac.za/bitstream/handle/2263/43227/Qwabe_Lending_2014.pdf?sequence=1) last accessed on 11 October 2018.

<sup>60</sup> Submissions from The Land Bank at a meeting held with the authors on 5 October 2018.

mortgage) with the applicant so they can rely on this track record to make an assessment, on the other hand, the Land Bank does not have the same information.

5.5.5.5. The authors considered the funding criteria applied by the Land Bank to the various categories of farmers. In the large/mega category, farmers must have collateral in the form of a mortgage or other types of loans mentioned earlier, revolving credit facilities, equity investments, off-balance sheet facilities, inventory and trade finance, working capital and guarantees and insurance products to manage risks.<sup>61</sup> Medium-sized farmers must secure a mortgage and medium-term loans to acquire land, livestock and equipment. Smallholder farmers are also expected to hold a mortgage and medium-term loans to acquire land, livestock and equipment. **Table 3** depicts a comparison of some of the application requirements of the Land Bank applied to commercial farmers and emerging farmers, respectively.

**Table 3: The Land Bank's funding requirements for commercial and emerging farmers**

Requirement	Commercial Farmer	Emerging Farmer
Business plan	✓	✓
Bank statements	✓	✓
Solvent balance sheet	✓	✓
Deed of sale/offer to purchase land	✓	✓
Collateral/security	✓	✓ (if up to R2million)
Loan to value – farm	✓ (70% of market value)	✓ (90% of market value)
Loan to value – movables	✓	✓
Loan to value – production	✓ (70% of turnover)	✓ (80% of turnover)
Max debt ratio – long term loan	✓ (55%)	✓ (70%)
Max debt ratio – medium term loan	✓ (55%)	✓ (80%)
Max debt ratio – short term loan	✓ (55%)	✓ (100%)
Affordability test – surplus after assistance as a % of liabilities ( $\leq 2\%$ )	✓	✓
Experience	✓	✓ (mentorship)
Off-take agreements/market	✓	✓

<sup>61</sup> The Land Bank Presentation 2018 at page 22.

Input supplier	✓	✓
Water rights	✓	✓ (The Land Bank can facilitate processing with DWS)
Concessionary rates – special mortgage	n/a	✓ (Prime less 0.5%)
Risk analysis	✓	✓

Source: Authors compilation derived from information submitted by the Land Bank dated 21 November 2018.

5.5.6. **Table 3** reveals that there is not much differentiation in the funding requirements applied by the Land Bank to commercial and emerging farmers. The Land Bank is criticised for adopting a business-like approach in the strict criteria for successful loan appraisal, especially for emerging farmers.<sup>62</sup> However, according to the Land Bank, its mandate set out in the preamble of its enabling Act, involves a balancing act of allocating funds and the need to strengthen existing agricultural financial services. No doubt there are complexities in making these determinations including employment, stakeholder accountability and prudential management.

#### 5.5.7. The disbursement model to farmers – use of intermediaries

5.5.7.1. Farmers in the medium to large scale segments are predominately established primary agriculture, commercial farmers and are handled by the Land Bank's provincial offices and through its intermediaries. The Land Bank is currently working with eleven (11) intermediaries. Seven (7) intermediaries (Unigro, GroCapital, Suidwes, Obaro, GWK, Capital Harvest and Vincemus) are managed through a service level agreement, and ten (10) intermediaries form part of its lending book (Akwandze, BKB, Humarsdrop, GWK, Lona Citrus, Omnia, Sernick, TWK, VKB and Unigro).<sup>63</sup> Intermediaries manage fifty-three percent (53%) of the Land Bank's loan book.

5.5.7.2. Intermediaries are market participants in the agricultural value chain and are a channel through which the Land Bank extends the funding and technical support to emerging farmers. Most of these eleven (11) intermediaries are competing farmers and agribusinesses in the agricultural sector.

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<sup>62</sup> Submissions from The Land Bank at a meeting held with the authors on 5 October 2018.

<sup>63</sup> The Land Bank Presentation ‘Fixed Income Investor Roadshow’ (August 2018) at page 103,

<https://landbank.co.za/Investor%20Presentations/Land%20Bank%20Roadshow%20August%202018.pdf> last accessed on 7 March 2019.

**Table 4: Intermediary Activities**

Company	Group Activities
Unigro	Financial services, a subsidiary of Afgri (large player)
GroCapital	Financial services, a subsidiary of Afgri (large player)
Suidwes	Large player, a subsidiary of Africum
Obaro	Financial services, 10% BEE equity
GWK	Large producer in the agricultural sector
Capital Harvest	The largest fruit export group in South Africa
Vincemus	Transport contractors
Akwandze	financial services linked to National Treasury's Jobs Fund
BKB	Large producer in the agricultural sector
Humarsdrop	Not identified
Lona Citrus	A shareholder of 6 farming groups in SA
Omnia	Larger player, listed on the Johannesburg Stock Exchange
Sernick	Larger player,a diversified organization with its focus on agriculture and agricultural processing activities, including a Bonsmara stud, animal feed production, feedlot, red meat production (abattoir, de-boning and processing) as well as retail outlets.
TWK	Co-operative
VKB	Large Player, listed on the Johannesburg Stock Exchange

Source: Authors compilation

5.5.7.3. The technical aspects associated with farming and enterprise development support are taken care of by the intermediary while the Land Bank provides the funding solution. The intermediaries assist the Land Bank with the end-to-end lending process from loan origination, disbursement, monitoring, collection and legal recoveries. Intermediaries are paid a management fee for their services while risk and profit-sharing arrangements are specified in the service level agreement (SLA) they enter into with the Land Bank.<sup>64</sup> SLAs also outline the conditions of the intermediaries' contributions to the granting of Land Bank loans. All lending activities are governed by credit policies which are approved by the Land Bank.

#### 5.5.8. The focus on emerging farmers

5.5.8.1. The Land Bank submits that its transformation focus in the smallholder category is to support farmers to grow into medium and large commercial status, but it requires

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<sup>64</sup> Land Bank Integrated Annual Report 2018 at page 43 [http://pmg-assets.s3-website-eu-west-1.amazonaws.com/Land\\_Bank\\_Integrated\\_Annual\\_Report\\_20172018.pdf](http://pmg-assets.s3-website-eu-west-1.amazonaws.com/Land_Bank_Integrated_Annual_Report_20172018.pdf) last accessed on 19 March 2019.

grant funding to supplement its loan funding in order to provide adequate support to these farmers. It does not have the necessary funding to provide farmers with non-financial support such as training, access to inputs and access to markets.<sup>65</sup>

5.5.8.2. In 2012, the Land Bank launched its Retail Emerging Markets (REM) Unit in response to the findings of the Strauss Commission to determine the most appropriate funding model for emerging farmers. The REM Unit was established as a dedicated division to respond to challenges of financing emerging farmers. Thus, the Wholesale Financing Facility (WFF) model was developed, specifically tailored for emerging farmers. It is further split into two funding approaches, direct lending to individual farmers and the other aimed at farmer groups.<sup>66</sup> The Unit has since been consolidated within the Commercial Development and Business Banking unit of The Land Bank.

5.5.8.3. DAFF provided an R150 million wholesale financing support facility (R50 million from MAFISA and R100 million from DAFF) that was used to subsidise the lending rates to intermediaries and subsequently the emerging farmers and to cover the cost of supplying technical assistance to the farmers by the intermediaries.<sup>67</sup> The WFF Funding Model is reflected in **Figure 3** below.

