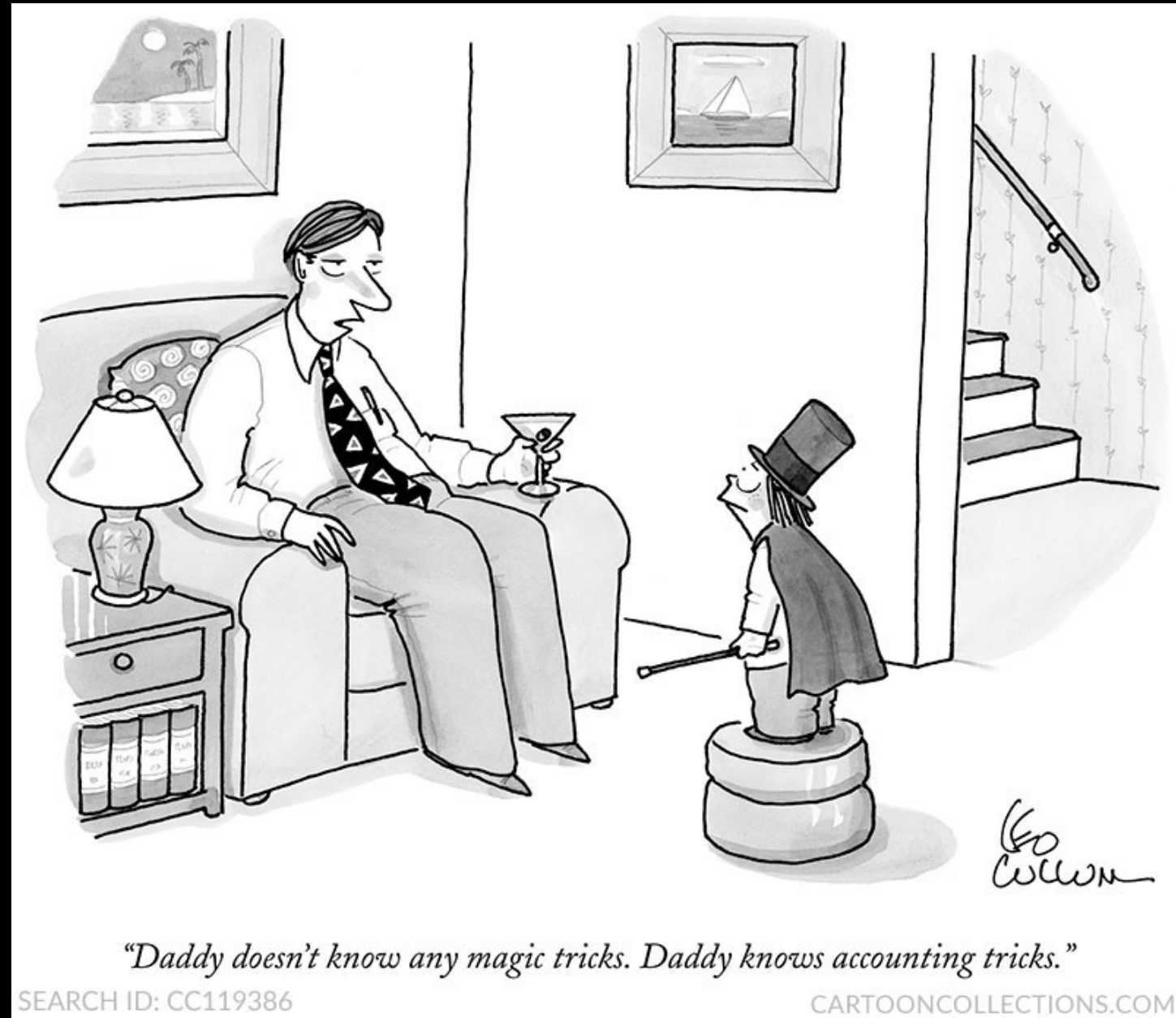


*ALLAN GRAY: PUTTING THE 'G' IN ESG*

# LESSONS FROM SA - FROM STEINHOFF TO TONGAAT

# STATE OF PLAY

- A rash of failures has exposed brittle governance, weak auditors, and suppliant boards
- Early cases - *Tigon*, *Regal Bank*, *Brett Kebble*
- More recent cases - *Steinhoff*, *Tongaat Hullett*, *EOH* and *VBS Mutual Bank*



