

The Treasury

South Canterbury Finance Limited Information Release

Release Document

April 2011

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Key to sections of the Official Information Act 1982 under which information has been withheld.

Certain information in this document has been withheld under one or more of the following sections of the Official Information Act, as applicable:

- [1] 9(2)(a) - to protect the privacy of natural persons, including deceased people
- [2] 9(2)(b)(i) - to protect trade secrets
- [3] 9(2)(b)(ii) - to avoid unreasonable prejudice to the commercial position of the person who supplied the information or who is the subject of the information
- [4] 9(2)(ba) - to protect information that is subject to an obligation of confidence, or that was or could be provided under legal compulsion, where making the information available would be likely to prejudice the supply of similar information and it is in the public interest for that information to continue to be supplied
- [5] 9(2)(d) - to avoid prejudice to the substantial economic interests of New Zealand
- [6] 9(2)(g)(i) - to maintain the effective conduct of public affairs through the free and frank expression of opinions
- [7] 9(2)(h) - to maintain legal professional privilege
- [8] 9(2)(i) - to enable the Crown to carry out commercial activities without disadvantage or prejudice.

Where information has been withheld, a numbered reference to the applicable section of the Official Information Act has been made, as listed above. For example, an [8] appearing where information has been withheld in a release document refers to section 9(2)(i).

In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.

From: Douglas Widdowson^[1]
Sent: Thursday, 7 May 2009 11:57 a.m.
To: John Park; Kathryn McBride; Peter Wilding; Stephen Reville; Craig Murphy
Cc: Andy Wood; Joanna Gordon; Peter Williams; Andrew Hemphill
Subject: [SEEMAIL] [SENSITIVE] Watchlist Reports for top finance companies - February
Attachments: Watchlist report - SCF - Tsy supplied data.pdf;
[Remainder of attachments not relevant to release]

John

As promised, the sector watchlist reports on the highest risk and highest impact finance companies as at the end of February. Equitable Mortgages still awaits completion. These reports should be read in conjunction with the reports provided at January.

Regards

Doug

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This message does not necessarily reflect the views of the Reserve Bank of New Zealand. If the recipient has any concerns about the content of this message they should seek alternative confirmation from the Reserve Bank of New Zealand."

South Canterbury Finance Ltd (SCF) – February 2009

Board Members ¹ :	Allan Hubbard (Chairman), Robert White, Edward Sullivan, Stuart Nattrass
Management:	Lachie McLeod
Trustee:	Trustee Executors
Guaranteed Deposits (\$)	\$1.9B
Deposit holders (#)	35k

Ownership

SCF is a wholly owned subsidiary of **Southbury Group Limited** (Southbury) - controlled by Allan Hubbard via his 70% shareholding.

Southbury also has interests in the following subsidiaries:

- **Scale Corporation Limited** – controlled by Hubbard interests with 83% of the shares held by Rangitata Plains Farms Limited (100% owned by Hubbard), Southbury Group and Hubbard personally.

Scale Corporation in turn owns:

- Mr Apple New Zealand Limited
- Polarcold Stores Limited which in turn owns:
 - Whakatu Coldstores Limited
 - Liqueo Bulk Storage Limited

The group is involved in the following:

- Shipping
- Cool storage – 164,000 tonnes
- Apple production (NZ largest producer)
- Liquid bulk storage
- **Helicopter (NZ) Limited** – controlled by Hubbard interests with 100% shares held by Southbury and Hornchurch Limited (owned 100% by SCF). Helicopter NZ owns and operates 41 helicopters.
- **Dairy Holdings Limited** – controlled by Hubbard interests with 59% of the shares held by Southbury & 3 American registered companies all with addresses at 39 George St, Timaru (Hubbard's office address). Dairy Holdings in turn owns:
 - Clumber Farms Limited
 - West Coast Dairy Limited

The group owns and operates 58 dairy units on 17,500 ha milking 45,382 cows and producing 15.3m kg of milk solids (15.3m x \$6 = \$91.8m gross revenues)

In addition to the above investments Southbury has interests in land holdings and a 4% interest in Pyne Gould Corporation (via SCF) which ultimately owns Marac Finance.

¹ No independent Board Members

Receivables

The following analysis is based on the data provided by SCF directly to The Treasury on 1st May 2009. The data provided is as at 31 March 2009.