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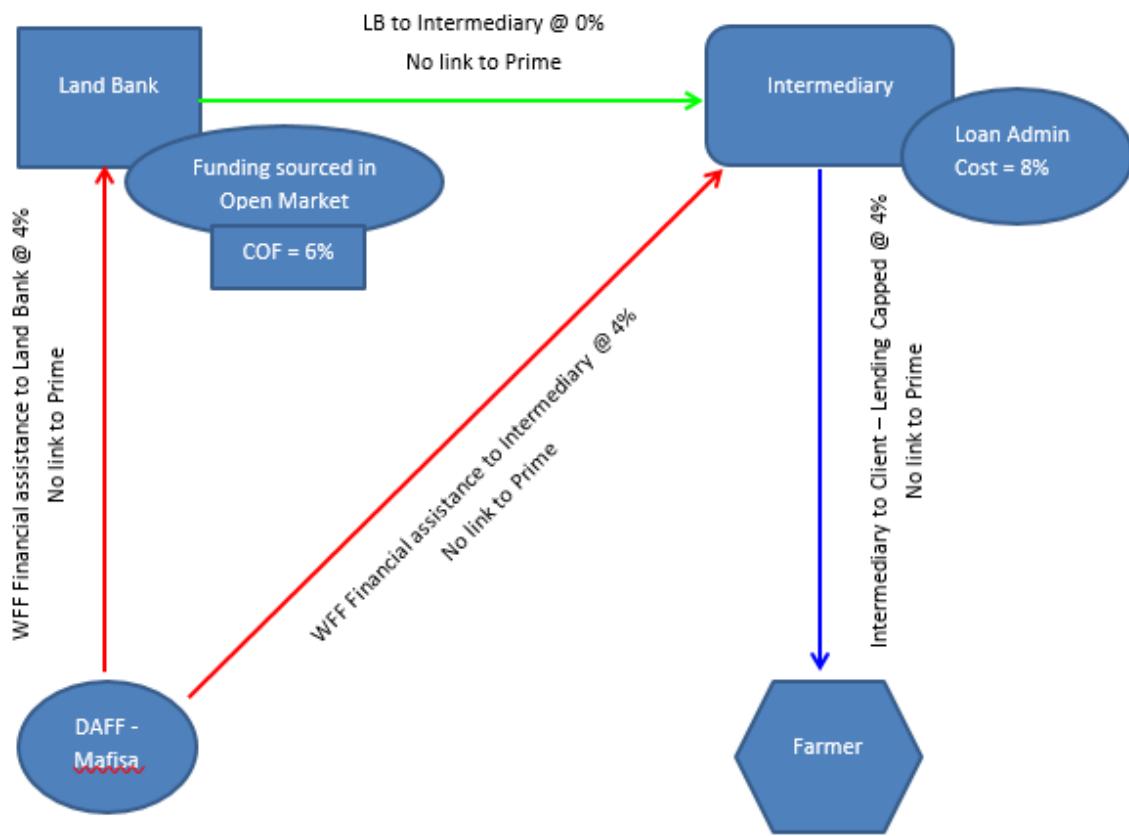
<sup>65</sup> Ibid at page 20.

<sup>66</sup> Mandisa Dlamini ‘The Case of The Land Bank’s Retail Emerging Markets (REM) Funding Model for Emerging Farmers’ (2016) The Graduate School of Business Cape Town at page 12. The author performed a quantitative analysis of the REM loan book to obtain a view of the growth of the book over time, the performance of the loans and repayment ability of the loans over time to assess if it provided value for emerging farmers. The quantitative analysis displayed that the portion of the REM loan book which consisted of non-performing loans was a small percentage, relative to the performance of the entire loan book. Furthermore, the REM loan book had increased sizeably since its inception, reaching out to a wider scope of emerging farmers. Overall, The Land Bank’s REM funding model was a success.

<sup>67</sup> The Land Bank Annual Report 2018 page 270 accessible at

<https://landbank.co.za/Shared%20Documents/Forms/DispForm.aspx?ID=16> last accessed on 7 March 2019.

**Figure 3: WFF Funding Model**



	Land Bank	Intermediary	Farmer	DAFF - <del>Mafisa</del>
<b>Income - Interest</b>	-	4%	-	-
<b>Income – Subsidy</b>	4%	4%	-	-
<b>Cost – Interest</b>	(6%)	-	(4%)	-
<b>Cost – Admin</b>	?	(8%)	-	-
<b>Cost – Subsidy</b>	-	-	-	(8%)
<b>Net Position</b>	(2%)	-	(4%)	(8%)

Source: The Land Bank's submission to the Commission dated 12 February 2019

5.5.8.4. Intermediaries used in this model would receive applications and determine whether the applicant qualifies and would work with the emerging farmer for a period of 5 to 7 years.<sup>68</sup> The implementation of the WFF model, in partnership with the intermediaries, included a scheme which presented the following value proposition: cash flow lending, concessionary interest rates and technical end-to-end farmer support and a market to which farmers could sell their produce.<sup>69</sup>

<sup>68</sup> Intermediaries generally have a target pool of emerging farmers to support, but farmers can approach the intermediaries directly. The Land Bank engages with emerging farmers through its provincial office network, and services the farmers directly or it puts them in touch with the intermediaries. Statement by Sydney Soundy, Farmers Weekly ‘Intermediary programmes can be helpful for emerging farmers’ (18 January 2017) <https://www.farmersweekly.co.za/agri-news/south-africa/intermediary-programmes-can-be-helpful-for-emerging-farmers/> last accessed on 7 March 2019.

<sup>69</sup> Ibid.

5.5.8.5. Funding was advanced to the intermediaries to subsidise the cost of the technical support provided to emerging farmers. Each intermediary and emerging farmer who participated in this model had to qualify with the credit terms and qualification criteria set out by the Land Bank. This type of funding model has a variety of products to suit the needs of the emerging farmer. Despite this, some of the Land Bank's requirements include access to owned or leased land and off-take agreements, which most emerging farmers do not have.<sup>70</sup>

5.5.8.6. Intermediaries used in the WFF model procured facilities and offered credit monitoring services on behalf of the Land Bank. According to the Land Bank, the intermediaries afforded the Bank with an opportunity to reach clients that it would not ordinarily reach.<sup>71</sup> This structure allowed it to reduce its non-performing loans and hold intermediaries accountable for its loan book quality.<sup>72</sup> Intermediaries were tasked to provide end-to-end business support to emerging farmers. Thus, through this model, emerging farmers would receive not only finance but also technical support and assistance to develop a range of skills which are suited to operating a sustainable and profitable farm.<sup>73</sup>

## 6. Analysis of Financing Trends

6.1. The aim of this section is, to present and analyse the trends of financing initiatives undertaken by the Land Bank and DAFF in the agricultural sector. This section reveals the findings from a time series analysis of the performance of some of their funding initiatives. This serves to highlight patterns associated with financing in the sector.

### 6.2. The Land Bank

6.2.1. **Figure 4** below demonstrates the trend analysis of the Land Bank's financing and loan book segmentation for commercial and transformation. The Land Bank defines transformation transactions as those undertaken by persons or entities that are wholly Black-owned (Black shareholding of 100%), majority Black-owned (Black shareholding of

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<sup>70</sup> Mandisa Dlamini 'The Case of The Land Bank's Retail Emerging Markets (REM) Funding Model for Emerging Farmers' (December 2016) The Graduate School of Business UCT accessible at [https://open.uct.ac.za/bitstream/handle/11427/25096/thesis\\_com\\_2017\\_dlamini\\_mandisa.pdf?sequence=1](https://open.uct.ac.za/bitstream/handle/11427/25096/thesis_com_2017_dlamini_mandisa.pdf?sequence=1) last accessed on 24 October 2018 at page 12 to 14.

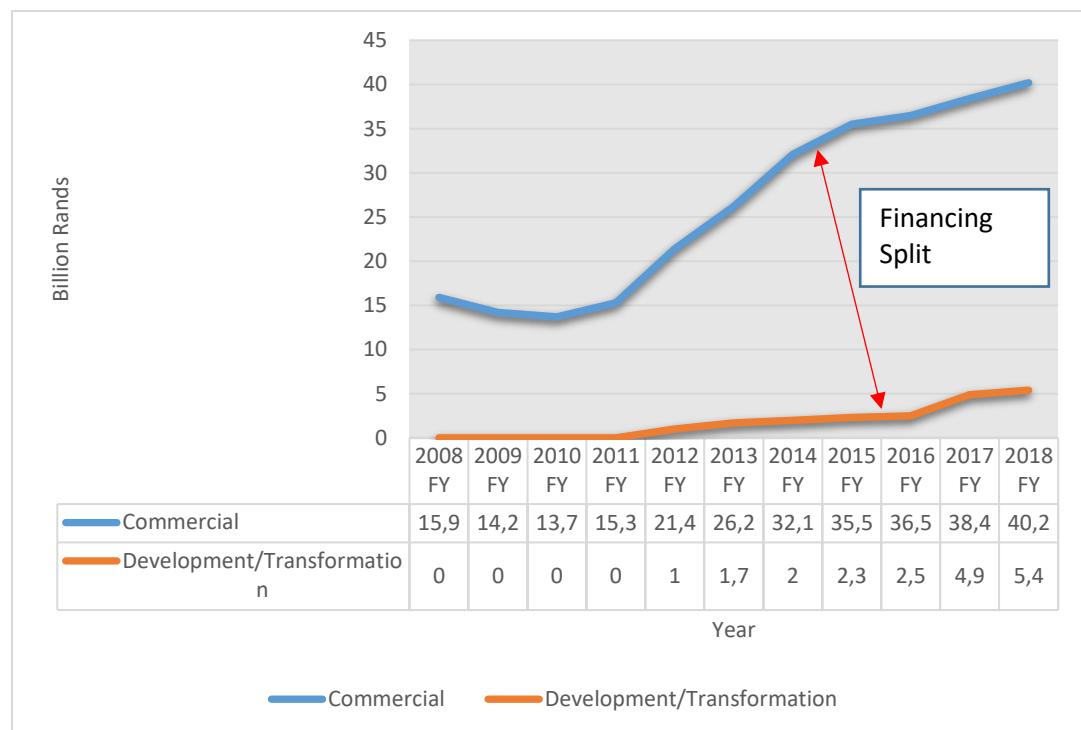
<sup>71</sup> The Land Bank Presentation 2018 at page 106.