“South Africa had an unblemished reputation among emerging markets for having the strongest management and ethical corporate standards. Now, after Steinhoff, it creates the impression that we’re no longer first among equals – we’re no different from other emerging markets where there are issues”

*–NICKY NEWTON-KING,  
FORMER CEO OF THE JSE*







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Zimbabwe: US\$5



## The Fall of a Stellenbosch Don

Inside Steinhoff's  
house of cards

'Don't ask me about my business'  
— Michael Corleone, The Godfather

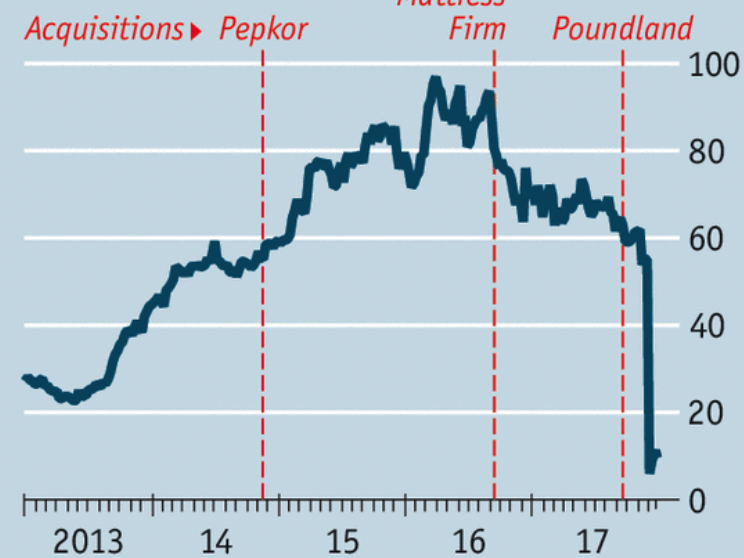
Inside

SA's best  
and worst  