There is concern that the information provided differs to the monthly reports provided to the Bank from the Trustee - in particular, the split of 1st and 2nd mortgages and the level of arrears/ impaired assets.

SCF's loan book size is ~\$1.53b with ~11,000 loan facilities and an average loan size of \$138k.

Concentration

The largest exposure of \$75M was made to the parent, Southbury Ltd. Security for this facility consists of a general charge over the entity, the remaining loan terms are unknown.

There are 35 facilities > \$10M (summary below) and 220 facilities > \$1M.

Borrower	Amount	RBNZ Comment	Security
[3]			

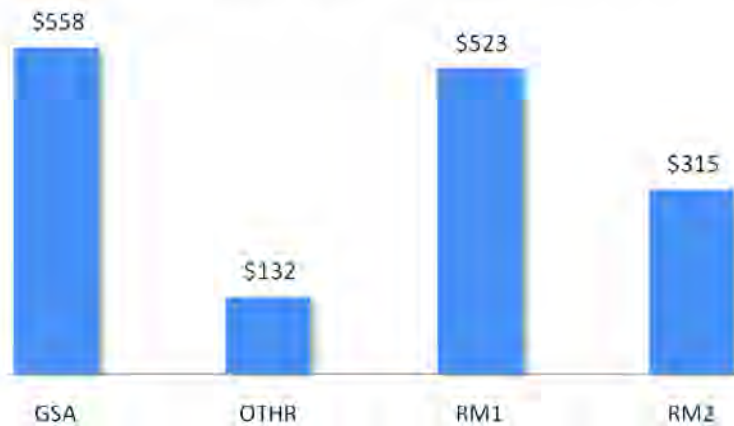
[3]

In Total, there are \$653M of loans with exposures above \$10M – representing ~43% of the total loan book. Of the loans reviewed above, \$151M were advanced to related parties, representing ~10% of the total loan book. Based on monthly RBNZ returns, total related party lending is circa \$200M or ~ 13% of the loan book.

Security charges

The following table details the various security instruments over the SCF loan book.

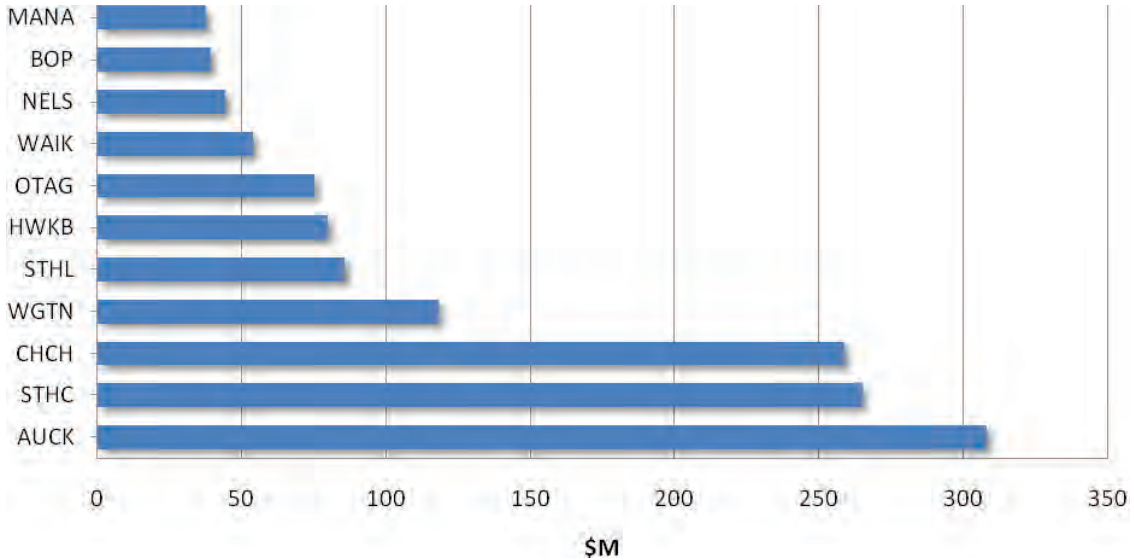
For the Property related sector, 58% is secured by 1st Mortgage, 32% is secured by 2nd Mortgage, 8% is secured by General Security agreement and 2% is “other/unsecured”.