<sup>72</sup> Ibid.

<sup>73</sup> Mandisa Dlamini 'The Case of The Land Bank's Retail Emerging Markets (REM) Funding Model for Emerging Farmers' (December 2016) The Graduate School of Business UCT accessible at [https://open.uct.ac.za/bitstream/handle/11427/25096/thesis\\_com\\_2017\\_dlamini\\_mandisa.pdf?sequence=1](https://open.uct.ac.za/bitstream/handle/11427/25096/thesis_com_2017_dlamini_mandisa.pdf?sequence=1) last accessed on 24 October 2018 at page 12 to 14.

51% or more) or substantially Black-owned (Black shareholding of between 30 and 50% and a BBBEE Level of 1 - 4).

**Figure 4: The Land Bank commercial vs. development/transformation financing (2008-2018)**



Source: The Land Bank (2018).<sup>74</sup>

- 6.2.2. **Figure 4**, shows the Land Bank's financing for the commercial sector compared to transformation during the period 2008 to 2018. According to **Figure 4**, it is evident that there has been a gradual increase in the Land Bank's lending from 2008 - 2018 on a year-on-year basis for both commercial and transformation. It also shows that the financing split for transformation and commercial sector is quite significant.
- 6.2.3. Although there has been an increase for the commercial sector and transformation from 2008 to 2018, it is notable that the financing split for transformation and commercial is narrowing at a slower rate. Therefore, for the Land Bank to be able to fulfil one of its objectives, namely; providing finance for emerging farmers in pursuit of the equitable ownership of land, agrarian reform and land distribution,<sup>75</sup> there has to be some form of significant convergence in the financing split for transformation and commercial sector over time.

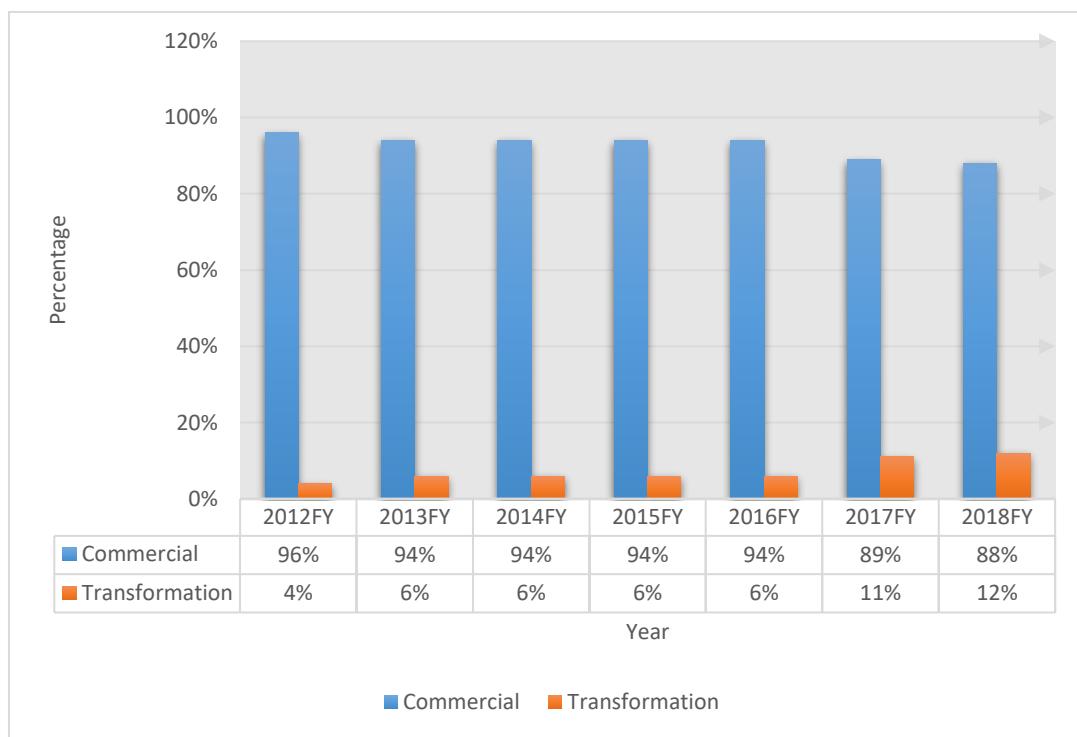
<sup>74</sup> Accessed from:

<https://landbank.co.za/Investor%20Presentations/Land%20Bank%20Financial%20Results%20Launch%20Presentation%2020082018%20consolidated%20final.pdf> last accessed on 15 November 2018.

<sup>75</sup> The Land Bank, accessed from: <https://landbank.co.za/Pages/Home.aspx> last accessed on 21 November 2018.

6.2.4. **Figure 5** below, depicts the percentages of the Land Bank's loan book segmentation during 2012 - 2018. It shows that there has been a gradual increase in the financing for transformation from 4% in 2012 to 12% in 2018. During 2013 and 2016, the yearly financing for transformation remained stagnant at 6%. **Figure 5** further illustrates that a more significant portion of the Land Bank's financing is directed towards the commercial sector, while a smaller portion is for transformation. This might be due to the Land Bank's lending model which is more on commercial terms and accounts for the risk of lending to emerging farmers who might default on their loans. Because the emerging farmer loans tend to be lower in value than commercial loans as the scale of operation is smaller, and thus a much larger number of loans will be required to balance this over time.

**Figure 5: The Land Bank's loan book segmentation (2008-2018)<sup>76</sup>**



Source: The Land Bank (2018).<sup>77</sup>

6.2.5. **Figure 6** below, demonstrates the Land Bank's subsidised lending under the WFF lending facility, which targets emerging farmers. According to **Figure 6**, it is evident that there has been a sustained increase in the WFF gross loans from 2012 to 2018. In this regard, there was an increase from R101.7 million in 2012 to R967.2 million in 2018. Although there was an increase in the gross loans under the WFF facility over a