suburbs P18

Flip over  
for SA in 2018

## In for a penny, in for a pound

Steinhoff International share price  
South African rand

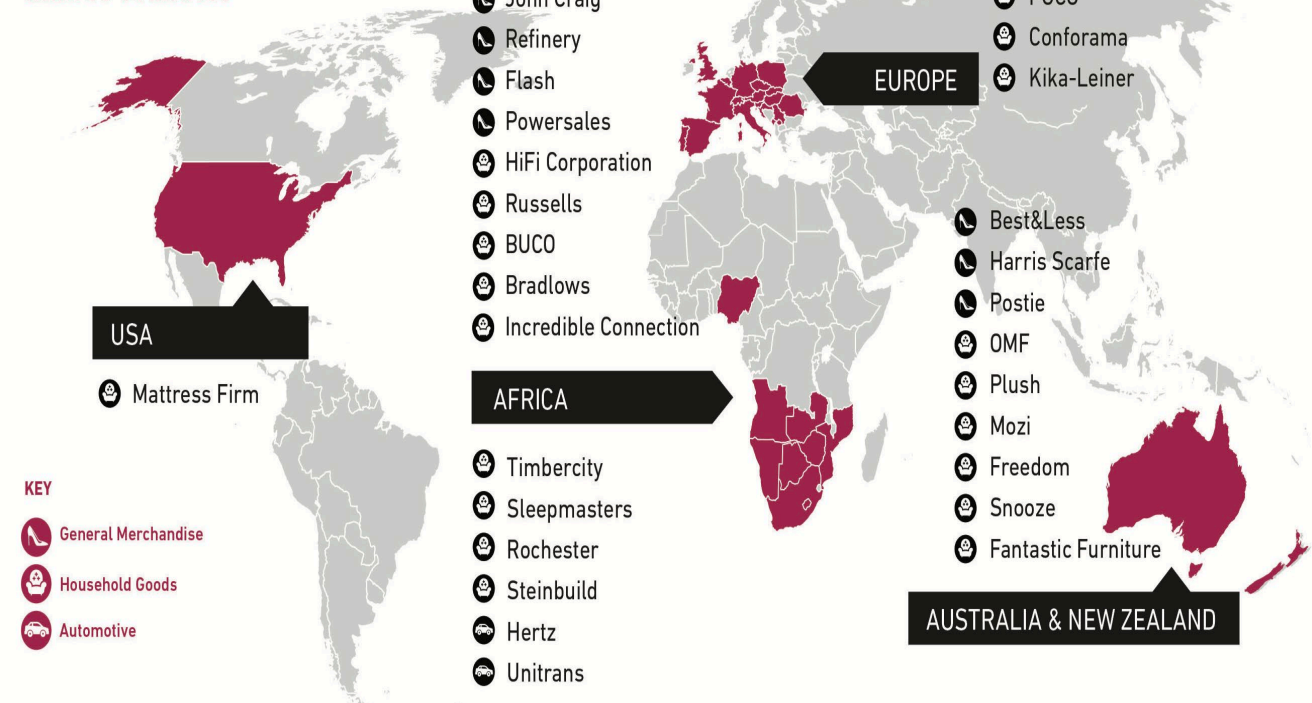


Economist.com



STEINHOFF  
INTERNATIONAL HOLDINGS N.V.

Before the December 2017 crash  
it was a global business empire  
with about **130 000** employees  
and **11 000** retail outlets in more  
than **30** countries



“We have reason to believe Steinhoff’s management have been defrauding the company for years”

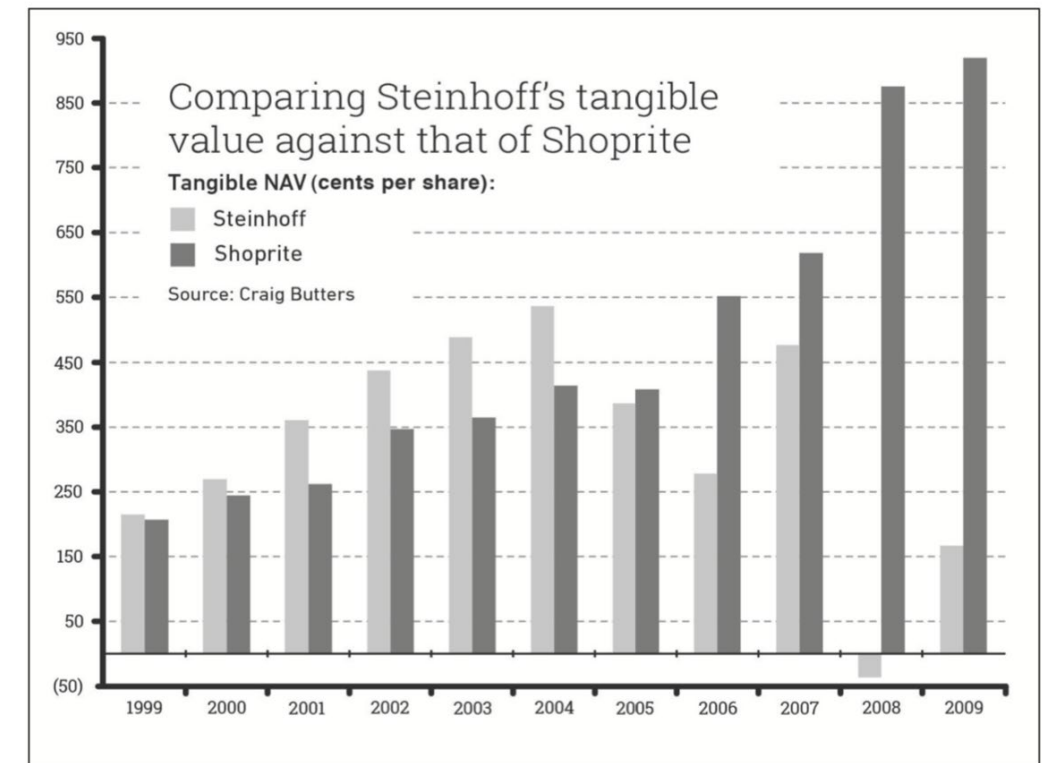
*–DELOITTE AUDITORS TO CHAIR  
CHRISTO WIESE, 29 NOV 2017,  
ONE WEEK BEFORE MARKUS JOOSTE  
RESIGNED*



