

CO-OP FUND POLICY AND PROCEDURES

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1. Objective

- a.** To create a self sustainable Co-Op Fund, this will re-invest surplus funds on a continuous basis in order to accelerate development in the Eastern Cape.

2. Macro Structure

The ECPCDF will be structured as part grant and part loan. The grant portion is essentially structured to cover the developmental aspects and provide the seed capital for start-ups. This is done by way of providing the equity portion on behalf of the incumbents.

The loan part is to ensure the viability and sustainability of the projects/business ventures and it would be managed by ECDC for an interim period and reviewed on an annual basis.

The fund will be ring fenced for co-operatives and be treated as a revolving fund for assisting prospective co-operatives.

The critical element is to develop requisite capacity for co-operative business ventures to be sustainable and thus, some money will be allocated for non financial support services (BDS) and the seed capital to cater for the equity share and the term loans to be invested in business.

To cover the broad spectrum of co-operatives a network of micro finance institutions /financial services co-operatives and savings and credit co-operatives will be piloted to service small loans up to R20 000 (twenty thousand Rand) with a focus on rural areas where there is greatest need. The development portion will not be applicable except the low interest rates capped at 3-7%.

ECDC will process loans above R20 000 up to R1 million.

Thus the fund will be administered by ECDC on behalf of DEDEA.

- a.** Total Fund of R50 million allocated as follows:
 - i. For Marketing and communication R1 million
 - ii. For Mentoring and Non-Financial Support R4 million
 - iii. For Seed Capital/Risk Fund R12 million
 - iv. For Term Loans R30 million
- b.** Financial Services Co-operatives:
 - i. R2 million for on lending (loans less than R20 000)
- c.** Marketing and communication: DEDEA
 - i. R1 million

3. Role of ECDC

- a.** ECDC as the implementing organ of Provincial Government will administer the Co-Op Fund as outlined in this document.

- b. All Co-Op investments will be clearly identified and separately reported on.

4. Purpose of this Co-Op Investment Policy and Procedure

- a. The Co-Op Investment Policy and Procedures are designed to establish policy, provide instructions and set forth the basic principles to be followed by ECDC in building a Co-Op Investment Portfolio, which could later form the core asset of a proposed Co-Op Bank;

5. Co-Op Investment Types: Products

- a. Seed Capital: Risk Fund - non repayable by the Co-Op
 - i. To form the equity base of the Co-Op
 - ii. This product will be utilized to comply with the minimum equity requirement of a Co-Op Investment
 - iii. This product will be used to fund fixed assets as well as working capital
- b. Term Loan: Repayable by the Co-Op
 - i. Five to ten year period
 - ii. This product will be used to fund
 - a. Fixed Assets (movable and immovable); and
 - b. The fixed portion of working capital i.e. some current assets such as debtors and stock

6. Disbursement of funds

- a. Funds will only be disbursed by ECDC to approved suppliers of the Co-Ops
- b. Such disbursements in a. above will only be made on receipt of original invoices from the manufacturer/supplier of the products
- c. No direct disbursement of funds will be made to the bank account of the Co-Ops without written approval of the relevant approval body

7. Product Mix

- a. Seed Capital: from Risk Fund
 - i. Thirty Percent (30%) of the total Co-Op Fund will be invested in Co-Ops in the form of Seed Capital to form the equity portion of all Co-Op investments;
- b. Term Loans
 - i. Seventy Percent (70%) of the total Co-Op Fund will be invested in the form of Long Term Loans and is repayable by the respective Co-Ops;
- c. Continued Review of Product Mix

- i. The proposed product mix in a. and b. above serves as a target from a risk perspective only and would be monitored given market circumstances from time to time.

8. Qualifying Co-Ops for Investments

- a. The following Co-Ops qualify for investment:
 - i. Worker Producer Co-operatives
 - ii. Services Co-operatives
 - a. Financial services co-operatives
 - b. Consumer co-operatives
- b. The following nine priority sectors qualify for investments
 - i. Agriculture and Agro-processing
 - ii. Forestry and timber industries
 - iii. Tourism
 - iv. Business Process outsourcing
 - v. Construction
 - vi. Automotive sector
 - vii. Textiles (job protection)
 - viii. Chemicals
 - ix. Metals processing
- c. The fund will support new and existing community formed Primary Co-operatives only, as defined in the Co-operative Act No. 14 of 2005 being a Co-operative formed by a minimum of 5 natural persons.