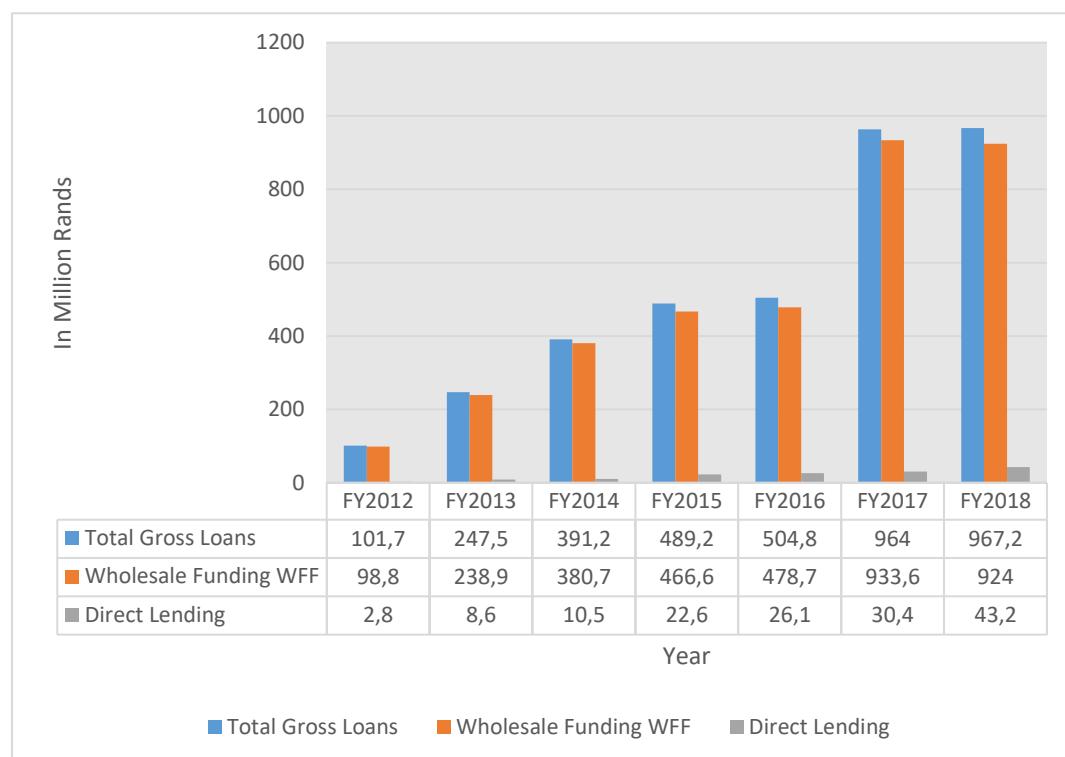
<sup>76</sup> It should be noted that data for transformation for the preceding years was unavailable or not reported.

<sup>77</sup> Accessed from

<https://landbank.co.za/Investor%20Presentations/Land%20Bank%20Financial%20Results%20Launch%20Presentation%2020082018%20consolidated%20final.pdf> last accessed on 15 November 2018.

sustained period, it is notable that a bulk of the funding was from the Land Bank, as DAFF's total contribution to the WFF is R150 million received between 2011 and 2016. It has been estimated that if the Land Bank receives an annual allocation of R100 million from the government, an additional investment of R1 billion of loans per annum to smallholder farmers can be subsidised at prime interest rate minus 2.5%.<sup>78</sup> This shows that in the absence of funding from government and other sources, the Land Bank's financial support to the emerging sector will be limited.

**Figure 6: The Land Bank's Wholesale Financing Facility (WFF) lending 2012-2018**



Source: The Land Bank (2018).<sup>79</sup>

### 6.3. Government funding through DAFF

- 6.3.1. The Land Bank also acts as the administrator and manager of the AgriBEE fund, which means that the Land Bank can only distribute funds to recipients based on DAFF's instruction. As previously mentioned, the purpose of the AgriBEE fund is to support small, medium and micro enterprises within the sector who wish to acquire a shareholding in existing commercially viable and sustainable enterprises, and to

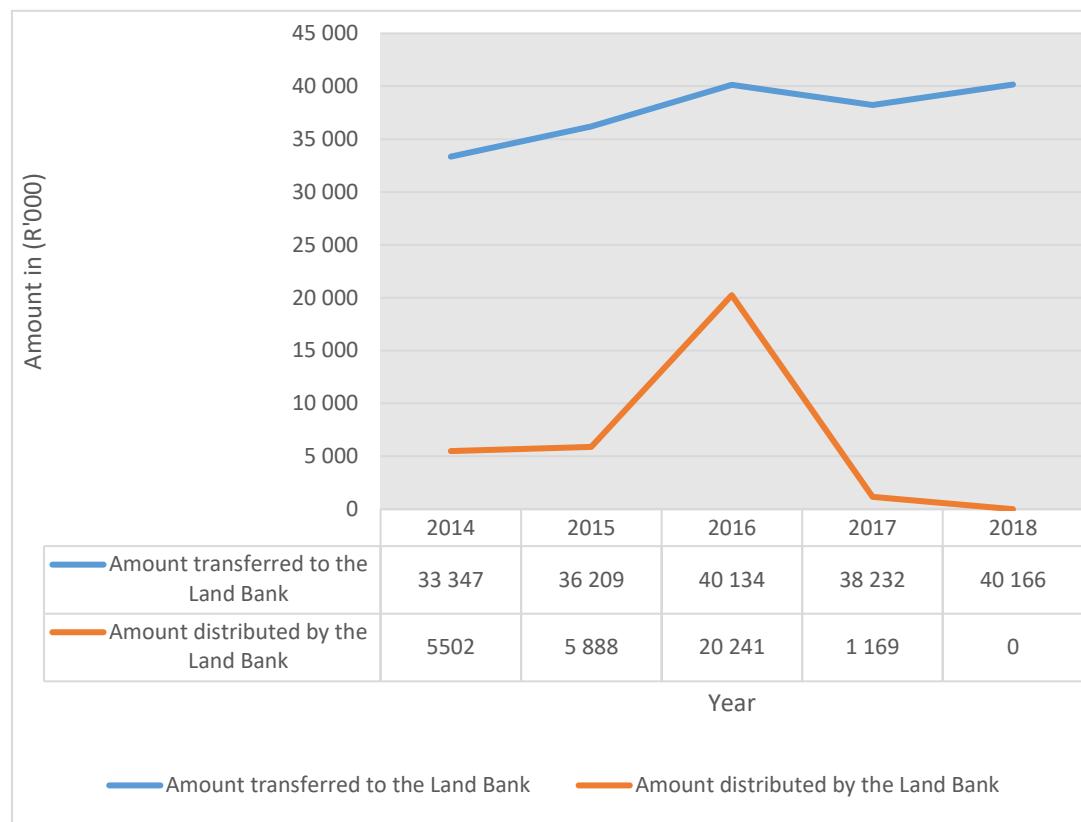
<sup>78</sup> The Land Bank Integrated Annual Report 2018 accessed from [http://pmg-assets.s3-website-eu-west-1.amazonaws.com/Land\\_Bank\\_Integrated\\_Annual\\_Report\\_20172018.pdf](http://pmg-assets.s3-website-eu-west-1.amazonaws.com/Land_Bank_Integrated_Annual_Report_20172018.pdf) last accessed on 18 February 2019.

<sup>79</sup> The Land Bank Fixed Income Investor Roadshow Presentation (August 2018) pg. 30.

advance enterprise development through agro-processing and value-adding activities to previously marginalised people who could not participate in the sector value chain.<sup>80</sup>

- 6.3.2. **Figure 7** shows a trend analysis of the DAFF funding allocation for the AgriBEE fund and the amount disbursed by DAFF under this fund.

**Figure 7: DAFF funding allocation for the AgriBEE fund and amount distributed by the Land Bank (2014-2018)<sup>81</sup>**



Source: Authors compilation from information obtained in the Land Bank's various annual reports (2014:176; 2015:175; 2016:195; 2017:187; 2018:268)

- 6.3.3. **Figure 7** demonstrates that there has been a gradual increase in the amount allocated to the AgriBEE fund during 2014-2018. For example, the amount transferred to the Land Bank increased from R33 347 000 in 2014 to R40 166 000 in 2018. **Figure 7** also shows that there was a decline in the amount disbursed by the Land Bank in 2016 and 2017. Although the research notes the difficulty in setting targets, such as no prior knowledge of how many funding applications would be lodged in a particular year, **Figure 7** reveals a funding surplus during 2014-2018 as the amount transferred to the Land Bank by DAFF, is not proportional to the amount disbursed by the Land Bank. This raises the question

<sup>80</sup> Accessed from <https://www.nda.agric.za/doaDev/sideMenu/AgroProcessingSupport/docs/Criteria%20for%20funding%20%20AgriBEE%20Fund.pdf> on 12 November 2018.

<sup>81</sup> It should be noted that data for the amount disbursed during the 2018 financial year was not recorded and therefore reflected as "0".

of whether there is appropriate planning by DAFF to identify relevant emerging farmers that can be funded in each year or whether such planning will always fail given the unknown factors.

