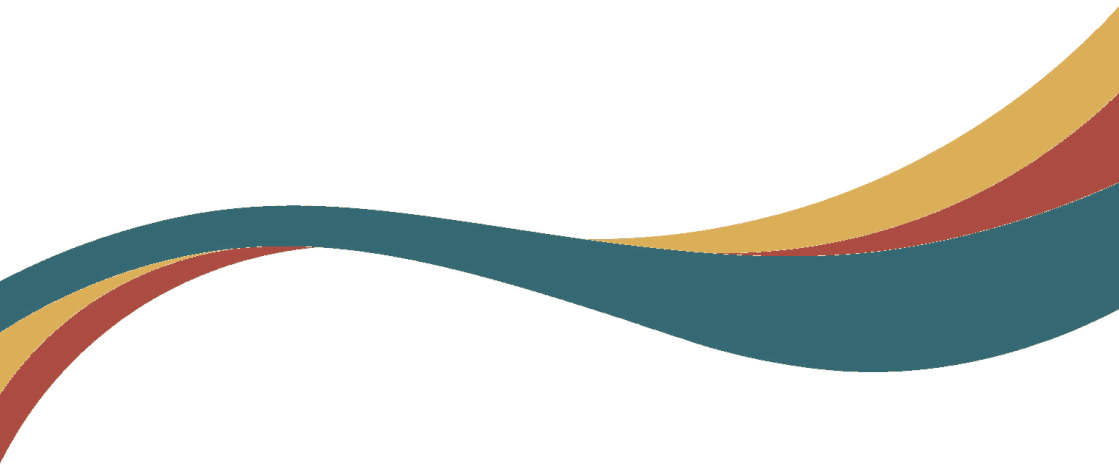




# INVESTMENT BRIEF





## FUND MANAGER



## FUND ADVISORY COUNCIL INCLUDE -



## ADVISORS



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## INTRODUCTION

The ability to provide the requisite defence equipment and services depends on the existence of a vibrant and competitive defence industry, comprising of local and international companies. Such an industry is seen as an integral part of the SANDF's capabilities and, in return, the industry views the SANDF as an anchor client. From an SA broader economic and trade point, point of view, there is a set of national imperatives that range from localisation to transformation and SMME development as well as strategic partnerships with international suppliers. All these imperatives are geared towards ensuring future sustainability of the SA Defence Industry (SADI). Furthermore, new entrants into the defence industry will have to be introduced for future sustainability

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## CURRENT CHALLENGES

Given the complexity and high cost of the defence material and equipment, the barriers of entry into the industry are high, which results in long-term single-source contracting and over-dependence on international suppliers, even in critical and sovereign capabilities.

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## THE NEED FOR THE DIF

- Grant access to finance for both existing and prospective defence companies
- Attract a wider pool of investors including local and international funding sources e.g. private funders and institutional investors
- Give access to support services, tools and support to keep the business running
- Provision of technical skills
- Job creation and skills transfer spinoff

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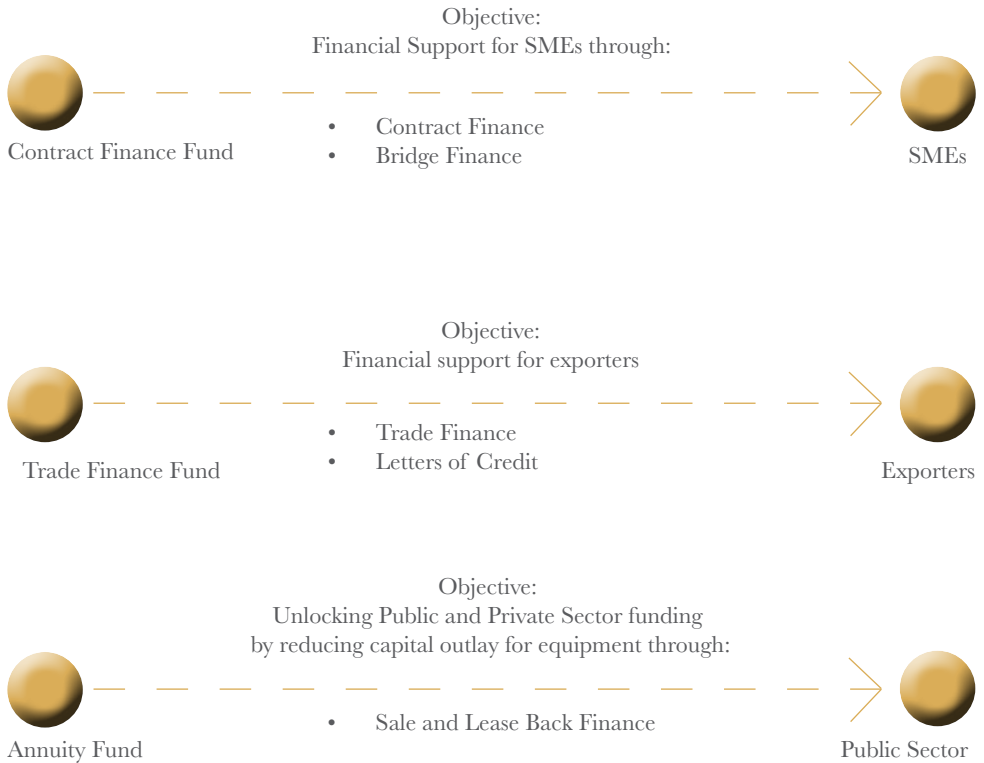
## NATIONAL RISK CONSIDERATION