9. Risk Tolerance

- a. Investments in Co-Ops require bigger risk appetite:
 - i. Investments do not require 100% security cover;
 - ii. Minimum equity structure (inclusive of seed capital product as set out in this document) of 30% required for all investments;
 - iii. Where minimum equity structure is not achieved, ECDC would utilize seed capital product to meet the minimum equity requirement. Equity contribution would be by way of a Grant and is not repayable by the Co-Op.
 - iv. ECDC to secure all possible and available security on the Loan Portion of all Co-Op investments;
 - v. The Loan Portion has not to be secured by personal surety from the members of the Co-Ops;
 - vi. Where a Co-Op holds more than one business interest ECDC should insist on registering cross guarantees in its favour from all these business interests;
 - vii. Short term insurance is a requirement for all Co-Op Investments with ECDC's interest clearly registered;

- viii. ECDC to arrange Group Life cover on all members of these Co-Op Investments;
 - ix. General Notarial Bonds (GNB) to be registered on all investments for the full value of the loan amount. Such GNB to include all moveable assets including receivables and stock.
 - x. Mortgage bonds to be registered over all immovable property purchased
 - xi. Suspensive sale agreements to be registered on all relevant fixed assets
- b. Aftercare service to mitigate risk required:**
- i. Account Managers are responsible for each investment made in each Co-Op from inception right through to receipt of last payment;
 - ii. Monthly management accounts collected and quarterly progress reports submitted by the Account Managers in the prescribed format as approved by the executive manager investments from time to time;
- Recovery and/or turn-around strategy should be followed where a loan is considered to be viable before any provision and collection action taken, except where it is suspected that ECDC is deliberately defrauded and it elects not to do any further business with the Co-Op invested in. The latter decision should be taken by the relevant development investment committee.
- c. Cash Flow implications of investments**
- i. Initially aggressive Co-Op investment options should be pursued in order to create a steady reserve income from this proposed Co-Op Investments;
 - ii. The Loan Portion is required to generate a return to ECDC on this Co-Op Investment portfolio. The return generated is then re-invested further in Co-Op investment opportunities;
 - iii. Constant Asset and Liability management is required to ensure continued investment in Co-Ops and eventually un-bundle this portfolio to form a fully fledged Co-Op bank;
- d. Penalty Rates for Co-Op Loans in default**
- i. Penalty Rate of an additional 4% points above the agreed rate on all loans in arrears.
 - ii. This penalty rate will take effect at the beginning of the third month of the Co-Op Loan being in arrears.

10. Suitable Co-Op Investments

Co-Op investments can be categorized as appropriate and non-appropriate. The paragraphs below sets out the distinguishing factors between the two categories:

a. Appropriate Co-Op Investments

- i. Projects with significant developmental impact:
 - a. Job creation/retention;
 - b. Empowerment;
 - c. Value addition;
 - d. Rural Development;
 - e. Export Income Generation;
 - f. Township Development;
 - g. Urban Renewal.
- ii. New Greenfield projects, expansion and rehabilitation transactions (e.g. business rescue);
- iii. All appropriate development investments must however reflect profitability and sustainable commercial viability as determined by the relevant development investment committees.
- b. Non-appropriate opportunities, which will not qualify as Co-Op Investments:**
 - i. Any development investment which might be offensive to the community directly affected by such Co-Op Investment;
 - ii. Any Co-Op Investment which might be offensive to the community at large;
 - iii. Any Co-Op Investment in the form of a loan to finance an acquisition of shares, listed or unlisted of which the such investment is not directly in the target company;
 - iv. Co-Op Investments with the purpose to acquire property, of which the property will be receiving its income from lease rentals only and the loan proceeds will be used for the acquisition of the property only;
 - v. A Co-Op Investment of which the nature thereof requires a period in excess of the recommended investment period of this Co-Op Investment policy to prove viability e.g. any type of investment where the project only shows viability after 10 years;
 - vi. An investment of which the main income stream is from a sub-contract i.e. not a primary contract;
 - vii. An investment where there is no direct decent jobs created or saved as a result of the investment;
 - viii. An investment which has the substance of being speculative;
 - ix. An investment made in any service provider to ECDC;
 - x. Any Co-Op Investment required to fund the purchase of another development investment from ECDC (ECDC does not lend money to a buyer to fund the purchase of a sale of its existing development investments).
 - xi. Any employees or immediate family / board members or immediate family / stakeholders of ECDC and DEDEA
 - xii. Co-op investments which have attracted funding from other Government Departments except in instances where such funding does not constitute “double dipping”