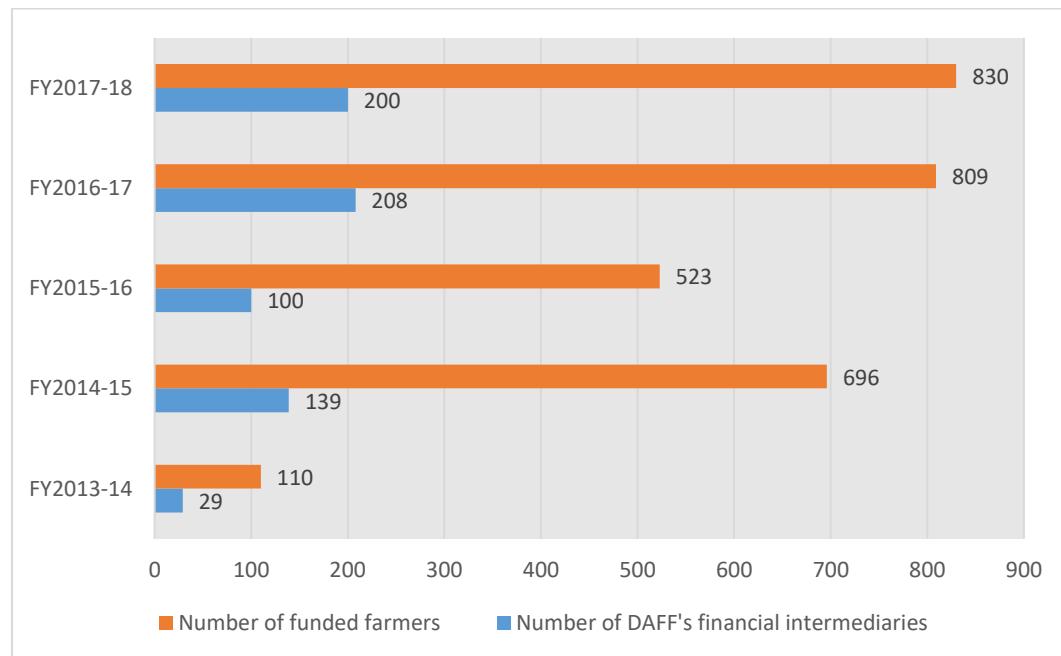
- 6.3.4. Furthermore, the primary challenge is that DAFF decides on who the recipients of funds should be and not the Land Bank. National Treasury noted that this places the Land Bank in an awkward position where it has to account for the misuse of funds, although it is not the decision maker.
- 6.3.5. The Land Bank also submits that there were administrative challenges, as the criteria from DAFF for the fund was sometimes not clear, which made it difficult for the Land Bank to distribute the funds timeously. National Treasury further explained that it had to withdraw funding allocated for MAFISA and AgriBEE programmes because the funds were being misused.
- 6.3.6. **Figure 8** below shows the number of DAFF's financial intermediaries and farmers funded between 2013 and 2018. It illustrates that the total number of financial intermediaries utilised by DAFF is increasing over time. In the process, a total of 7145 smallholder farmers have been assisted through intermediaries in the past five years by DAFF.<sup>82</sup> Annual assessments of financial intermediaries performed by DAFF indicate that generally, the level of viability and sustainability of programmes of financial intermediaries in the sector is low. Some of the contributing factors include heavy reliance on grant funding and inability to access financial support from other financial institutions.<sup>83</sup>

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<sup>82</sup> DAFF's response to the Parliamentary Monitoring Group on 11 May 2018 accessible at <https://pmg.org.za/committee-question/8796/> last accessed on 22 November 2018.

<sup>83</sup> Ibid.

**Figure 8: Number of DAFF's financial intermediaries and the number of funded farmers (2013-2018)**

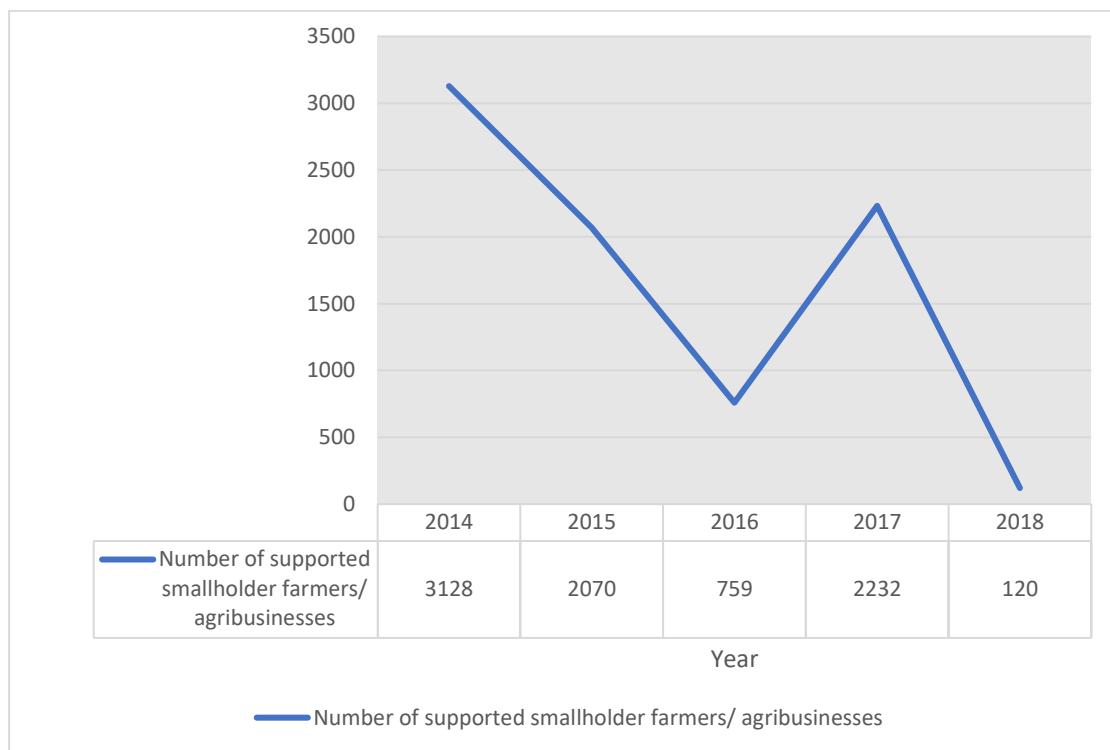


Source: The Authors compilation from information sourced from DAFF<sup>84</sup>

- 6.3.7. **Figure 9** below illustrates the performance of the MAFISA fund during the period 2014 to 2018. From **Figure 9**, it is apparent that there has been a fluctuation in terms of the number of smallholder farmers and agribusinesses that were supported over time. For example, in 2014 there were 3128 farmers supported, while in 2016 this number plunged to 759. However, in 2017, the number of supported farmers increased to 2232 from 759 recorded in 2016, which is a 194% increase. During 2018, the number of supported farmers further declined to 120 which is the lowest number when compared to the five (5) years of 2014-2018 studied.

<sup>84</sup> Accessed from <https://pmg.org.za/committee-question/8796/> last accessed on 22 November 2018.

**Figure 9: Performance of the MAFISA fund (2014-2018)**



Source: *The Authors compilation from information sourced from DAFF.*<sup>85</sup>

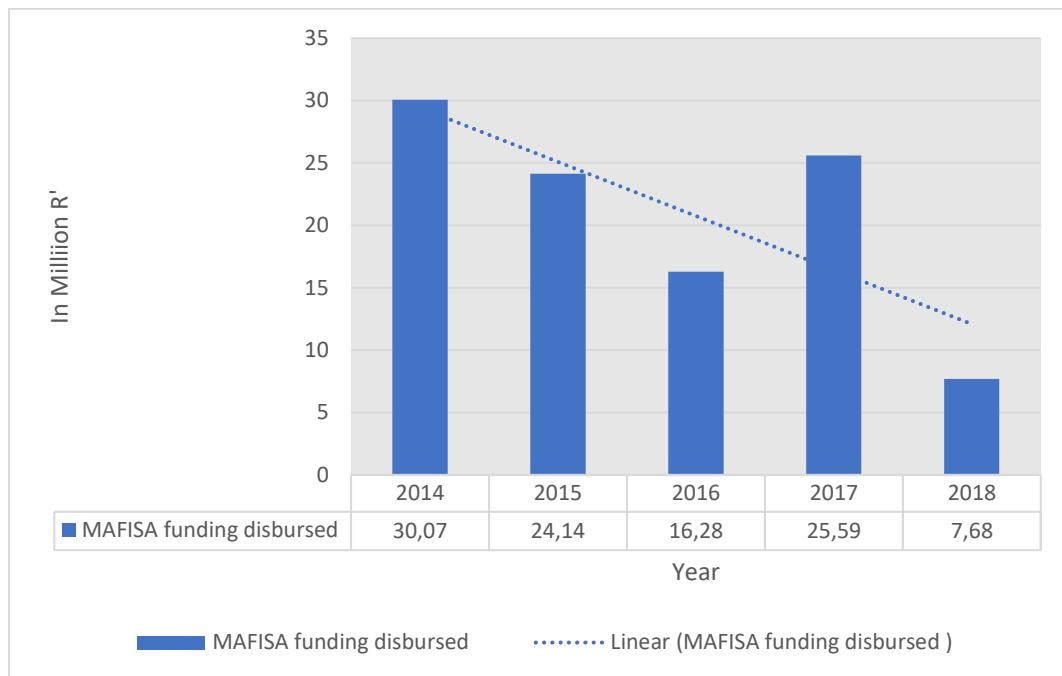
6.3.8. **Figure 10** below shows the financing trend of the MAFISA fund from 2014 to 2018.

