ASISA

SUBMISSION TO STANDING COMMITTEE ON FINANCE

14 March 2017

ASISA is:

- An industry association representing the savings and insurance sectors.
- Empowered by a mandate from an industry that manages some R9 trillion of our nation's savings and investments.
- Our members are the majority of South Africa's asset managers, collective investment scheme management companies, linked investment service providers, multi-managers and life insurance companies. (127 member companies).
- Members manage the long-term savings and investments of customers in the following regulated product ranges:
    - Pension and provident funds
    - Retirement annuities
    - Endowment policies
    - Collective Investment Schemes (unit trusts, exchange traded funds, hedge funds)
    - Risk protection policies such as life, disability and dread disease cover

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CONTEXT

This document has been prepared as a written submission in response to the request by the Standing Committee on Finance for stakeholders to make comments on the transformation of the Financial Sector. The invitation specifically refers to a focus on "deracialising; high level of monopoly; progress on implementation of the Financial Sector Code and other related matters".

The Financial Sector is often considered to be synonymous with "banks". We would like to emphasize the role and importance of other financial institutions, alongside the banks, in the successful operation of the Financial Sector in contributing to a vibrant and growing economy. As of June 2016 the largest four banks in SA had capital of approximately R 465 billion. They had also taken deposits amounting to R 4.7 trillion from depositors including the savings industry. This allowed them to advance loans and other forms of financing amounting to some R 5.2 trillion. The savings and insurance sector, by way of comparison, is almost twice as large having taken in and deployed R 9.4 trillion of savings.

ASISA, as an industry body representing the savings, investments and life insurance industry, hereby makes a written submission on behalf of its members and also wishes to make an oral submission to the committee.

IN SUMMARY

This submission concludes that in our view:

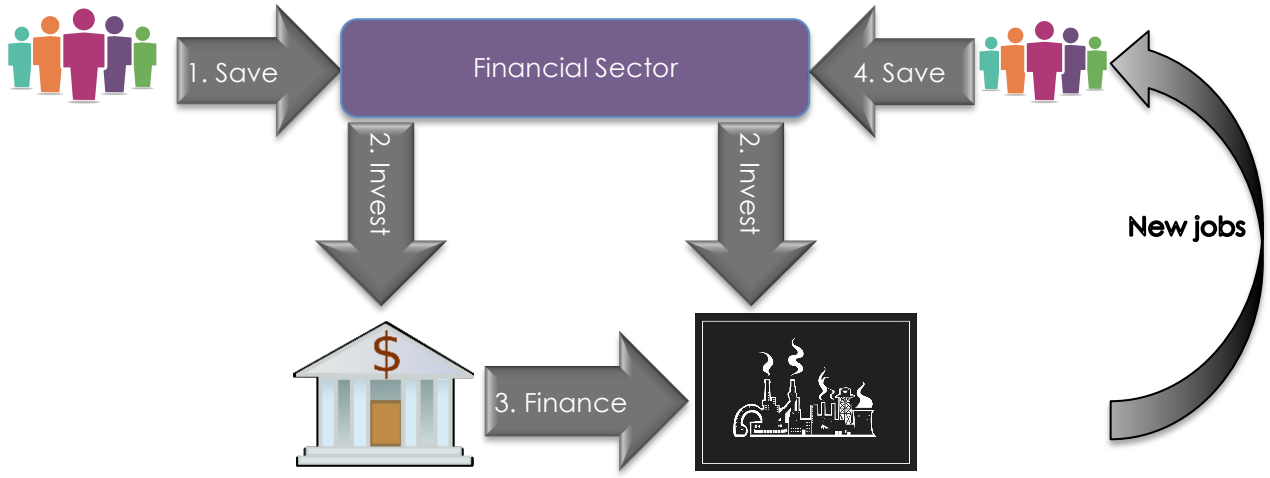
- The savings industry acts as custodian for assets belonging to savers. It also mobilises these savings deploying them into productive enterprise that, in turn, creates more jobs, wealth and then more savings in a virtuous circle. This circle creates ownership of SA assets by ordinary citizens building their wealth.
- The South African financial sector performs well on international standards and is regarded as being efficient, trustworthy and inspires confidence.
- The size of our large institutions should not be confused with monopolistic activities. Our institutions are large but not monopolistic. This size is needed for growth and stability. Large savings pools are needed for funding of large growing institutions and this growth is best supported by collective pools of savings rather than individual shareholders.
- The savings and insurance sector has made good progress in transformation. It has met many of the transformative goals of the FSC. Where we have not yet reached the targets, we have put measures in place to fast track our progress towards meeting and exceeding these goals.
- We have consistently urged coherence in policy, legislation and regulation which recognises the developmental needs of our country in terms of the NDP.