The dependence of the Defence Force on foreign-sourced equipment, munitions, spares and technical support will curtail South Africa's strategic independence, freedom of strategic action and, to an extent, places sovereignty at risk.



## DEFENCE INDUSTRY FUND - OVERVIEW

In progressive risk stages, Crede will launch a series of investment funds. Each has an independent objective to serve end goals of transformation and support for SMEs, Public Sector, Exporters and specialised industrial projects.





## CONTRACT FINANCE FUND - OVERVIEW

Target Fund Size	R1 Billion
Max Loan Size	R50 000 000
Min Loan Size	R100 000
Target Return	CPI plus 8%
Min Loan Term	1 Month
Max Loan Term	36 Months
Weighted Average Loan Term (target)	6 Months
Fund Life	Open-Ended
Products	<ul style="list-style-type: none"><li>• Contract Finance</li><li>• Trade Finance</li><li>• Bridging Finance</li></ul>
Fund Structure	En Commandite Partnership
Management Fees	Nil
Administration Fees	0.1%
Interest Sharing Incentive	80:20

### INVESTMENT RATIONALE

- SANDF (Armscor/Department of Defence) to act as anchor client for contracts and provide payment security to the Fund
- Fund Manager to support Armscor to reach B-BBEE procurement targets by providing financing to Black-Owned and Empowered SMEs.
- Department of Defence (DOD) current spend in excess of R12 bn on goods and services per annum.
- Armscor (2016/17) BEE acquisition procurement shortfall of R2.4 bn presents a good opportunity for the Fund to close the gap.
- Credit Enhancement Mandate Rules established to protect the Fund against non- payment and/or non-delivery.

# THE OPPORTUNITY - ARMSCOR



4,000



Number of suppliers in the Department of Defence (DOD) Database

200



Average number of contracts awarded annually with deliverables below 12 months

600



active SME suppliers in DOD Database

## Security of Payment



Contracts placed only once funds have been made available. Funds are ring-fenced once contract is placed for that particular contract

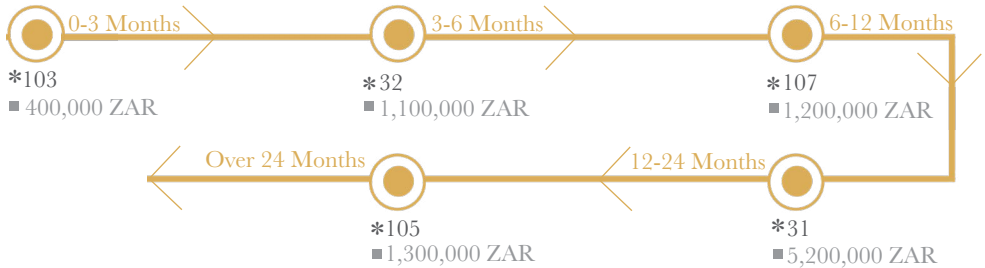
98%

paid suppliers within 30 days or less

### KEY:

-  Number of SME Suppliers
-  Average Contract Value

### Contract Duration



Source: SMEs Armscor



As per table below, an amount of at least R12.5 billion in expenditure is spent annually by the DOD on goods and services such as - computer services, contractors, operating leases, property payments and inventory. This presents a sizeable market opportunity for SMEs in Defence and Defence Related Industries. The Fund will look to provide financial support to SMEs to enable them to finance and deliver on these contracts.