11. Specific Investment Policies

- a. Geographical Spread**
 - i. Any investment of which the head office of the Co-Op invested in falls within the provincial boundaries of the Eastern Cape; and/or
 - ii. The majority of the jobs created directly as a result of the investment and not indirectly as a spin off thereof falls within the provincial boundaries of the Eastern Cape.
- b. Developmental Issues**
 - i. Co-Op Investments must create direct new decent jobs, and/or
 - ii. Co-Op Investments must save existing jobs, and/or

12. Expected Return on Co-Op Investment Portfolio

- a.** The Co-Op Investment portfolio should at all times render a market related return;
- b.** Six monthly revision of product mix and its effect on overall return (refer paragraph 3 b. above) should be conducted;
- c.** Six monthly revision of pricing of individual products to ensure overall return is retained.

13. Requirements from Applicants

- a. Own Contribution**
 - i. No own contribution is required from a Co-Op Investment proposal as this could come from the seed capital product as detailed in this document;
 - ii. Co-Ops must demonstrate 100% commitment from its members;
- b. Expertise**
 - i. Members of a Co-Op Investment must display some expertise in the area of the proposed investment either on a technical or business level;
 - ii. Should the members of the Co-Op Investment not have the required level of skill to drive the proposed investment they should be referred to ECDC Development Services to attend the necessary training courses to improve their level of skill and/or be given access to an appropriate mentor to assist in same.
- c. Active Involvement**
 - i. It is a requirement by ECDC that the members of a Co-Op Investment proposal be actively involved in such investment;
 - ii. Active involvement requires full time participation in the activities of the investment by all of the members in a single investment.
- d. A Co-Op Investment proposal can only be considered if:**
 - i. The members of the Co-Op have lean credit records, and/or provides ECDC with written proof of arrangements made to clear same

- ii. The members of the Co-Op who holds existing accounts with ECDC (including rental accounts) must not be in arrears/default;
- iii. Where an existing Co-Op Investment is in default, it could only be considered for further investment based on an appropriate recovery and collection strategy and only after an appropriate due diligence has been conducted by ECDC to justify the proposed recovery and collection strategy refer paragraph 10 below.

14. Moratoriums

- a. A maximum moratorium of 6 months from final drawdown is allowed on all new development investments;
- b. A moratorium can only to be considered when the cash flow of the development investment indicates such requirement.

15. Recovery and Collections

- a. All Co-Op Investments in default will be notified in writing of such default and listed with an appropriate credit organization (such as ITC) immediately after compliance with NCA requirements (where applicable);
- b. Where such further investment in a Co-Op in default is required to effect recovery of the business it requires the prior written approval by the executive manager investments to conduct a full investigation into the affairs of such Co-Op (refer paragraph 8 d iii above);
- c. All investments in default will be charged an investigation fee on the outstanding balance at the time of default (more than 3 months in arrears). Such fee is required to cover the cost of a recovery initiative, which will include a proper investigation and due diligence exercise with a recovery and collection recommendation to the Development Investment Committee;
- d. The collections unit must inform the relevant account managers immediately when a Co-Op falls into arrears. The account manager must then immediately visit the Co-Op and compile a quality review report.

16. Levels of Authority

The following levels of authority will apply to Co-Op Investments:

- a. Term Loans for amounts not exceeding R500 000 (Five Hundred Thousand Rand):
 - i. Approval requires:
 - a. Signed recommendation by responsible account manager; and
 - b. Signed recommendation by responsible manager: and
 - c. Signed approval by Executive Manager: Investments

- ii. There is no formal committee required to approve these investments;
 - iii. Approval is obtained on an ad hoc basis through the compilation of the appropriate investment papers duly signed by the responsible officials.
 - iv. The district support teams to note the recommended co-op investments
 - v. District support teams (DST) are not to affect the formal requirements of a quorum, thus decision making is not determined upon the availability of the DST members.
 - vi. Minutes of meetings must be kept at all times.
- b. Term Loans for amounts more than R500 000:**
- i. Development Investment Committee (DIC)
 - a. Approval mandate for amounts not exceeding R1 000 000 (One Million Rand);
 - b. Listing of deals approved submitted to Exma for notification;
 - c. Development Investment Committee must meet at least once per week;
 - d. The Development Investment Committee can meet on an ad hoc basis as and when the need arises;
 - e. Minutes must be compiled for all meetings;
 - f. Minutes must be numbered and dated and stored in a single location.
 - g. Members of DEDEA Head Office (senior managers) standing provincial selection team to be represented in meetings taking decisions on approval
 - ii. Exma
 - a. Approval Mandate for amounts not exceeding R5 000 000 (Five Million Rand);
 - b. Listing of deals approved submitted to Board;
 - c. Exma can meet on an ad hoc basis as the need arises;
 - d. Minutes must be compiled for all meetings;
 - e. Minutes must be numbered and dated and stored in a single location
 - f. DEDEA general manager or her delegated person to be represented in meetings taking decisions.
 - iii. Board
 - a. Approval Mandate for amounts exceeding R5 000 000 (Five Million Rand)
 - iv. Involvement of DEDEA and DCF
 - a. It is envisaged that members of DEDEA and DCF be invited to attend the relevant Investment Decision making bodies on invitation as observers for the interim period and once the ECDC board has ratified their proposed status they will participate as explained above.