SECTION A – FINANCIAL SECTOR PLAYS A VITAL ROLE IN THE ECONOMY

Classical economics teaches that factors of production are Labour, Land and Capital. The capital needed to fund new economic activity has traditionally come from banks. However, in the last five decades or so, the role of the savings industry has risen dramatically in prominence in the funding of economic enterprise.

As people have expended their labour to earn wages, so they have become wealthier and chosen to save some of their wages for the future – either to be used in a time of crisis, or to be saved for their retirement. This savings cycle may be depicted as follows:

The virtuous savings circle:



As may be seen above, the financial sector plays a vital role in aggregating the savings of individuals and organisations and then re-deploying those savings to

1. Help grow the economy by mobilising those savings for reinvestment, and
2. Protecting those savings for future needs, be that for emergency or for retirement.

SOUTH AFRICAN FINANCIAL SECTOR PERFORMS WELL INTERNATIONALLY

Any financial sector needs credibility and stability without which people will not save or invest. One need only look at the many financial crises that have occurred in the past for practical evidence of the effects of a lack of trust in the financial system. It is for this reason that the SA financial system has been built in the way that it has.

In the context of the World Competitiveness Report for 2016 South Africa improved its rating by 7 places from 56 to 49 relative to 2014/5. The President and Cabinet issued a statement commending this performance.

It is interesting to note the performance of the South African Financial Sector in this regard. Today SA easily ranks in the top ten financial systems in the world when considering the level of efficiency, trustworthiness and confidence of the financial market. This places SA ahead of respected economies like Norway, the USA and the UK. This is an impressive feat and has allowed SA to develop a sophisticated financial system given the developing nature of the country. This brings many positive benefits to the country including:

1. Relatively inexpensive borrowing to fund infrastructure and socio-economic development (emphasising the need for fiscal discipline and stability)
2. Foreign investment to grow the economy (emphasising the need to protect our credit rating)
3. Liquid investment markets allowing for the growth of the savings and pensions of our citizens (emphasising the need for stability and governance in the financial sector)

As South Africans we can be proud that South Africa rated number 7 out of 144 as regards efficiency, trustworthiness and confidence of the financial market. It rated number 6 out of 140 on availability of financial services (refer attached graphics).

FINANCIAL SYSTEM RANKING (for the level of efficiency, trustworthiness and confidence of the financial market – World Economic Forum Competitiveness Report 2015)

COUNTRY	**RANK** (out of 144)
Hong Kong SAR	1
Singapore	2
New Zealand	3
Malaysia	4
Finland	5
Australia	6
South Africa	**7**
Canada	8
United States	9
Norway	10

The South African financial market ranks particularly highly as regards its competitiveness in relation to 140 other economies. This makes it a more desirable destination for foreign investment and borrowings than many emerging markets.

FACTOR	**RANK** (out of 140)
Availability of financial services	6
Financing through local equity market	1
Soundness of banks	8
Regulations of security exchanges	2
Overall financial market development	**12**

The sophistication, stability, efficiency and governance of the SA market has attracted investment and allowed SA access to relatively inexpensive capital to grow the economy and protect savings. This is evidenced by the fact that foreign investors hold approximately 39% of the JSE shares and 30% of South African bonds in issue.

WHY THE FINANCIAL SECTOR IS NEEDED

As mentioned above, the financial sector plays two roles in the SA economy – it acts as a custodian for peoples' assets and it facilitates the mobility of savings from those who save to those who need financing and capital. These two roles are both vital but their distinction is important. In general, the banks provide financing and credit while the savings and investment industry acts as a custodian for people's long-term savings. These arrangements often last many years and in some instances multiple decades.

In South Africa the savings industry may direct investments in support of Government, the State Owned Companies and local authorities in the development of infrastructure. This could also be providing funding for the corporate sector for developmental initiatives. The savings of people are mobilized through well-regulated product pools. (See figure 1 below).