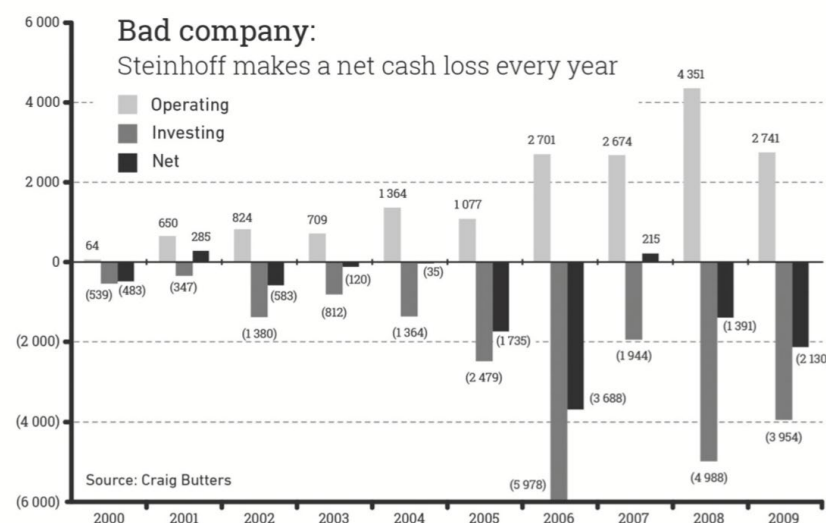
# RED FLAGS (1)

- Steinhoff had a superstar board with three PhDs in accounting - yet it had SA's worst accounting scandal
- In the end, R106bn of "fictitious and/or irregular transactions" over more than a decade . Assets worth R246bn had to be impaired

Comparing Steinhoff's (SHF) tangible value with that of Shoprite (SHP)



Bad company: Steinhoff generates negative cash flows every year . . .



