



Investec Asset Management (Pty) Limited
36 Hans Strijdom Avenue
Foreshore, Cape Town
South Africa 8001
Telephone: +27 (0) 21 416 2000
Facsimile: +27 (0) 21 416 2001
www.investecassetmanagement.com

28 January 2015

Attention: **AG Wicomb**
 Standing Committee on Finance

Submitted by: Investec Asset Management (Pty) Ltd
 Please note that we would like to present to the Committee in person during the hearing

Dear Sirs

RE: SUBMISSION REGARDING: BANKS AMENDMENT BILL

Retrospective changes to property rights will hurt pensioners & the whole SA economy

During the Global Financial Crisis (GFC) several governments were forced to use tax-payer money to bail out banks that had over-borrowed and had in turn made bad loans. In a bid to keep the financial system stable, they avoided putting banks into liquidation by injecting capital, thus preventing creditors from experiencing any loss. The resultant concern was that debt-holders were inadequately assessing the risks of a bank as they expected governments to bail out such institutions if they got into trouble.

Limiting tax-payer exposure to the banking sector

The Basel III regulations sought to prevent a recurrence of these events. The crux involved finding a mechanism by which banks could be rescued without imposing costs on the tax-payer. This meant providing the Resolution Authority – be that the Finance Minister or the Banks Regulator – with many of the powers they would historically have had under liquidation, under curatorship. Therefore the regulator could restructure a bank while minimising the risks to the financial system.

As such, the new style sub-ordinated debt became “bail-in-able.” This meant that the regulator could permanently convert the debt to equity or write it off at their discretion, once they believed an institution was at or rapidly approaching the Point of Non-Viability.

These developments make sense given the events of the GFC. There were several issuances of this new style capital by the big four South African banks through 2014.

Old style Tier II debt had much greater protections than New style Tier II debt

However, old style sub-ordinated debt otherwise known as Tier II debt, issued prior to 2014 that conformed to Basel II is not equivalent to the new style debt. The old style debt enjoys far greater protections. As a result, the interest rate investors charged to buy old style debt was notably lower than that charged for new style debt. Such protections include the fact that old style Tier II debt is not bail-in-able and therefore cannot be converted to equity at the election of the regulator. Currently, the payment rights of old style Tier II debt ranks equal with other creditors of a bank prior to liquidation of the bank.

Curatorship is not equivalent to liquidation

The Banks Amendment Bill is attempting to nullify these rights of old style Tier II debt-holders – and retrospectively remove their equal right to payment outside of liquidation, effectively treating them as if they are new-style Tier II debt, which they are not. The Treasury is arguing that curatorship is equivalent to liquidation.

Result is losses for pensioners, higher interest rates and lower foreign investment

This is simply not true. The Treasury are attempting to use this piece of legislation to make it retrospectively true. The consequences will be as follows:

- Foreign investment will be deterred as investors worry about arbitrary changes to existing property and asset rights.
- Funding costs will rise for banks and other companies in South Africa, as investors realise that government is willing to rescind rights retrospectively.
- The SA economy will ultimately face higher borrowing costs as banks pass through the higher interest rates they are forced to pay onto consumers and businesses.
- In addition, savers in South Africa, workers in many pension funds, will suffer an unfair loss if this legislation is implemented retrospectively.

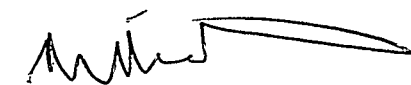
Conclusion

We support the National Treasury's aim of ensuring a sound financial system with minimal potential costs to the average tax-payer. However this cannot be done in a manner that completely sacrifices the property rights of an asset that was sold under a different legal and economic framework three to six years ago.

As a result, we support the solution that has been proposed by the Tier II Debtholder Committee.

Yours faithfully

Per:



Nazmeera Moola,
Economist and Strategist, Investments