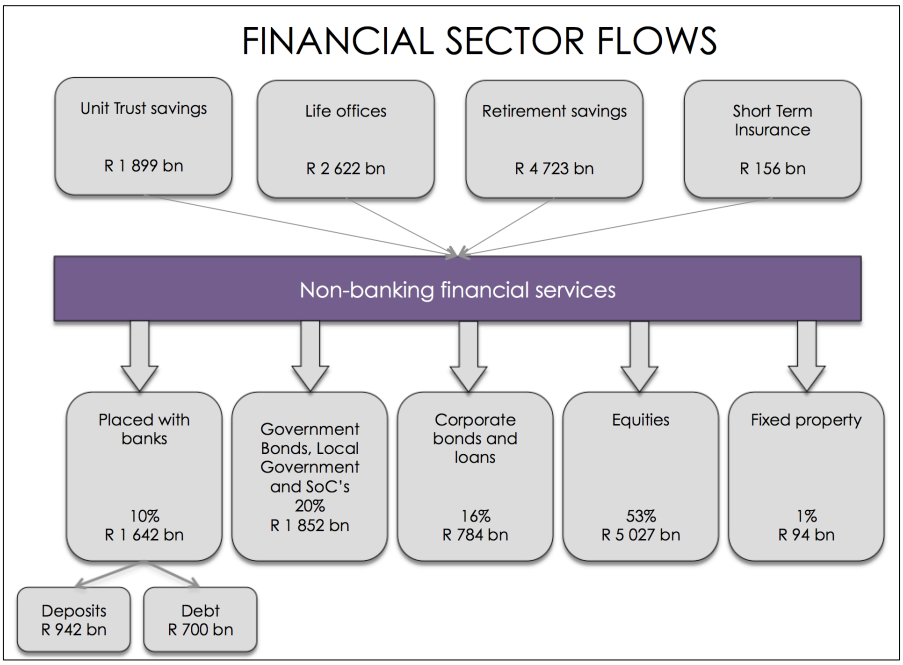


Figure 1: Source SARB Quarterly Report 30 June 2016

Some headline statistics are relevant in this regard:

- Unit Trusts: R1.9 trillion invested by 5,7 million account holders.
- Retirement Funds: R4.7 trillion invested representing the retirement savings of 16 million members.
- Investment managers have generated positive returns for the members of pension funds over the past 20 years. For example, R 100 invested 20 years ago would be worth R 1 430 today. (Source: Alexander Forbes Global Large Manager Watch)
- Life Offices: R2.6 trillion representing 33 million policies. Benefits paid in 2015 amounted to R429 billion.

- The total liabilities to policyholders at 31 December 2015 amounted to R2.4 trillion which was covered by assets of R2.6 trillion.
- Given the very long-term nature of these liabilities the Life Offices have to carry additional capital in terms of Capital Adequacy requirements (CAR) of R41 billion. The Life Office industry carries four times this required amount – R182 billion. This capital not only acts as a buffer against sudden economic downturn but is also fully invested in the economy.

The savings that are mobilized are deployed as follows:

- SA Government, Local Authorities and SoC's (R1.8 trillion):
  - Government - The savings sector holds R1.4 trillion of SA Government Bonds. This money is used by Government to facilitate infrastructure development and service delivery either directly or by the allocation to Provincial Governments or Local Authorities. Unfortunately currently some of this money is used to fund current expenditure i.e. salaries. The Minister of Finance has started addressing this in his last two budget speeches.
  - State Owned Companies: The savings sector has deployed R425 billion into bonds issued by State Owned Companies. This money is utilized in the delivery of infrastructure i.e. energy, transport, roads, water etc.
  - Local Authorities: Saving Sector has deployed R15 billion into bonds issued by the major local authorities. This is used for the development of infrastructure and service delivery.

- Other Investments - In addition to the above, ASISA members have deployed savings directly into various projects. This amount of R120 billion has been deployed as follows:
  - Renewable energy – The IPP has 31% black ownership and will generate R29 billion in dividends to black communities over the next 20 years
  - Township development
  - Affordable housing
  - Urban regeneration
  - Student accommodation
  - Water
  - Roads
  - Agriculture (emerging farmers)

The deployment of capital in various projects referred to above creates jobs, and in the context of infrastructure and service delivery, has a positive social impact.