Geographic

The following table covers 90% of the SCF loan book. The majority of the lending has been advanced in the Auckland, South Canterbury and Christchurch districts.

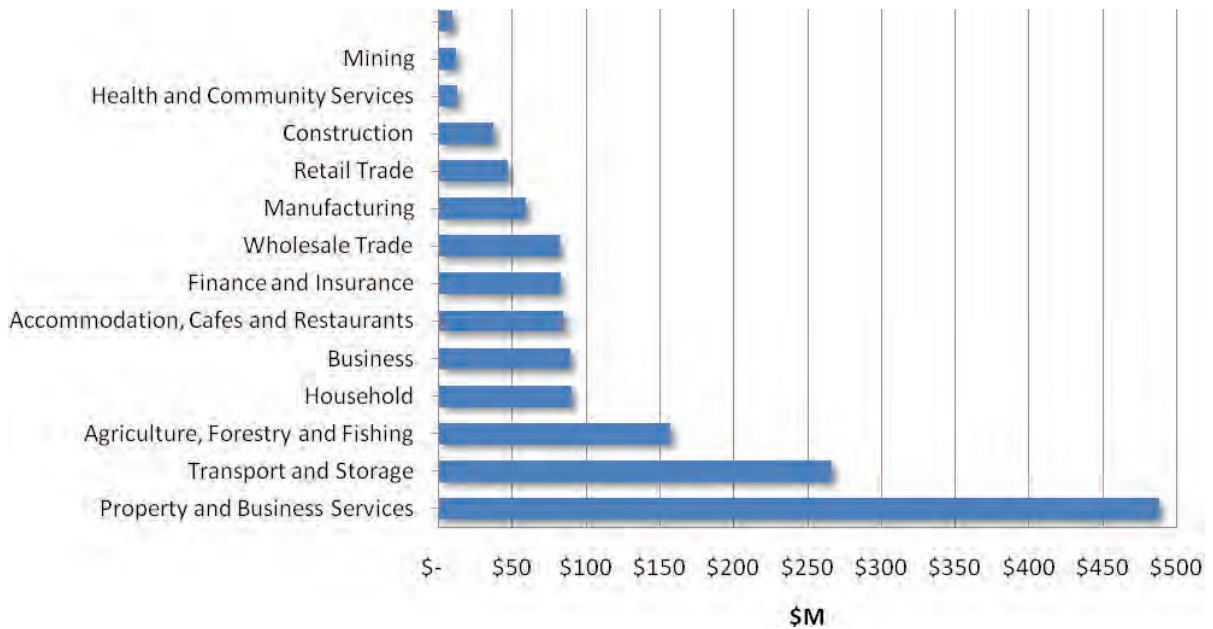
It is worth noting that the smaller districts of Southland and Hawkes Bay had combined lending of ~\$170m.



Sector

The largest sector serviced by SCF is “Property and Business Services”, of which, Property Developers represented ~\$330m, Property Services represented ~\$100m and Business Services represented ~\$50m.

The next largest sectors are Rural and Transport with a combined portfolio of ~\$420m.



Note. 15% of the loan book (~\$230M) had sector classification as “unknown”, for the purposes of this report, the receivables classified as “unknown” were allocated to the remaining sectors proportionate to their current weighting.

Circa 80% of Property Development loans are concentrated in Auckland, Wellington, Christchurch or Waikato.

SCF's traditional source for lending is within the South Canterbury, Southland and Otago districts. Excluding a \$75M related loan facility to Southbury Ltd, this demographic comprises ~23% (~\$350M) of the SCF loan book, including ~125M for the Rural and Transport sectors comprising.

Loan Book performance

SCF Impaired assets are recorded at \$180M, representing ~12% of the total loan book. Of these Impaired Assets, SCF have provisioned for ~\$16M. \$90M of these impaired assets have Registered 1st Mortgages as security.