Effective tax rates of Steinhoff and acquired entities

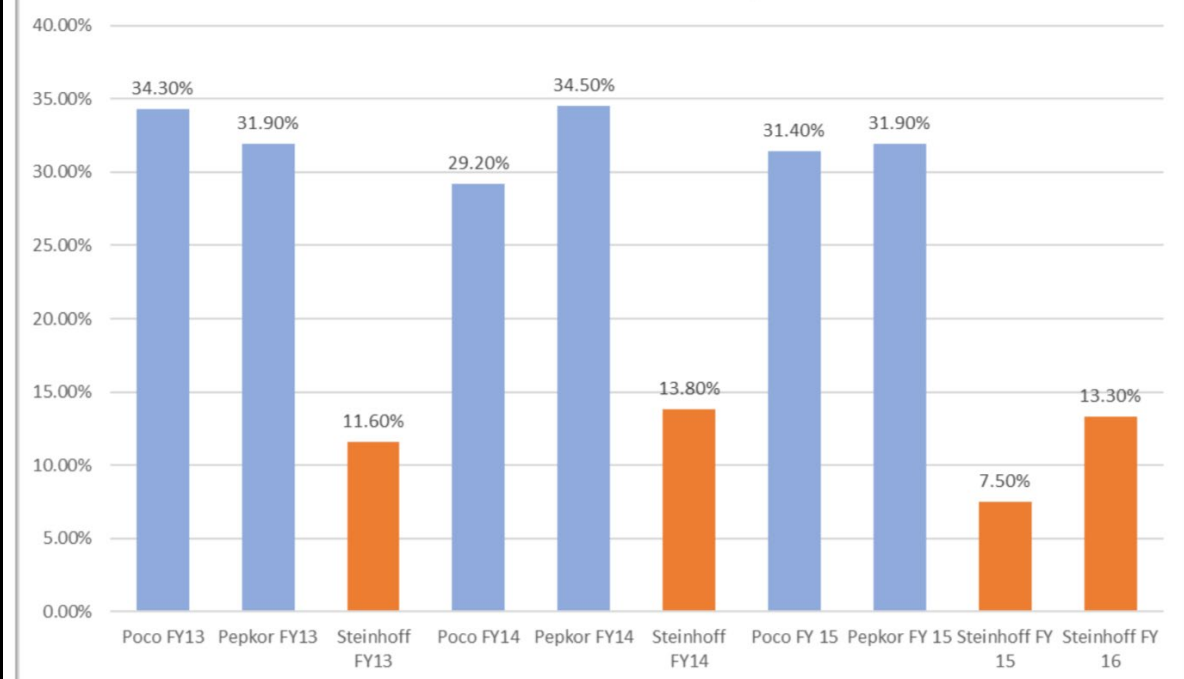


Figure 44 Effective tax rates of Steinhoff and acquired entities



# RED FLAGS (2)

- Immense undisclosed related party deals
- Off balance sheet deals in Europe - Champion
- Lifestyle of the CEO didn't match remuneration



Behavior	Comment
Cash flow does not match earnings?	They bear no resemblance
Hide losses via discontinued operations?	Carried JD as discontinued for over 2 years
Aggressive and irrational acquisition spree?	Poundland, Darty, Mattress Firm
Change in financial year for no reason?	Yes
Change in divisions to make comparisons difficult?	Yes
Undisclosed associated party dealings?	Campion Capital, Siegmur Schmidt
Odd investments?	EUR 1.2bn "loans to Chinese suppliers"



“At every single board meeting, the directors grilled management ... we also insisted on reports from, and discussions with the auditors and the law firms. But the fact is, we were simply lied to”