- Corporate South Africa:
  - Corporate Bonds: Debt funding to the amount of R750 billion. This is to provide capital for expansion.
  - Investment in Shares: R5 trillion, a substantial portion of which is invested in listed shares.

- Banking Sector:
  - The savings sector has deployed R1.6 trillion into the banking Sector by way of cash, deposits and bank paper.
  - It should be noted that banks are not able to create money. They can only on-lend funds based on their depositor base. The money raised through the savings sector, private individuals and other entities is then on lent to ordinary people, Government, State Owned Companies, local authorities and the Corporate Sector.

Pools of money representing 33 million policies in force, 5.7 million unit trust account holders and 16 million members of retirement funds now become owners of listed South African companies. (See figure 2 below). The black portion of savings schemes as measured owns 23% of the shares in the top 100 companies listed on the JSE. Foreigners, mainly Pension Funds, own 39% of the top 100 companies (± R2 trillion).

JSE Top 100 shares	**% held**
SA Black ownership	**23%**
Direct Ownership	**10%**
- Strategic partners	6.0%
- Community Schemes	2.5%
- Employee Schemes	1.5%
Indirect ownership	**13.0%**
- Savings pools	13.0%

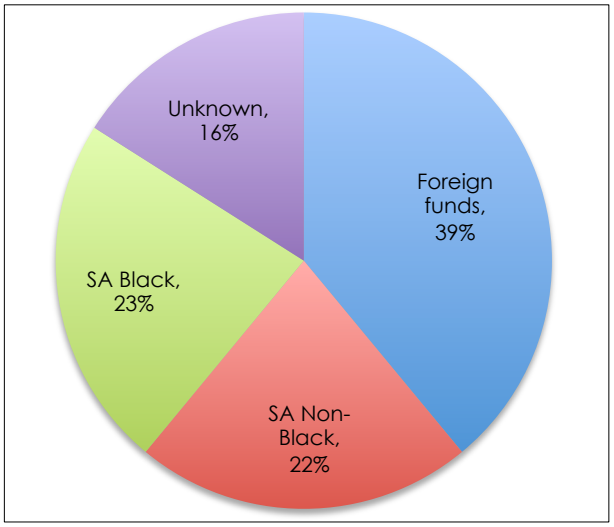


Figure 2 Ownership of JSE Top 100 shares

Please see Notes overleaf.

Notes:

- The ownership statistics above are per the JSE.
- The direct black ownership component has also been quoted by the President in his State of The Nation address on 9 February 2017 and the Minister in the Presidency in a recent speech. This has largely been achieved through BEE deals.
- The 23% quoted in the graphic, becomes 39% when the foreign operations are excluded as required by BEE legislation.
- The unknown component relates mostly to small pension funds with both black and white South African members.
- It should be noted that white individuals own less than 7% of JSE listed companies. Savings pools, both local and foreign, own the bulk of the JSE shares.
- In order to maintain and accelerate the momentum illustrated, it is important to constantly monitor the access to financial services and empowerment financing components of the Financial Sector Code.

In deploying this capital the savings industry must strike a fine balance between **protecting** the savings of the people and **investing** in the economy with a reasonable risk adjusted return. The long-term nature of these arrangements again emphasises governance and stability.

The South African financial sector performs well internationally. It is efficient, trustworthy and inspires confidence. It also plays a vital role in mobilising capital and protecting the savings of the majority of South Africans.

SECTION B – HIGH LEVEL OF MONOPOLY?

SOUTH AFRICAN FINANCIAL SECTOR MONOPOLY

The Standing Committee expressed concern as to the high level of monopoly in financial services. We question whether or not there is, in fact, a monopoly. We do recognise that while some firms are large, they are not monopolistic and that their scale allows them to fund the necessary growth.

Investment firms need scale to drive down costs to the consumer and to provide stability of their investment teams and process for the realisation of long-term investment returns. Insurance firms need scale to drive down costs to the consumer and to ensure longevity and capital needed for the support of long term insurance contracts. We have seen that firms in the savings and insurance sectors tend towards a structure of a few large players attracting the large pools of assets and many medium and smaller firms competing in specific niches. This may be as a result of a unique product or service offering by the smaller firm or because they are able to address a specific market niche not available to the larger player.