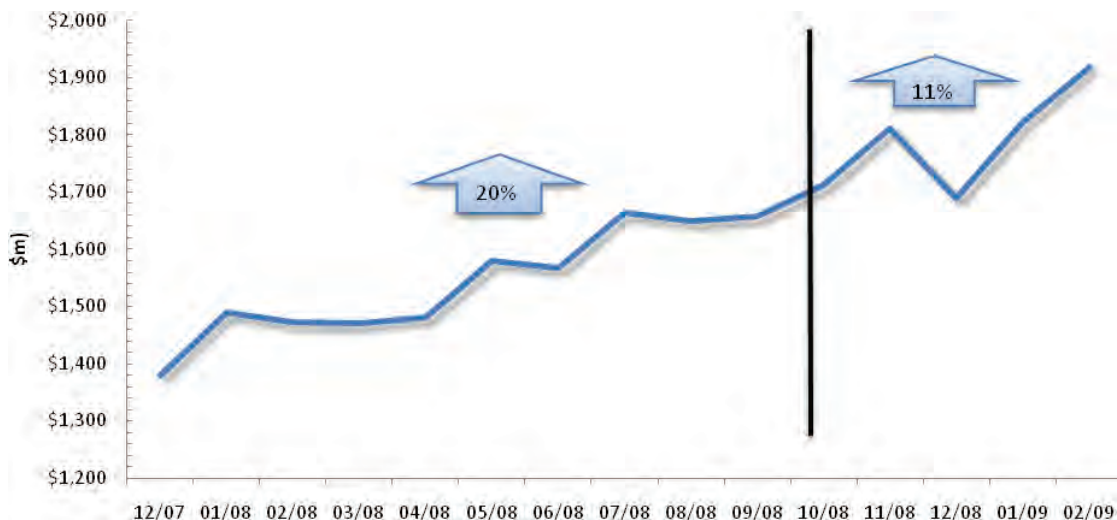
SCF have a further \$113M of "past due" assets, representing ~7% of the total loan book. None of these facilities have provisions held against them.

It is noted that this information provided directly from SCF to the Treasury differs to the monthly Reserve Bank return provided by the Trustee which stated Impaired Assets were \$164M and Past Due Assets were \$82M.

50% of all Impaired and Past Due assets are to the Property Development sector. The Transport and Rural sectors comprise ~10% of all Impaired and Past Due assets.

Liquidity

The following graph details the inflows for SCF, both post and pre introduction of the DGS. It is reasonable to assume that investor confidence in SCF is higher than that observed with other Finance Companies. Whilst the introduction of the DGS has had a positive impact on the level of net inflows, there was no identified negative trend leading up to that point.



The following graph demonstrates that SCF has a reasonable match-funded position. Further, they have cash assets of ~\$300M and a undrawn bank funding line of \$125M.



Estimated Loss to the Crown

When calculating estimated loss, the following assumptions are made:

1. A 30% Probability of Default is applied to each loan in the loan portfolio
2. A 30% LGD is applied to loans with 1st Registered Mortgages, a 65% LGD applied to loans with GSA security and 80% LGD applied to all other lending.

By applying the above assumptions, the loan book value is discounted from \$1.5b to \$1.25b

Other discounts are applied to various assets of the company, including a 90% discount to Fixed Assets and a 75% discount to Equity investments.

Total Assets are discounted to \$1.6b and Liabilities currently stand at \$2.1b, including \$1.9b of guaranteed deposits.

It is assumed that the Crown will share 90% of the total loss, with the remaining creditors sharing the remaining 10%.

It is therefore estimated, that in the event SCF would fail, the claim on the Crown under the DGS is between **\$400M - \$500M**.

Summary

- + Delinquency and Impaired Assets are reasonable against peers.
- + Modest level of facilities with interest capitalised.
- + Q1 09 profitability represents ~ 13% ROE - Whilst considered modest given asset quality and low levels of equity and provisions, it is reasonable comparative to peers / environment.
- + Reasonable liquidity / match funding position

- Concentration / Large exposures – 81% of the book has loan sizes > \$1M
- High level of exposure to property development
- Modest levels of Loss Provisions held.

- High level of related party lending – 13% of loan book.
- The practice of transferring assets between related or connected entities does not have full transparency and may not always be in the best interest of the creditors.
- Modest and diminishing Capital position – ~5% to ~6% ratio after Risk Weighting adjustments.
- Consistency and accuracy of data
- In the event SCF fails, the estimated claim under the Crown guarantee is circa \$485m