**Figure 10** also demonstrates that there has been a gradual decline in the trend of the amounts disbursed under the MAFISA fund over some time. For instance, in 2014, the total amount disbursed was R30.07 million, while by 2018 the total amount disbursed decreased to R7.68 million. However, the decrease in the disbursed amounts overtime can be attributable to the number of qualifying funding applications received by financial intermediaries administering the MAFISA fund in a particular year. Also, the decrease is a result of a reduced number of intermediaries over time, no additional budget allocation for the fund and the financial risks of some applicants.

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<sup>85</sup> Submission of the Department of Agriculture, Forestry and Fisheries dated 12 December 2018.

**Figure 10: Financing trend of the MAFISA fund (2014-2018)**



Source: The Authors compilation from information sourced from DAFF.<sup>86</sup>

## 7. The research observations

### 7.1. The mandate and structure of the Land Bank

- 7.1.1. The authors note that the Land Bank's operations are underpinned by a commercial approach towards lending, which can have a bearing on its developmental mandate. It does not receive any funding from the National Treasury. It raises funds from capital markets, advanced loans and charges interest to the different categories of farmers. The research considered the Land Bank's normal funding operations and found that it must source funds at commercial rates and make a return to sustain its operations. It is for this reason that the funding model has strict disbursement conditions and reporting requirements.
- 7.1.2. The critical structural barrier affecting the transformation objectives of the Land Bank is the fact that it is currently a self-sufficient and self-funding institution. There is, however, a paradox that exists about the mandate and structure of the Land Bank which may pose challenges to achieve developmental outcomes.
- 7.1.3. The mandate and structure of the Land Bank are not aligned. The Land Bank is expected to manage the risk of its investments while achieving a developmental mandate. Its funding criteria are therefore geared to fund bankable businesses. This may not enable

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<sup>86</sup> Department of Agriculture, Forestry and Fisheries. Submission dated 12 December 2018.

a developmental mandate. A reconsideration of its mandate and structure is necessary to address this paradox. A change in structure will empower the Land Bank to develop further necessary changes in its organisational and policy-making structures to enable it to realise its developmental mandate fully.

- 7.1.4. If the status quo continues, the structure of the Land Bank will continue to cater to a particular category of farmers (medium to large commercial farmers) who meet its risk profile. While the authors acknowledge that there is a need to fund medium to large commercial farmers for food security, if the same structure of the Land Bank remains, this leaves a funding gap for emerging farmers. In this case there will need to be another entity with a developmental mandate that can leverage off existing government funding and programmes and incorporate them into one national developmental framework that will cater for emerging farmers. Within this framework, emerging farmers could be funded through either grant or development funding models such as blended finance and incubation. The focus of the framework should be specifically geared to the emerging sector. The coordination of efforts and spend should be done at the national level.

## **7.2. Funding models**

- 7.2.1. Many of the issues raised relate to the mechanics of how, when and at what cost funding is made available to farmers. The challenge for funding institutions is to provide agricultural credit that meets the unique demands of the various categories of farmers in the sector, including commercial and emerging farmers. In fact, in engagements with stakeholders, it was stated that when considering lowering barriers to entry it is necessary to be clear about the category of farmer that is the focus of the intervention and the differentiation in agricultural commodity value chains. One must distinguish between capital to acquire land, for infrastructure, equipment and inputs and day-to-day operations. These would require different models of financing.
- 7.2.2. Although some improvements have been made, small-scale farmers are yet to be reached by these institutions.<sup>87</sup> Funding institutions have been slow to find appropriate finance models that support access to finance among the various categories of farmers,

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<sup>87</sup> Department of Agriculture, Forestry & Fisheries ‘National Policy on Comprehensive Producer Development Support: Draft 5 version 3’ (30 May 2018) on page 1, accessible at [https://www.daff.gov.za/docs/media/Draft%205%20ver%203%20Policy%20on%20CPDS\\_30May2018\\_accepted%20change.pdf](https://www.daff.gov.za/docs/media/Draft%205%20ver%203%20Policy%20on%20CPDS_30May2018_accepted%20change.pdf) last accessed on 14 November 2018.

including small-scale farmers. Therefore, there are still gaps in terms of the various categories of farmers that can be adequately financed by these institutions.

- 7.2.3. Farming enterprises across and within different sub-sectors (commodities) require various levels of capital investment and operating expenditure and also possess vastly different revenue-generating potential.<sup>88</sup> Farm sizes also differ significantly. This is also due to the different farmer categories and farming systems co-existing in South Africa. There are unique competition dynamics pertaining to the different commodities in the agricultural sector. Similarly, there are unique funding requirements for different value chains.
- 7.2.4. Smallholder farmers with commercial intent should be able to access more finance, lease more land and source inputs at affordable prices. Thus, funders will need to adapt or develop tailor-made funding models for emerging farmers.
- 7.2.5. Some stakeholders interviewed during the research suggest that the idea is not for all small-scale farmers to become commercial farmers, but to assist the small-scale agri-entrepreneurs with ambitions of growth. It was stated that not all small-scale farmers want to increase scale and become commercial farmers. According to some stakeholders, only a few small-scale farmers will become commercial farmers, and there will remain a role for smallholder farmers. Some farmers may choose to stay in a lower risk pool where they are getting a significant turnover. This is where spatial targeting may present value. BFAP has made use of a combination of databases, platforms and geographic information system (GIS) to map the concentration of emerging farmers and vulnerable households across South Africa. By layering this information, various strategic and spatially targeted comprehensive producer support programmes can be initiated and developed to improve the chances of success for emerging farmers.
- 7.2.6. DAFF's draft National Policy on Comprehensive Producer Development Support recognises the lack of coordination and collaboration among key stakeholders in the provision of producer support.<sup>89</sup> The Policy outlines an institutional mechanism for implementation that involves coordination and collaboration among key stakeholders and government departments. In the same way, there should be coordination among

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<sup>88</sup> BFAP Baseline Agricultural Outlook 2018 – 2027 at page 11, accessible at <http://www.bfap.co.za/wp-content/uploads/2018/08/BFAPBaseline-2018.pdf> last accessed on 12 November 2018.

<sup>89</sup> The Policy is accessible at [http://www.daff.gov.za/daffweb3/Draft%205%20ver%203%20Policy%20on%20CPDS\\_30May2018\\_accepted%20change.docx](http://www.daff.gov.za/daffweb3/Draft%205%20ver%203%20Policy%20on%20CPDS_30May2018_accepted%20change.docx) last accessed on 12 November 2018. The policy references DAFF's commitment to secure at least 10% of public expenditure for agriculture as part of the Government's commitment to the Malabo Declaration. However, National Treasury conveyed to the authors that this figure is likely to be reduced given that the needs of South Africa's agricultural sector is not similar to the agricultural needs of some of the other signatories of the Malabo Declaration.

the Land Bank, DFIs, DRDLR and Department of Water and Sanitation on issues affecting farmers. It recommends that DAFF consider alternative and innovative financial mechanisms to ensure access to finance for smallholder farmers through models such as blended finance.<sup>90</sup> It also recommends that government together with the private sector should develop affordable, and viable insurance packages for producers to cover the inherent risks of production activities along the value chain, thus supporting a blended finance model.