This structure is evidenced in mature markets (US, UK, Germany and Australia) as well as emerging markets (Nigeria and Kenya). The same structure has naturally formed in South Africa. These are not monopolistic as there is still fierce competition between the small number of large players and the many medium and smaller players. In this instance the large players should be viewed as a positive outcome as opposed to a monopoly, which is often viewed as a negative outcome.

As we have seen above, the large sizes of these institutions assists in at least three areas:

1. Capital to fund future liabilities and to provide stability to savers and to the market,
2. Capital to fund large scale investment such as is required by government for new bond issues or infrastructure projects, and
3. Scale to drive down costs to the consumer.

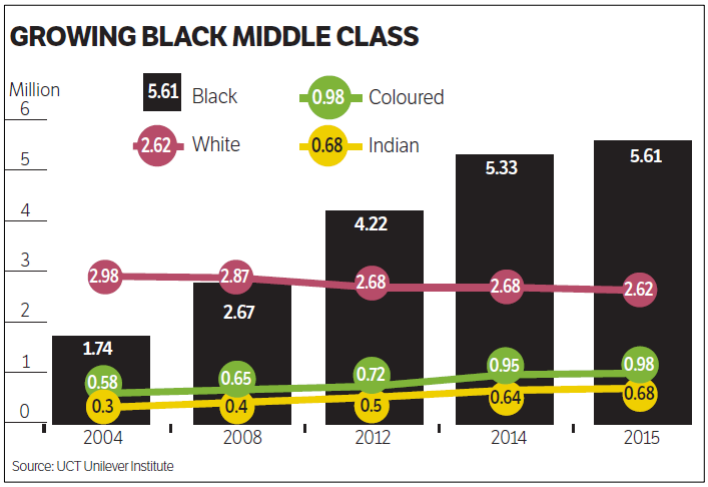
By aggregating large pools of savings, financial services companies are able to finance economic growth (in the form of investment in public investments or private investments). These activities assist in growing the economy and providing jobs to South Africans who, in turn, start building wealth and become the next generation of savers.

We are of the view that the SA market is large and not monopolistic. This reflects a positive competitive balance between a number larger, medium and smaller player to the benefit of all.

SECTION C: TRANSFORMATION AND THE FSC

TRANSFORMATION IN SOUTH AFRICA

Unfortunately, despite all that has been done to date South Africa remains a very unequal society. As this graphics illustrates, we are making progress as a country and have managed to triple the size of the black middle class over the last 11 years. This is largely on the back of a changing labour market environment, in which black people are gradually making up a larger component of the senior workforce. It is imperative that as a country we maintain and accelerate the rate of change, where possible.



From the perspective of the savings and insurance industry the growth of a wealthier black middle class is a favourable outcome. This not only benefits those families but also grows the savings pool, which in turn grows the opportunity for economic growth in the country.

TRANSFORMATION WITHIN THE SAVINGS AND INSURANCE SECTOR (ASISA MEMBERS)

As far as the savings and insurance industry is concerned, the Financial Sector Code establishes our transformation targets. This is a very important transformation framework against which the performance of our members is measured.

The tables that follow reflect the transformation statistics of our industry. Some members will have performed better and some worse than the industry scores detailed below. Their individual performance will be reflected in their verified BEE certificates.

ASISA

Life Offices – Comparative statistics

	Actual 2005	Actual 2015	Target 2015
Black Ownership	16%	31%	25%
Management control			
- Board	30%	49%	50%
- Executive directors	22%	47%	50%
- Senior top management	n/a	39%	40%
- Senior management	16%	35%	60%
- Middle management	32%	48%	75%
- Junior management	45%	75%	80%
Skills development			
- Skills development spend	1.2%	4.9%	3%
- Learner-ships	2.1%	10. 6%	5%

Investment Managers – Comparative statistics

	Actual 2005	Actual 2015	Target 2015
Black Ownership	16%	31%	25%
Management control			
- Board	30%	43%	50%
- Executive directors	22%	39%	50%
- Senior top management	n/a	39%	40%
- Senior management	16%	34%	60%
- Middle management	32%	45%	75%
- Junior management	45%	67%	80%
Skills development			
- Skills development spend	1.2%	4.7%	3%
- Learner-ships	2.1%	11.4%	5%