17. Key Policy Indicators

a. Co-Op Terms

- i. Co-Op investments are required to retain and increase the principal amount of the Co-Op Investment Portfolio
 - a. Term loans:
 - i. Minimum 3 years
 - ii. Maximum 5 years
 - ii. Early redemption penalty levied on early settlements:
 - a. Co-Op Investments: equal to three monthly installments;

b. Interest rates

- i. Co-Op Investments must provide an acceptable return to ECDC as determined by the executive manager investments from time to time;
- ii. Co-Op Term Loans priced at 0% (zero percent) interest and will earn fees only;

c. Fees and Charges

- i. Co-Op Seed Capital
 - a. Structuring fee of 3% of value of transaction;
 - b. Fee payable up-front or deducted from first drawdown.
- ii. Co-Op Term Loans
 - a. Structuring fee of 3% of value of transaction;
 - b. Fee payable up-front or deducted from first drawdown;
 - c. Legal fees as determined by the executive manager investments from time to time;
 - d. Valuation fees where applicable at cost;
 - e. Bond registration fees where applicable at cost.
 - f. Management Fee of 3% of contract value recoverable from Co-Op on a monthly basis over the term of the loan

d. Co-Op Investment Size

- i. Seed Capital (Risk Fund)
 - a. Any single seed capital portion not to exceed R420 000 (Four Hundred and Twenty Thousand Rand);
 - b. Any group of investments to the same related Co-Op not to exceed R420 000 (Four Hundred and Twenty Thousand Rand);
 - c. Minimum development investment of R5 000 (Five Thousand Rand).
- ii. Co-Op Term Loans
 - a. Minimum Co-Op Investment of R20 000 (Twenty Thousand Rand)
 - b. Maximum development investment of R1 million (One Million Rand).

- e. Security**
 - i. ECDC must secure each Co-Op Investment with every available form of security;
 - ii. Where a Co-Op has more than one investment of a similar nature and ECDC is required to invest in only one, cross guarantees is required from all the other investments.
- f. Financial Model**
 - i. Capital Structure
 - a. Equity to total assets of at least 30% at peak funding requirement;
 - b. Redemption of the Co-Op Term Loan within 5 years to 10 years;
 - c. Co-Op Term Loan to total assets not to exceed 60% of total assets.
 - ii. Sensitivity Ratio
 - a. Minimum of 15% turnover sensitivity acceptable (turnover should be able to drop by 15% without endangering the viability of the project).
 - iii. Cash Flow Requirement
 - a. Total outside funds to Cash Flow not to exceed 5 years at peak funding requirement.
- g. Deal Structure**
 - i. Greenfield Investments
 - a. All new investments require the investment to be made in a newly registered Co-Op with audit confirmation that it has never traded before such investment is made;
 - b. All Co-Op investments require a properly constituted members agreements which will contain appropriate measures to protect ECDC as a Investor in such Co-Op;

18. Co-Op Investment Procedures

- a. Application Process**
 - i. Interview
 - a. Account manager interviews prospective client to explore investment opportunities;
 - b. Account manager must capture details of prospective client on IT system;
 - c. Account manager must disclose to the prospective client the process which needs to be followed before an approval can be obtained from ECDC to make an investment;
 - d. Account manager must provide prospective client with a listing of required information which must be submitted to ECDC to enable it to process the application;
 - e. Account manager must provide prospective client with an ECDC application form;