- 7.2.7. The blended finance model refers to when public and private investors strategically mobilise additional private finance. The research considered the use of blended finance as a model that can be used for the mobilisation of additional finance from private and public investors towards sustainable development in emerging economies.<sup>91</sup> The OECD Development Assistance Committee in February 2016 agreed to develop an inclusive, targeted and results orientated work programme on blended finance.<sup>92</sup> It has introduced policy guidance and principles on the use of blended finance to deliver a development impact. In this regard, the OECD issued five (5) blended finance principles around mobilising development funding:<sup>93</sup>
- Principle 1 - Anchor blended finance use to a development rationale;
  - Principle 2 – Design blended finance to increase the mobilisation of commercial finance;
  - Principle 3 - Tailor blended finance to local content;
  - Principle 4 – Focus on effective partnering for blended finance; and
  - Principle 5 – Monitor blended finance for transparency and results.
- 7.2.8. The mechanisms adopted may provide much-needed recommendations to bring together the public and private investors for the use and deployment of blended finance to emerging economies.
- 7.2.9. In September 2018, President of the Republic of South Africa, Cyril Ramaphosa announced plans to crowd in private resources for the creation of a public-private

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<sup>90</sup> Ibid at page 3.

<sup>91</sup> OECD “Blended Finance” accessible at <http://www.oecd.org/development/financing-sustainable-development/development-finance-topics/blended-finance.htm> last accessed on 12 November 2018.

<sup>92</sup> Ibid.

<sup>93</sup> The OECD’s explanation of the 5 Blended Finance Principles around mobilising the funding, accessible at <https://www.oecd.org/dac/financing-sustainable-development/development-finance-topics/OECD-Blended-Finance-Principles.pdf> last accessed on 12 November 2018. The Land Bank informed the authors that it has adopted these principles in developing its blended finance model.

infrastructure fund, which will seek to mobilise non-government resources, including from domestic and international development finance institutions (BRICS countries), domestic pension funds and commercial banks.<sup>94</sup> Blended finance will be mobilised from the Land Bank, IDC and commercial banks for transactions in the agricultural sector over the next 3 to 5 years.<sup>95</sup> At this stage, it is not clear how this approach will be phased in. The responsibility to support accelerated transformation in the sector will have to be shared among many players, including the various government departments, the private sector, as well as established commercial farmers.

- 7.2.10. Blended finance is typically easier to deploy in countries and sectors where policy frameworks for investment are well established and where revenue streams are clear.<sup>96</sup> Structural impediments to sustainable development increase the perception of risk. Many private sector participants are wary of investing in emerging farmers given their concerns about absorptive capacity, low returns and sustainability. Furthermore, successful agricultural development requires the establishment of value chains consisting of land, infrastructure, funding, access to water rights, skills and access to routes to market. Multiple role players will have to participate.
- 7.2.11. The Land Bank, DAFF and DRDLR are responsible for developing a blended finance model. They are ideally positioned to add value to the transformation of the South African agricultural sector while remaining financially viable.<sup>97</sup> The Land Bank appears to have started implementing blended finance models, for instance in the deciduous fruit value chain.<sup>98</sup> A R600 million fund was established, providing debt finance and comprehensive business support (technical and business support, market access and crop insurance) to black-owned businesses in the deciduous fruit value chain.<sup>99</sup> This consists of granting funding provided by the Jobs Fund to the Deciduous Fruit

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<sup>94</sup> Terence Creamer ‘Ramaphosa plans to crowd in private resources for infrastructure fund’ (21 September 2018) Engineering News, accessible at [http://www.engineeringnews.co.za/article/ramaphosa-aims-to-crowd-in-private-resources-for-infrastructure-fund-2018-09-21/rep\\_id:4136](http://www.engineeringnews.co.za/article/ramaphosa-aims-to-crowd-in-private-resources-for-infrastructure-fund-2018-09-21/rep_id:4136) last accessed on 12 November 2018. See also ‘Cyrils Stimulus Package’ Pressreader, accessible at <https://www.pressreader.com/south-africa/daily-dispatch/20180924/281526521975746> last accessed on 12 November 2018.

<sup>95</sup> Ibid.

<sup>96</sup> Haje Schutte ‘Blended Finance must deliver for the least developed countries (4 June 2018) OECD accessible at <https://www.devfinance.net/blended-finance-must-deliver-least-developed-countries/> last accessed on 12 November 2018.

<sup>97</sup> Bennie van Rooy Opinion ‘The Land Bank in perfect position to assist transformation’ (15 August 2018), accessible at <https://www.iol.co.za/business-report/opinion/opinion-land-bank-in-perfect-position-to-assist-transformation-16577316> last accessed on 12 November 2018.

<sup>98</sup> Refer to the ‘The Land Bank:Fixed Income Investor Roadshow August 2018’ Presentation accessible at <https://landbank.co.za/Investor%20Presentations/Land%20Bank%20Roadshow%20August%202018.pdf> , last accessed on 13 November 2018 at page 55.

<sup>99</sup> Ibid at page 52.

Producers Trust interest-free and concessionary debt financed by the Land Bank.<sup>100</sup> The Land Bank, however, does not at this stage have data to measure the success or failure of such a model.

### **7.3. Funding criteria**

- 7.3.1. There appears to be some information asymmetry which exists about the funding criteria used in some funding initiatives. One of the ways to address the asymmetry is to standardise the criteria so that it is clear and easily understood by emerging farmers. If all of the existing funding institutions in the sector standardised their funding requirements, criteria for eligibility for funding, risk assessments and credit policies applied this would assist emerging farmers. This will also serve to ensure that emerging farmers are aware of the requirements and can source funding more efficiently. This standardisation of funding criteria should also filter down to financial intermediaries so that they adopt the same approach when dispersing funds.
- 7.3.2. The research does, however, note that any funding criteria will still need to ensure that it takes into account the different dynamics that may exist given the different markets and commodities and the risks associated. Further, like any criteria, it still needs to ensure that it separates those farmers who have viable interests against those that do not.

### **7.4. Timing of disbursements**

- 7.4.1. The research found that one of the challenges faced by new entrants is with regards to the period in which disbursements are released to them by funding institutions. Generally, funding is not released in time to meet the urgent financial relief sought by emerging farmers. The authors acknowledge that there are administrative challenges faced by funders which may have an impact on turnaround times in the processing of funding applications and disbursing of funds such as performing the necessary due diligence and improving the business plans presented by emerging farmers into fundable projects.
- 7.4.2. The research also demonstrates that emerging farmers should also be cognisant of the timing in which they submit their applications to ensure that they plan appropriately. However, funders can assist in ensuring there is better guidance to farmers on when to apply and the timelines involved.

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<sup>100</sup> TP Nchocho The Land Bank Presentation to the Portfolio Committee on Agriculture, Forestry and Fisheries (24 April 2018) accessible at [http://pmg-assets.s3-website-eu-west-1.amazonaws.com/180424Land\\_Bank.pdf](http://pmg-assets.s3-website-eu-west-1.amazonaws.com/180424Land_Bank.pdf), last accessed on 14 November 2018. Refer to The Land Bank Presentation 2018 at page 44.

- 7.4.3. Funders should pay attention to the needs of applicants as part of their assessments of funding applications. This will provide funders with necessary information regarding the timelines when applicants require funding. Funders must also be well capacitated with agricultural specialists who understand and have the expertise to factor-in production calendars or cycles of different types of farming.

### **7.5. Use of intermediaries**

- 7.5.1. Although incumbents have the technical capability and expertise to provide non-financial support to emerging farmers through intermediary structures, the Land Bank should re-evaluate its assessment criteria for the appointment of intermediaries to ensure that they do not overtly allow for a platform to inhibit entry and expansion of emerging farmers.
- 7.5.2. During the engagements with the Land Bank, it submitted that it had requested intermediaries to become more transformative, firstly in their structures and secondly to ensure that applicants can pay back their loans. Therefore, according to the Land Bank, although intermediaries can facilitate access to funding through their structures, emerging farmers face barriers to entry such as collateral and equity.
- 7.5.3. The inherent concern of positioning incumbents as intermediaries in development funding structures is that they are unlikely to support initiatives that aid the expansion of their potential competitors such as emerging farmers. Competition would favour a position where incumbents are not responsible for funding competitors. It is also notable that some of the firms that are intermediaries are firms that have previously been investigated by the competition authorities for possible contraventions of the Competition Act.
- 7.5.4. Funders should be capacitated to deliver this producer support and should be responsible for managing their entire loan book. Market experts with technical knowledge of the agricultural sector should be in-sourced. If this is not a practical solution, funders must play a more significant role of oversight over intermediaries. In this regard, they would need to implement improved monitoring and evaluation measures and metrics for transformation in the SLAs they enter into with intermediaries.