An additional aspect specific to Asset Managers, that ASISA constantly monitors, is the extent to which transformation amongst the ranks of the investment decision makers is taking place. ASISA believes that this is especially important given the vast amounts of capital that is managed by these people on behalf of ordinary South African citizens. The table below illustrates the last available statistics in this regard:

INVESTMENT DECISION MAKERS	
Black males	29%
Black females	13%
Black people	**42%**
White males	45%
White females	13%
White people	**58%**

Independent reporting of financial sector progress (facilitated by the Financial Sector Charter Council) commenced in 2005. Whilst the progress in our view is both encouraging and commendable, some challenges remain, especially at Senior and Middle Management levels. In order to address these challenges, the industry has been implementing the following interventions:

- As can be seen from the table above, significantly more is spent on skills development of black staff than is required by the FSC. This is in order to facilitate progression through the Management ranks. The sector has also employed many more black interns than required, in order to sustainably support the talent pipeline into the future.
- The sector has also committed to spending 8% of payroll, on Junior Management and other staff, in the draft revised Financial Sector Code.
- ASISA Academy – As may be seen from the statistics above our members fall short of the targets in some categories. The shortage of skilled work ready candidates is recognised as one of the key difficulties in meeting the FSC targets. In an effort to address this problem ASISA has created an Academy to train and prepare black candidates for work readiness. The Academy was created 11 years ago and aims to develop skills in an accredited and academically rigorous environment with lectures offered by industry professionals (for no compensation). Courses offered include:
    - Equity analysts boot camp – to develop a pipeline of professionals for the Investment Management industry
    - Work ready students – Here the Academy works in collaboration with SA universities:
        - TSIBA – a black university for the very poor funded by business. The Academy course is chosen as an elective as part of a degree course. To

date 84 students have been on internships with ASISA members and 90% have been offered permanent employment.

- University of Johannesburg – Here 37 postgraduate students elected an Academy course and all have taken up internships with ASISA members. Around 83% have been offered permanent employment.
- Collaboration with ABSIP – Black students at university on Academy courses funded by ASISA.

- Trustee training – The Academy, in collaboration with BATSETA, delivers courses to pension funds trustees. The ASISA Foundation funds this initiative. To date 885 trustees have been on these training courses, which are vital in preparing trustees to execute their duties with due governance and skill. Topics covered include:
  - Fiduciary responsibility
  - Investments
  - Active ownership of shares

STATISTICS - Procurement

The following table serves to illustrate the fact that the Life Offices, who are the major procurers of goods and services in our sector, have performed well against the bulk of the targets agreed to in the FSC, in regard to enterprise and supplier development. We are also very aware of the importance of small business, in the context of inclusive growth and employment. ASISA members thus have agreed to work together on the transformation of the industries supply chain, with the following results thus far:

- The locally and internationally acclaimed ASISA ESD Fund was launched in 2013
- The fund provides both financial and non-financial support to small black businesses who are suppliers to members, and also attempts to provide access to contracts
- The Fund has raised R300m from members thus far, with approx. R200m more committed
- We are working with in excess of 360 black owned small businesses
- Jobs have been created at highly efficient cost (R60k each) relative to national benchmarks
- Turnover within these businesses has increased by an average of 22%
- We believe that this collective sector based approach is more effective and could be replicated in other sectors of the economy.

MEASURE	ACTUAL	TARGET	COMMENT
All Suppliers	91%	70%	Targets achieved on all aspects other than black women owned companies but there is still significant scope for growth, given the notes below. The sector has thus committed to higher targets in revised FSC
QSE/EME	29%	15%	
Black owned	15%	12%	
Black women owned	5%	8%	
ESD Spend	95%	Varied	

Notes on small business in South Africa:

- 70% of jobs are created by enterprises with fewer than 50 employees
- 78% of all registered businesses are black owned
- Only 47% of businesses have however been in existence for more than 5 years, and only 29% for more than 10 years.

It is thus critical that the right mix of non-financial support, market access and financial support is provided by the sector to small business.

STATISTICS – Financial inclusion

As stated previously, financial inclusion and the financing of transformative initiatives, across the SA economy, plays a vital role, in ensuring SA is placed on a path to inclusive growth, which leads to a normalised society, as evidenced by acceptable disparities in wealth between the various race and gender groups.