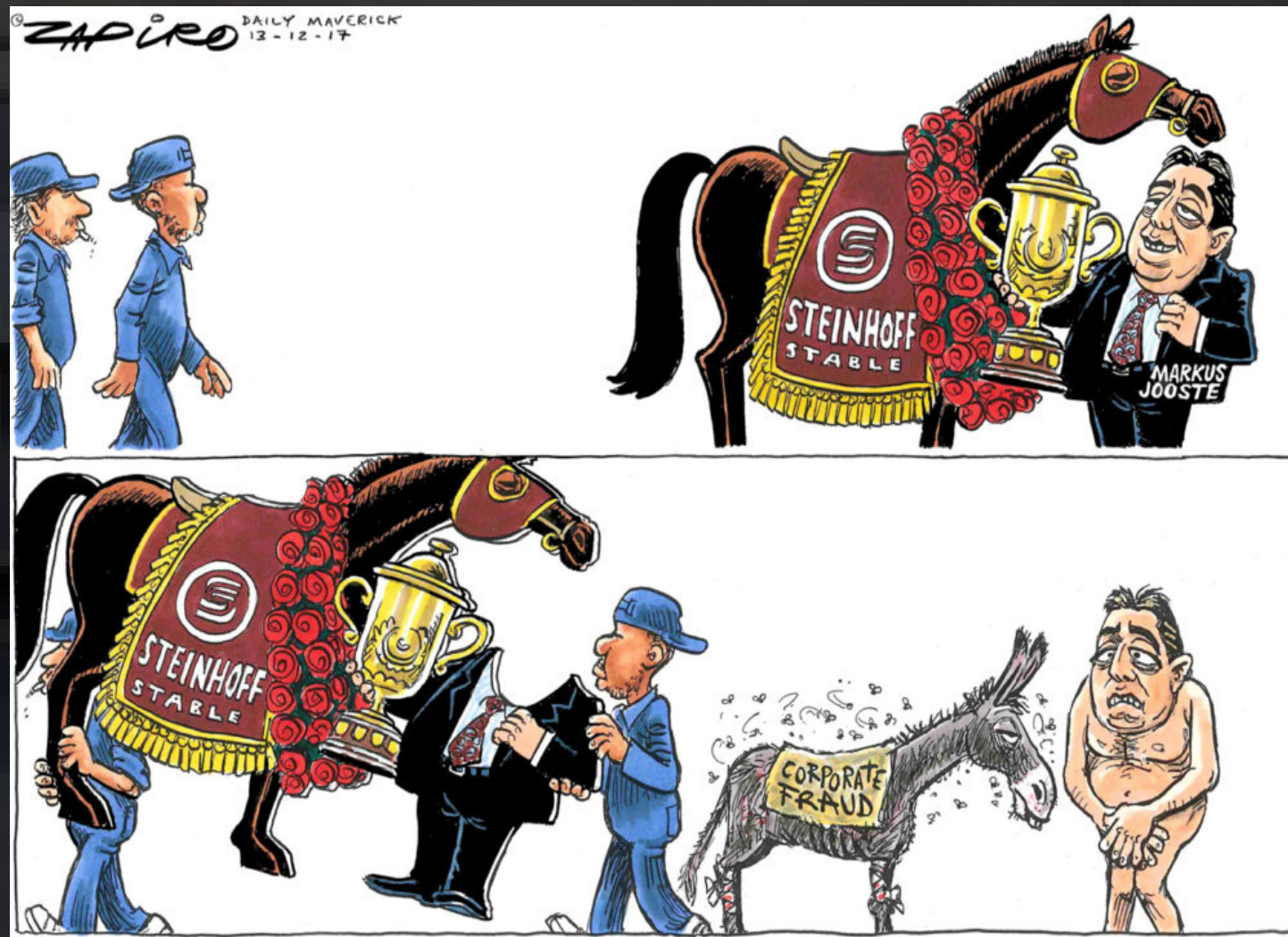
—FORMER STEINHOFF DIRECTOR JOHAN  
VAN ZYL





“Almost everyone you  
ever met at Steinhoff was  
an accountant. There  
was only ever one  
perspective”