### **7.6. Strategic purchaser role of funders**

- 7.6.1. The research indicates that for emerging farmers and new entrants to become successful enterprises they need economies of scale. The rising costs of equipment and other inputs needed by emerging farmers is also one of the barriers to entry. Therefore,

given the fact that funders provide financing to farmers to acquire infrastructure and inputs (such as tractors and other harvesting tools), the funders can play an active supplier role by acquiring and supplying these inputs and infrastructure to farming enterprises that they can negotiate through coordination of resources.

- 7.6.2. Funders should consider being strategic purchasers and suppliers of infrastructure and inputs, as they would be able to acquire these strategic enablers at lower prices and obtain discounts when they buy in bulk. It is envisaged that this will relieve the burden that new entrants and emerging farmers face to compete effectively in the sector. This is value-chain financing, which is advocated as an appropriate mechanism to address the high barriers to entry in the agricultural sector.

## **7.7. Patient and lifecycle funding**

- 7.7.1. A further problem related to effective entry and expansion of emerging farmers is the absence of lifecycle funding in some aspects, with the financiers providing once-off capital payment in some instance. It is notable that this is more likely concerning grant funding, as further loans are generally available on the payment of an initial one. Funding is required through various aspects of production, but also in relation to getting the product to market. In other words, there is also a gap in terms of providing financial (and non-financial) support, to access markets, technical skills and assistance to provide alternatives to meet collateral requirements of financial institutions.
- 7.7.2. Further, for entry to be effective, funding is required not only for the entire lifecycle of the agribusiness but until the farmer reaches a point where they can sustain themselves. Such an approach requires patient funding which considers the multiple exogenous factors and risks that farming enterprises face.
- 7.7.3. The Report of the High-Level Panel on the Assessment of Key Legislation and the Acceleration of Fundamental Change led former President Kgalema Motlanthe published in November 2017 (Motlanthe High-Level Panel Report), found that the risk of default is often assessed to be high, given the rate of failure of small business in South Africa, though this partly reflects lack of access to finance and to markets. To resolve this dilemma, the Panel recommended that legislative efforts support the advancement of patient capital to new or small businesses, with an emphasis on equity and royalty-based financing schemes, in addition to loans.<sup>101</sup>

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<sup>101</sup> Report of the High Level Panel on the Assessment of Key Legislation and The Acceleration of Fundamental Change (November 2017) at pages 37 and 42.

- 7.7.4. The research also recognises that patient funding may not be feasible when funding is raised commercially or where there is no government funding support for the DFIs. However, it is found that absent the Land Bank's extended loan facility, patient and lifecycle funding is generally absent in the agricultural sector.
- 7.7.5. Farmers end up in a situation where they exit the market due to cash flow problems and lack of market support. Different types of farming involve high sunk and start-up investment costs which cannot be recovered by emerging farmers in the short-term.
- 7.7.6. There needs to be an understanding by government and funding institutions that not all projects or enterprises funded may have returns, but it certainly will be a process of learning and development for farmers to become sustainable and competitive. This is a strategic objective of a developmental mandate.
- 7.7.7. Funding institutions in the sector need to understand that their clients are long term. In other words, they should be prepared to provide financial and non-financial support for the long term in order to secure longevity in farming enterprises and food security for consumers. There needs to be provision and planning to fund farmers through the lifecycle of the farming enterprise.

## **7.8. Coordination and collaboration among key stakeholders**

- 7.8.1. Lack of access to finance is a consistent theme when it comes to constraints facing emerging farmers. The Motlanthe High-Level Panel Report 'advocated for coordination across departments and spheres of government to align policies and actions for successful implementation.<sup>102</sup> It was noted that successful implementation of legislation is hindered by fragmentation in government, where different departments can be found to be working in silos and face budget shortages.<sup>103</sup> It uncovered that different government departments had mounted numerous initiatives for agricultural support, such as the CASP, MAFISA and the Recapitalisation and Development Programme (RECAP).<sup>104</sup> However, it uncovered that there has been a clear lack of coordination by DAFF and DRDLR in the delivery of these initiatives. In addition, there

<sup>102</sup> Report of the High Level Panel on the Assessment of Key Legislation and The Acceleration of Fundamental Change (November 2017) at page 515 accessible at [https://www.parliament.gov.za/storage/app/media/Pages/2017/october/High\\_Level\\_Panel/HLP\\_Report/HLP\\_report.pdf](https://www.parliament.gov.za/storage/app/media/Pages/2017/october/High_Level_Panel/HLP_Report/HLP_report.pdf) last accessed on 21 November 2018.

<sup>103</sup> Ibid at page 75 and 215. DAFF's National Policy on Comprehensive Producer Development Support also referenced this challenge.

<sup>104</sup> Ibid at page 217. CASP seeks to enhance provision of support services to promote and facilitate agricultural development, while MAFISA aims to empower micro and small-scale entrepreneurs and farmers to improve their livelihoods and develop their businesses. RECAP aims to provide technical and financial support to farms in distress to increase production, commercialisation, employment, and food security.

was a lack of clarity in relation to target groups, resulting in reduced take-up. The findings of this research paper support this view.

- 7.8.2. DAFF's draft National Policy on Comprehensive Producer Development Support also recognises the lack of coordination and collaboration among key stakeholders in the provision of producer support.<sup>105</sup> The primary challenge is the efficient utilisation of these resources for which collaboration is crucial. The provision of funding is not adequately complemented with the provision of other non-financial support services. Non-alignment of policies between the different spheres of government and stakeholders has had a negative impact on the sector.
- 7.8.3. The research finds that there is poor coordination between funders with respect to providing financial and non-financial support to emerging farmers. The memoranda of understanding (MOUs) entered into between the key stakeholders appear not to be effective mechanisms for ensuring coordination. In this regard, there is a need to create mechanisms that will improve coordination and collaboration among government departments and other key stakeholders in the agricultural sector, such as the Land Bank, DAFF, IDC, DRDLR, the Department of Environmental Affairs and the Department of Water and Sanitation. This coordinated effort by stakeholders to strategically utilise their resources for the maximum benefit of emerging farmers in the sector will assist in achieving their objectives.<sup>106</sup> Coordinated support programmes need to be initiated through a regulated policy framework that will ensure that all relevant players work together.

## 8. Conclusion

- 8.1. The research aimed to examine funding as a barrier to entry and expansion affecting emerging farmers in the agricultural sector. It is clear from the findings of the research that funding remains a high barrier, especially for emerging farmers. In this regard, it is unlikely that the persisting concentration in the sector will be addressed, as there will be little change in the structure of the market.
- 8.2. The research found that the funding framework in the country does not appear to be geared to emerging farmers and caters more to existing commercial farmers. The competitive landscape in the sector is thus in imbalance as emerging farmers have to overcome structural, regulatory and behavioural barriers in order to compete effectively.

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<sup>105</sup> The Policy is accessible at [http://www.daff.gov.za/daffweb3/Draft%205%20ver%203%20Policy%20on%20CPDS\\_30May2018\\_accepted%20change.docx](http://www.daff.gov.za/daffweb3/Draft%205%20ver%203%20Policy%20on%20CPDS_30May2018_accepted%20change.docx) last accessed on 12 November 2018. See page 6.

<sup>106</sup> It is acknowledged that this forms part of The Land Bank's Corporate Plan for FY2019 to FY2021 at page 75.

8.3.The barriers found in the sector relate to how the funding institutions and programmes are structured and operated. It is clear from the findings that there is no fully developmental funding mechanism, as Land Bank is unable to fulfil this mandate. Concerning where the government provides grant funding through its various projects, this is not always sufficient to make the farmer's business sustainable. In order to overcome these structural and regulatory barriers, there will need to be a change in policy and regulation in order to introduce a coherent funding framework that will allow for entry and greater participation.

8.4.Other barriers relate to how the relevant stakeholders in the sector conduct themselves. Incumbents who act as intermediaries have little incentive to introduce competition against themselves and would thus do as little as possible in this role. The research also found that there is a lack of coordination amongst the various players and programmes in the country and that a single framework would go a long way to achieve coordination.

-End-

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