Development Bank of Southern Africa Limited

Registration number: 1600157FN

JSE alpha code: DIDBS

("DBSA or "the Bank")

Audited annual financial statements for the year ended 31 March 2020

Overview

DBSA is a development finance institution; whose only shareholder is the Government of the Republic of South Africa. This summary of the condensed year-end financial results is published on SENS to provide information to the holders of the Bank's listed debt instruments. The condensed year end results are prepared in accordance with the requirements of International Financial Reporting Standards (IFRS) and its interpretations as issued by the International Accounting Standards Board (IASB), the presentation requirements of IAS 1 and requirements of section 27 to 31 of the Companies Act of South Africa (Act No.71 of 2008), these being the relevant and corresponding sections specified in the Development Bank of Southern Africa Act. The annual financial statements are available on the DBSA website (*https://www.dbsa.org*). The Bank will advise noteholders when the remaining reports forming part of the Integrated Annual Report are available on the website.

Audit of the annual financial statements

The annual financial statements of the Bank for the year ended 31 March 2020 have been audited by the Bank's auditor, The Auditor-General of South Africa (hereafter referred to as the AG). The AG in his audit report, which is available for inspection at the Bank's Registered Office, stated that his audit was conducted in accordance with International Standards on Auditing, and has expressed an unqualified audit opinion on the annual financial statements for the year ended 31 March 2020.

Context of the annual financial statements

During the last quarter of the year under review, the global spread of COVID-19 created an unprecedented health and economic crisis which saw most countries closing borders and implementing lockdown measures to contain the spread of the virus. The economic fallout from the pandemic necessitated the implementation of unconventional monetary and fiscal policy measures across the world. In South Africa an infrastructure-led recovery was identified as an important driver of the post-lockdown recovery plan. The South African economy recorded its third consecutive quarter of economic decline of 2.0% (seasonally adjusted and annualised) in the first quarter ending 31 March 2020. This followed contractions of 1.4% and 0.8% in the fourth and third quarters of 2019, respectively. The first-quarter downturn was largely driven by, among others, sharp declines in mining and manufacturing output.

Following the outbreak of the COVID-19 pandemic, the Bank increased its expected credit loss provisions on the performing loan book resulting in higher expected credit loss coverage and lower profitability levels when compared to the prior year. However, development loan disbursements increased by more than 75% when compared to 2019 levels. The Bank achieved higher levels of loan approvals and commitments compared to the prior year. Furthermore, the Bank remained focused in line with its mandate, on pursuing its growth strategy designed to augment disbursements through emphasis on its catalytic role aimed at contributing to sustainable infrastructure development beyond the confines of its own balance sheet. Through this strategy, the Bank aims at crowding in third party funding through de-risking projects through early stage project preparation and structuring and innovative solutioning.

Preparation of the annual financial statements

The annual financial statements have been prepared under the supervision of the Chief Financial Officer, Boitumelo Mosako CA (SA). The directors take full responsibility for the preparation and for correctly extracting the financial information from the underlying audited annual financial statements for inclusion in the SENS announcement.

Basis of preparation

The annual financial statements have been prepared in accordance with the recognition, measurement and disclosure requirements of International Financial Reporting Standards (“IFRS”), Public Finance Management Act of South Africa (“PFMA”), Section 27 to 31 of the Companies Act of South Africa and the Development Bank of Southern Africa Act.

Except for where indicated in the detailed financial results, the accounting policies and practices applied during the year ended 31 March 2020 are in all material respects consistent with those applied in the Annual Financial Statements for the prior year. The Bank adopted IFRS 16 Leases during the period under review and the impact of the standard was not material (refer to page 9 below).

The annual financial statements are prepared on the historical cost basis except for the following assets and liabilities that are stated at their fair value: derivative financial instruments, financial instruments held at fair value through profit and loss, financial instruments designated at fair value through profit and loss, land and buildings, equity investments, other financial assets, post-retirement medical aid benefit investment, funeral benefit and post-retirement medical aid liabilities. The preparation of annual financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates.

Key impressions of the financial results and activities

<u>Funding and liquidity management</u>

The Bank's liquidity and capital positions remain strong despite the recent Moody's Investors Service downgrade of the DBSA's long-term foreign currency issuer credit rating to a notch below that of the sovereign, and of the Bank's long-term national scale issuer rating to Aa3.za, from Aa1.za. Notwithstanding the disruption of the local fixed income market, the DBSA has been successful in raising funding from international development finance institutions as well as international and local commercial banks. Total debt increased from R51bn as at 31 March 2019 to R61bn as at 31 March 2020 and this increased debt capital was used to fund the Bank's development activities and infrastructure financing amounting to R15.7bn. Further, the Bank successfully redeemed the DV22 bond amounting to R9.2bn during the year under review.

<u>Capital adequacy</u>

The debt-to-equity ratio including R20 billion callable capital as at 31 March 2020 amounted to 108% (31 March 2019: 90%), well below the Bank's regulatory debt-to-equity ratio cap of 250%. In the same vein, the Bank's capital ratio expressed as a percentage of balance sheet shareholder capital to unweighted total assets as at end March 2020 was approximately 37% (March 2019: 42%). Callable capital is shares authorized but not yet issued. The Bank's balance sheet equity position increased during the year from R37.2bn as at March 2019 to R37.6bn as at 31 March 2020.