- *STEINHOFF CHAIR HEATHER  
SONN, 2018*



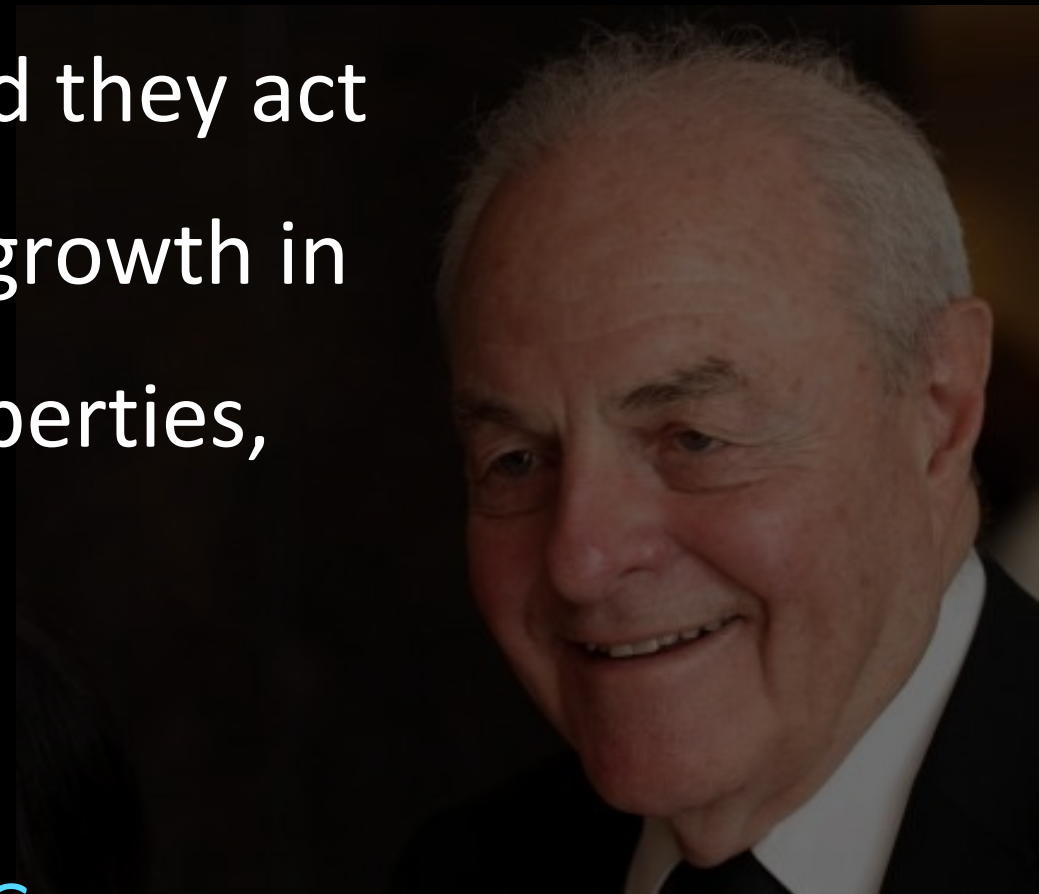
Steinhoff's culture "consists of people who trust each other blind ... we think alike, we operate alike, we respect alike, and we like alike"

- ACCOUNTANT WHO WORKED AT STEINHOFF, PRE-2013

# *Were Steinhoff's directors "sufficiently sceptical?"*

“Ultimately, it’ll be a question of fact. Did they see things that were red flags? And did they act on it? For example, was the constant growth in revaluation of subsidiaries, of the properties, was that a red flag?”