As can be seen from the tables below, ASISA members (the Life Offices) have also largely embraced the inclusion and funding targets set in the FSC. These targets are also likely to be increased, when the FSC revises them, at the end of 2017.

ACCESS TO FINANCIAL SERVICES	Actual Points	Target Points	Comment
Appropriate Products	1.5	3	Medical insurance standard envisaged for 2017
Penetration	6.3	7	
Transactional access	2	2	
Consumer Education	1.5	2	ASISA Foundation

EMPOWERMENT FINANCING	Actual Points	Target Points	Comment
Targeted Investment	12	12	Transformational Infrastructure, Low Cost Housing, Black SME, and Black Agriculture Funding
BEE Transaction Financing	2.8	3	Focus on Black Business Growth Funding *

* In terms of the new FSC the savings industry has a commitment of R 27 billion for the funding of black business

The ASISA Foster the Future initiative

In the context of financial inclusion it is important to highlight the following:

- The ASISA Foundation, ASISA Academy and ASISA Enterprise and Supplier Development Fund have the following initiatives in place:
    - Development of black insurance brokers (in conjunction with Inseta).

- Development of black Independent Financial Advisors. This includes the first intake of 21 black interns via the Academy.
- The ASISA Foundation financial literacy programme:
  - Saver Waya Waya – 8008 residents of disadvantaged communities and 1200 students from TVET's.
  - Projects "Qapela" and "WageWise" – 4530 workers trained; 2200 of which in conjunction with the National Union of Mineworkers.
  - Project "Flame"– This was done in conjunction with the National Association of Stokvels - 650 people underwent financial literacy training and 220 underwent Township Entrepreneurial training.

  All financial literacy projects undergo an independent assessment to ensure that the desired impact is achieved.
- In terms of governance the ASISA Foundation owns 51% of the ASISA Enterprise and Supplier Development Fund. The Board of Trustees of the Foundation includes representatives from:
  - Government
  - Labour Unions
  - Community Groups
  - ASISA members

We have made significant strides in transforming our industry but much more needs to be done. We have implemented some solutions where these are in our control and continue to work with other stakeholders to improve transformation in our sector, specifically where we fall short of FSC targets as an industry.

WHAT MORE IS BEING DONE? (POWER OF COLLABORATION BETWEEN ALL STAKEHOLDERS)

Above and beyond the measures referred to above that have been proactively implemented by ASISA, its members have also authorised ASISA to be involved in other issues beyond the direct scope of our industry. Some of these initiatives include:

- ISFAP – ASISA members, together with the banking industry, have provided administrative, management and technical support for the ISFAP initiative. This includes substantial support to assist NSFAS with the enrolment of new students in 2017. ASISA has also been part of a larger team modelling a financial solution for the funding of fees for poorer students. Funding and technical input has been provided to the ISFAP pilot currently being implemented. It is noteworthy that the government is actively working on the improvement of education and has recently published a list of occupations in high demand. We are hopeful that this will work in alleviating the skills shortage and will assist in preparing the younger generation for work readiness and productive employment in the economy.
- CEO Initiative – ASISA and its members have been involved and supportive of the initiatives introduced as part of the interactions between the Minister of Finance and corporate South Africa. These initiatives were initially focussed on the prevention of a ratings downgrade that would have had a significant impact on the cost of borrowings by the government, and also on the value of our collective savings. While this initiative was successful it has been expanded to include transformation, economic growth and job creation. Here too our members have contributed to the cause. Their involvement extends beyond a significant investment of their time and resources but also includes financial support. Some of those initiatives include:
    - Youth Employment Service – Internships to some 1 million job seekers
    - SME Fund for small and medium black enterprise
    - Infrastructure and support for development of black business with the banking industry amounting to R 100 billion
    - Old Hands Network – providing resources and support for emerging businesses and the public sector
    - InvestSA and One Stop Shop – to promote SA as an investment destination and to ensure policy coherence
    - Presidential Investment Advisory Council - We have consistently urged coherence in policy, legislation and regulation which recognises the developmental needs of our country in terms of the NDP.

T Dloti, (Chair of ASISA Board) **and PL Campher** (CEO ASISA)
10 March 2017