Loan asset quality and expected credit losses provisions

IFRS 9 requires that the Bank considers forward looking information in the calculation of expected credit losses. In doing so, the Bank is required to make reasonable forward-looking assumptions. However, forecasting under the current environment is complex and expected credit loss provisions have a high variability potential because of the influence from the ongoing economic recession and recovery prospects. Given the current deterioration in the macroeconomic base, the Bank experienced a rise in expected credit loss provisions. The Bank increased its expected coverage levels on the performing loan book from approximately 4% in 2019 to 7% as at 31 March 2020 resulting in the balance sheet provision for expected credit losses increasing by 65% to R10.2 billion (31 March 2019: R6.2 billion). The total expected credit loss charge increased from R1.4bn for the March 2019 financial year to R3.6bn for the March 2020 financial year. As at 31 March 2020, the IFRS 9 Stage 3 gross non-performing loan ratio (gross non-performing loans to total gross development loan book) amounted to approximately 7%; and remained largely unchanged when compared to September 2019 half year levels although up when compared to March 2019 (5%).

Asset growth

The Bank's total asset base increased by 12% from R89bn as at March 2019 to R100bn as at March 2020 primarily due to a solid net growth in the development loan book. Despite the growth in the asset base, there was a marginal decrease in net interest income on the back of SARB interest rate cuts. Development loan disbursements amounted to R15.7bn representing an increase of more than 75% when compared to 2019 development loan disbursement levels. As at 31 March 2020, the equity investment portfolio remained largely unchanged at R6bn when compared to the prior year March 2019 (R6bn).

Profitability & Efficiency

The Bank has remained profitable despite a challenging environment which has been worsened by the outbreak of the COVID-19 pandemic. The net profit for year ended March 2020 decreased by R2.5bn from approximately R3bn in the prior year to R503m due to increased expected credit loss provisions resulting from adjusting for the estimated COVID-19 pandemic impact on the performing loan portfolio. The Bank has a net foreign currency USD asset position and given the depreciation of ZAR against USD; exchange rate gains increased to R1.2bn compared to foreign exchange gains of R744m in the prior year. The Bank closely monitors and manages its exposure to foreign exchange rate risk, with the result that the gains reflected in the income statement were on the back of substantially limited downside risk exposure to potential Rand appreciation.

The Bank remains efficient in managing operational costs and the cost optimisation strategy continues to be effective. The total cost-to-income ratio for March 2020 amounted to 28% (23%: March 2019) and the ratio continues to track in line with our cost optimization strategy.

Development impact performance

DBSA successfully delivered infrastructure to the value of R66.3bn billion in total, of which R43.1bn was infrastructure catalysed. In addition, the Bank achieved R2.4bn in projects prepared and committed and was able to unlock infrastructure within under resourced municipalities amounting to R1.4bn. During the year under review, 2 062 learners benefited from 4 newly built schools, 60 501 learners benefited from 110 refurbished schools and 600 people benefited from 200 urban housing dwellings completed. Further anticipated development impact includes benefit to 143 485 households from funds committed to municipalities, funds approved for the preparation of projects of black owned entities to a total value of R1.9 billion and R3.4 billion approved for projects of black-owned entities.

Statement of Financial Position as at 31 March 2020

in thousands of rand	2020	2019
Assets		
Cash and cash equivalents at amortised cost	3 458 836	2 922 876
Trade receivables and other assets	328 069	365 579
Investment securities	1 787 361	1 880 502
Derivative assets held for risk management purposes	812 053	713 304
Other financial assets	36 152	43 732
Development loans held at fair value through profit or loss	22 413	-
Equity investments held at fair value through profit and loss	5 993 951	5 937 578
Development bonds at amortised cost	1 288 278	1 290 179
Development loans at amortised cost	86 240 264	75 816 506
Property, equipment and right of use of assets	417 518	435 020
Intangible assets	80 220	83 133
Total assets	**100 465 115**	**89 488 409**
Equity and liabilities		
Trade, other payables and accrued interest on debt funding	696 324	678 991
Repurchase agreements at amortised cost	587 338	-
Derivative liabilities held for risk management purposes	784 835	297 798
Liability for funeral and post-retirement medical benefits	42 885	44 484
Debt funding designated at fair value through profit or loss	1 505 805	6 469 451
Debt funding held at amortised cost	59 040 495	44 516 190
Provisions and lease liabilities	229 856	309 010
Total liabilities	**62 887 538**	**52 315 924**
Equity		
Share capital	200 000	200 000
Retained income	23 005 253	22 717 877
Permanent government funding	11 692 344	11 692 344
Other reserves	191 749	293 808
Reserve for general loan risks	2 488 231	2 268 456
Total equity	**37 577 577**	**37 172 485**
Total equity and liabilities	**100 465 115**	**89 488 409**