— PROF MERVYN KING





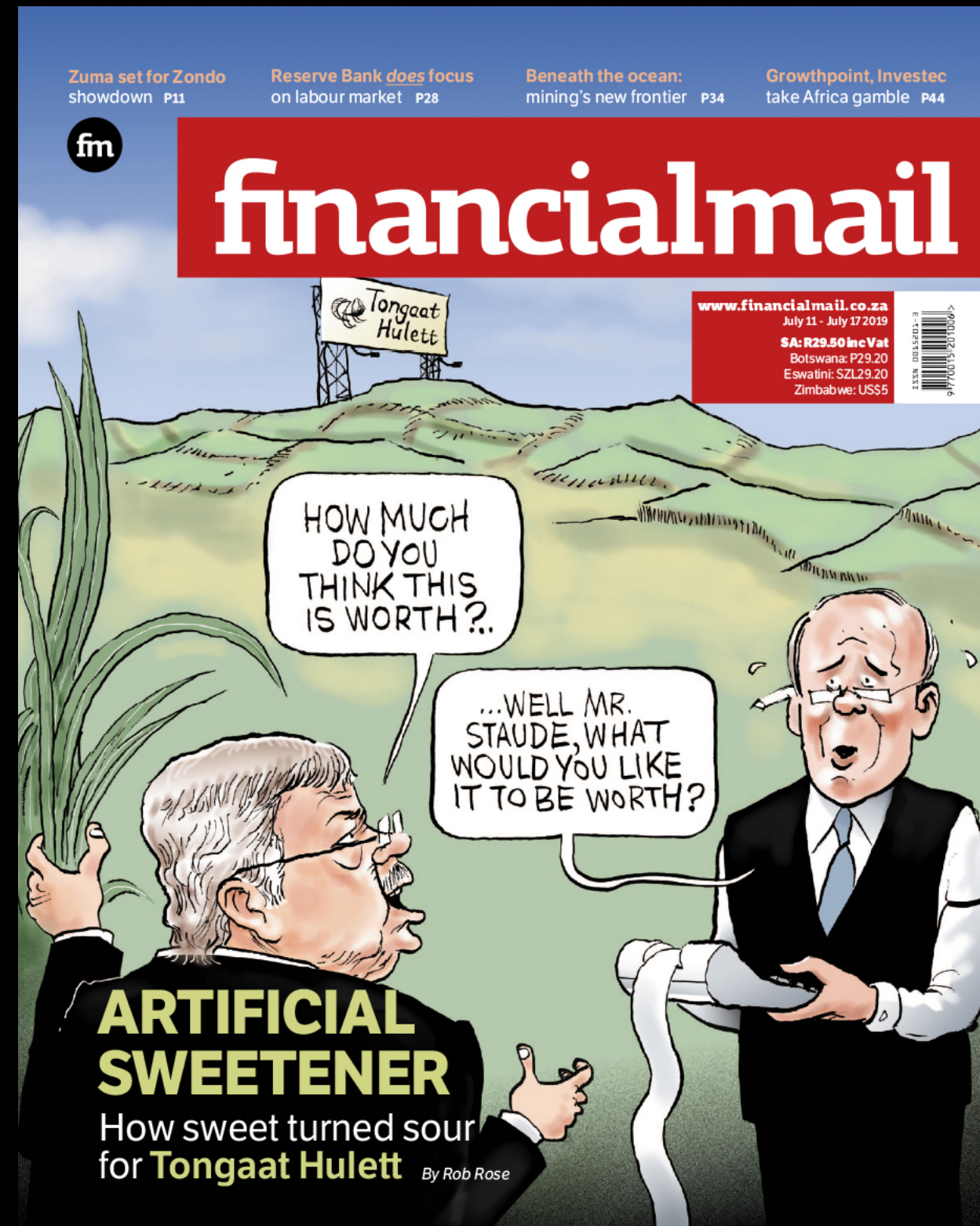
STEINHOFF'S FRANKFURT  
LISTING, DECEMBER 2015





# THE CASE OF TONGAAT HULETT

- R11.3bn of “restatements”. Operating profit fell from R1.95bn to R142m
- PwC: sugar cane roots were overvalued, land deals were backdated, and expenses capitalised
- CEO Gavin Hudson: “rather than making reality your friend and telling investors you have to ... cut costs, you do things in the hope that things will get better next year”



# TONGAAT AND GOVERNANCE



- PwC: “there was a culture of deference and lack of challenge at Tongaat that resulted in employees following instructions on accounting practices without questioning the basis for those accounting practices”
- Since 2014, Tongaat’s executive committee didn’t meet. Former CEO Peter Staude admitted this the FM. A weak board didn’t challenge this
- New CEO Gavin Hudson: “in most companies, goals are set and accountability is clear. At Tongaat, I’ve been surprised by the lack of management processes ... no minutes were taken, no actions points were put down for follow-up”
- Hudson: "The public at large should be holding companies to account, and asking more questions. Ultimately, everyone is a shareholder in these JSE-listed companies through our pension funds. We all have a role to play in keeping everyone honest”



# *THE MATRIX OF RED FLAGS*

- ❖ Weird control structures — Naspers, Shoprite
- ❖ Autocratic boss — Tongaat Hulett, Steinhoff, EOH
- ❖ Poor disclosure — Enron, Mirror Trading
- ❖ 'Too good to be true' syndrome — Barry Tannenbaum
- ❖ Too much 'paper activity' — Steinhoff, EOH
- ❖ Deals that don't make sense — Steinhoff
- ❖ Resignation of staff and auditors — Fifa, Blue Financial
- ❖ Cash flow v profit — Corpcapital, Steinhoff
- ❖ Excessive debt — Tongaat
- ❖ Politically-based deals — Trillian, Bosasa

WE ALWAYS  
INSIST THEY  
WEAR  
BLINKERS !

AUDITORS  
PROBED  
OVER  
STEINHOFF  
SCANDAL

JOOSTE

Deloitte.