- f. Account manager must provide prospective client with details of ECDC fees and charges as well as applicable interest rates if applicable;
 - g. Account Manager must conduct an interview with a prospective client and is not allowed to process an application without having had an interview with the prospective client;
 - h. The interview stage is the first opportunity to assess the ability of the client and his understanding of the business enterprise in which ECDC is expected to invest;
 - i. The interview is conducted to explore whether the business opportunity presented by the prospective client is indeed within ECDC' s Co-Op investment policy;
 - j. There are no limits as to how many interviews an account manager should have before proceeding to the basic assessment stage of the investment process;
 - k. The account manager is obliged to inform the prospective client if his business proposal does not falls within ECDC Co-Op investment policy. This will ensure that there are no expectations created that ECDC will invest in his proposal.
 - l. All interviews and the outcome thereof must be recorded by the account managers;
 - m. A central record must be compiled of all interviews and the outcome thereof.
- ii. Request for Information
 - a. The request for information must be confirmed to the client in writing
- iii. Basic Assessment (applicable to all Co-Op Investments):
 - a. Capture on IT System on receipt of all information including the completed application form from the prospective client;
 - b. Account manager must conduct a Basic Assessment (desk top) as to whether the received application should be considered by ECDC for investment;
 - c. The basic assessment recommendation from the account manager must contain the reasons for such recommendation;
 - d. The basic assessment recommendation must contain a proposed term sheet to the client reflecting the basis of the proposed investment;
 - e. The basic assessment recommendation and term sheet must be signed by the account manager;
 - f. The basic assessment recommendation and term sheet must be recommended by the manager: loans and equity;
 - g. The basic assessment recommendation and term sheet must be approved by the executive manager: investments

- iv. Term Sheet: applicable to all Co-Op Investments
 - a. The proposed term sheet issued to the client must clearly indicate that it is an expression of interest to invest in the proposed deal only and does in no way constitute an approval of such proposed investment until all the condition contained therein are complied with;
 - b. The term sheet must be signed by the client indicating his acceptance of the proposed terms before any further processing of the investment application can take place.
- v. Due Diligence
 - a. On receipt of the signed term sheet a due diligence must be conducted by the account manager supported by his direct unit manager;
 - b. The due diligence must be conducted inter alia on the physical site of the proposed investment;
 - c. The due diligence report must be compiled in the prescribed format;
 - d. The due diligence report must be signed by the account manager and the responsible manager.
- vi. Submission
 - a. The due diligence report is submitted to the relevant decision making body for consideration;
 - b. The final decision making body can only consider such due diligence report if it is signed by both the account manager and the relevant manager.
- vii. Implementation
 - a. The Account Manager is responsible to collate all the required information from the client and deliver same to the implementation officer;
 - b. The relevant business plan should be part of the loan agreement and should therefore be signed by an authorized member of the Co-Op when signing the loan agreement;
 - c. Implementation Officer must ensure that all the legal requirements pertaining to an investment is met. If required he has to consult with ECDC legal advisor;
 - d. Payment is only effected after all securities are in place and conditions precedent have been met and all documentation is checked and verified by the relevant Account Manager, Manager Co-Op Investments and the Implementation Officer;
- viii. Aftercare
 - a. Collect Monthly Accounts
 - i. Account managers must collect monthly management accounts from Co-Op Investments in their care;

- ii. If monthly management accounts are not submitted by the Co-Op client it constitutes a breach of agreement and such Co-Op client must be given written notice to such effect and warned of possible cancellation of agreement;
 - iii. Account managers must analyse these monthly management accounts and inform the relevant decision making body immediately of any significant deterioration in the financial affairs of such investments;
 - b. Quarterly Visits & Reports
 - i. Account managers must visit their allocated Co-Op Investment clients each quarter;
 - ii. Account Managers must submit a progress report in the prescribed format to the relevant decision making body after each such visit.
- b. Re-advances**
 - i. Application for re-advances on existing investments must follow the application process as outlined in this document.
- c. Presentation of Co-Op Investment Opportunities**
 - i. All presentations of investment opportunities must be made to the relevant decision making bodies by the Account Manager responsible for initiating the investment.
- d. Format of Investment Submission Papers**
 - i. All presentations submitted to the relevant decision making bodies shall be in the prescribed format as approved by the executive manager investments from time to time

19. Guidelines for Policy Deviation

- a. All Co-Op Investments deviating from the Co-Op Investment policy requires the next level of approval for such deviation;

20. Review and update

- a. All policies and procedures pertaining to Co-Op Investments shall be reviewed and updated on a regular basis;
- b. Such review and updating of these policies are the responsibility of the relevant investment committees;
- c. All additions, deletions and amendments to these policies shall be approved by the Board of the ECDC.