Statement of Comprehensive Income for the year ended 31 March 2020

in thousands of rand	2020	2019
Interest income		
Interest income calculated using the effective interest rate	8 019 931	8 157 805
Other interest income	266 386	252 034
Interest expense		
Net interest expense calculated using the effective interest rate	(3 392 585)	(3 344 288)
Other interest expense	(470 229)	(571 101)
Net interest income	**4 423 503**	**4 494 450**
Net fee income	255 513	193 380
Net foreign exchange gain	1 171 519	743 713
Net (loss)/gain from financial assets and financial liabilities	(529 027)	69 945
Investment and other income	202 617	139 773
Other operating income	**1 100 622**	**1 146 811**
Operating income	**5 524 125**	**5 641 261**
Project preparation expenditure	(41 539)	(1 405)
Development expenditure	(47 192)	(20 505)
Expected credit losses on financial assets held at amortised cost	(3 632 679)	(1 441 056)
Personnel expenses	(751 070)	(751 300)
General and administration expenses	(489 738)	(292 403)
Depreciation and amortisation	(29 321)	(19 579)
Profit from operations	**532 586**	**3 115 013**
Grants paid	(28 654)	(18 318)
Profit for the year	**503 932**	**3 096 695**

Statement of Other Comprehensive Income for the year ended 31 March 2020

in thousands of rand	**2020**	**2019**
Profit for the year	**503 932**	**3 096 695**
Items that will not be reclassified to profit and loss		
(Loss)/gain on revaluation of land and buildings	(15 661)	19 947
Movement due to changes in own credit risk on financial liabilities designated at fair value through profit or loss	(31 794)	(12 852)
Remeasurement of funeral and post-employment medical benefit liability	3 450	2 750
	(44 005)	**9 845**
Items that may be reclassified subsequently to profit and loss		
Unrealised loss on cash flow hedges	(133 443)	(143 346)
Loss on cash flow hedges reclassified to profit and loss	78 839	94 367
	(54 604)	**(48 979)**
Other comprehensive loss	**(98 609)**	**(39 134)**
Total comprehensive income for the year	**405 323**	**3 057 561**

Condensed statement of changes in equity for the year ended 31 March 2020

in thousands of rand	2020	2019
Balance at 1 April 2019	**37 172 485**	**34 114 924**
Impact of adoption of IFRS 16	(231)	-
Restated balance at 1 April 2019	**37 172 254**	**34 114 924**
Profit for the year	503 932	3 096 695
Unrealised loss on cash flow hedges	(133 443)	(143 346)
Loss on cash flow hedges reclassified to profit and loss	78 839	94 367
(Loss)/gain on revaluation of land and buildings	(15 661)	19 947
Movements in changes in own credit risk	(31 794)	(12 852)
Remeasurement of funeral and post-employment medical benefit liability	3 450	2 750
Balance at 31 March 2020	**37 577 577**	**37 172 485**

Condensed Statement of Cash Flows for the year ended 31 March 2020

In thousands of rand		
Cash flows generated from operating activities	3 613 758	3 796 777
Cash flows (used in)/generated from development activities	(9 016 612)	1 216 652
Cash flows generated from/(utilised by) investing activities	32 637	(345 238)
Cash flows generated from/(utilised by) financing activities	5 838 680	(5 516 646)
Effect of exchange rate movement on cash balances	67 497	29 478
Net increase/(decrease) in cash and cash equivalents	**535 960**	**(818 977)**
Cash and cash equivalents at the beginning of the year	2 922 876	3 741 853
Cash and cash equivalents at the end of the year	**3 458 836**	**2 922 876**

Events after the reporting period

On the 17th of August 2020, the National Treasury, Department of Public Works and Infrastructure: Infrastructure South Africa and the DBSA signed the Infrastructure Fund Memorandum of Agreement (MOA) mandating the DBSA to establish and manage the Infrastructure Fund. The signing of the MOA is a significant milestone for the country and paves the way for bringing together key stakeholders to create a platform for blended finance of infrastructure projects. The Infrastructure Fund is one of three national infrastructure funding mechanisms – the others being commercial funding and fiscal allocations. The sources of funding for the Infrastructure Fund will therefore include local capital markets, local and international financing institutions in the private and public sectors as well as the government. There were no other adjusting events that occurred after the reporting date other that impact of COVID-19 pandemic.

Outlook

Despite the challenging economic environment, the DBSA has a strong leadership and management team steering the Bank through the challenging COVID-19 pandemic-driven recessionary environment whilst following principles of good corporate governance. The Bank has a resilient balance sheet and continues to play a significant role in infrastructure development through lending and non-lending activities, whilst making progress in the implementation of the country's Infrastructure Fund and playing an active role in crafting enhancement of municipal service delivery through the District Delivery Model. The Bank's continued success hinges on the Bank's ability to grow developmental impact using its own balance sheet and partnering with others. Both domestic and global economic factors are critical to the achievement of the Bank's objectives. The Bank has a healthy pipeline of projects that form a solid springboard for success in the future and will continue to focus on disbursing to infrastructure projects to grow developmental impact in line with its mandate.

2 October 2020

Debt Sponsor

Nedbank Corporate and Investment Banking, a division of Nedbank.