	2018/19	2019/20	2020/21
R million	Total	Total	Total
<b>MTEF Allocation</b>			
Compensation of Employees	27 116.7	29 193.7	31 365.9
Goods and Services	12 330.8	12 927.8	13 745.9
Transfers and Subsidies	7 614.4	7 701.7	7 980.6
Payment for Capital Assets	887.8	873	906.8
<b>Total</b>	<b>47 949.7</b>	<b>50 696.2</b>	<b>53 999.3</b>

Table: Economic Classification - Current Medium Term Framework Budget: 2014 – 2019

## PROCUREMENT TARGETS - ARMSCOR

In summary, in the 2016/17 financial period, Armscor spent 7.52% of the R6bn acquisition budget versus 15% target spend (R907million), 2.65% on EMEs versus a target of 15% (R907 million). The major shortfall is expenditure on Black Owned Entities (BOEs) which came in at R545 million spend versus a target of R2.4 billion.

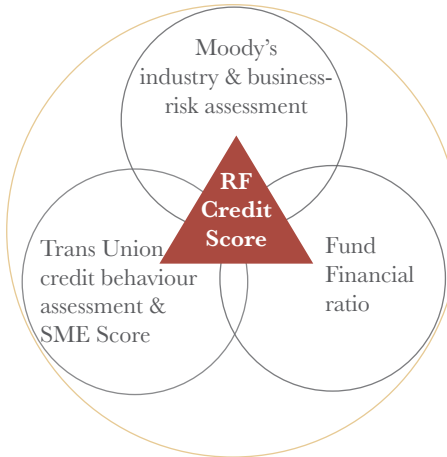
Total Acquisition Procurement Spend		R 6 052 202 067		
Enterprise Classification	B-BBEE SPEND	Current	Target	R Shortfall
QSEs	R 454 916 966	7.52%	15%	(R 452 913 344)
EMEs	R 160 598 984	2.65%	15%	(R 747 231 326)
BOE>51%	R 545 287 006	9.01%	40%	(R 1 875 593 820)
BWOE>30%	R 175 958 381	2.91%	12%	(R 550 305 867)

Table: Target BEE Spend Armscor AFS 2016/17

Fund I and subsequent funds to be launched under DIF will provide financial support to companies with the appropriate technical abilities, track record, teams and empowerment credentials for Armscor to reach its BEE expenditure targets.



## CREDIT EVALUATION PROCESS



Moody's Financial Health Assessment

Considers industry and business-specific data to determine a business's probability of failure

TransUnion's Credit Behaviour Assessment

Considers the credit behaviour of a business and its directors and probability of default

Affordability Assessment

Evaluates a business's credit worthiness based on various affordability ratios & probability of failure based on Altman

Fig: SME Credit Moderation Components

### Post-Loan Monitoring

## CONTRACT FINANCE FUND - MANDATE RULES

### Credit Enhancement

(1)	SME must be registered with DOD/Armscor/CSD
(2)	Fund must be the first to receive payment
(3)	SME must have a valid open contract
(4)	Loan amount limited to open contract value
(5)	No previous cancellation due to non-performance
(6)	SME must agree to Biz Support and Monitoring Programme
(7)	Bank receipt account ceded to Fund to receive first payment
(8)	Technical documentation (submitted to DOD/Client) must be submitted to Fund as well
(9)	DOD/Armscor must validate contract and security of payment
(10)	Valid BEE certificate



## INVESTMENT TEAM

### Sandile Sokhela, CFA

Investment Experience 16 years

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Qualifications CFA Charterholder  
Masters in Development Finance  
Bcom (Hons) (Corporate Finance & Investments)  
Bcom (Economics and Finance)

### Duzi Ndlovu, CFA

Investment Experience 22 years

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Qualifications CFA Charterholder  
MPhil (Applied Ethics)  
Bcom (Accounting)

### Elsje Niemann, CFA

Investment Experience 12 years

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Qualifications CFA Charterholder  
MBA (Cum Laude)  
BEng (Hons) (Cum Laude)  
BEng (Cum Laude)

### Greg Hoffman, CA (SA)

Investment Experience 5 years

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Qualifications CA (SA)  
Post Graduate Diploma: Accounting  
BBusSc (Finance & Accounting)

### Sean Emery

Credit Committee Member/ CEO of Rainfin

Investment Experience 20 years

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Qualifications BPhys  
Post Graduate Diploma: Management - Corporate Finance  
Elective



VISIT US ON:  
[www.credecapital.co.za](http://www.credecapital.co.za)

CONTACT US ON:  
(+27) 11 268 6900  
[info@credecapital.co.za](mailto:info@credecapital.co.za)

**FIND US AT:**

Suite 2  
Ground Floor, Vdara Two  
Vdara Office Park  
41 Rivonia Rd  
Sandhurst  
Johannesburg  
2196