MONDAY, 9 NOVEMBER 2020

irfa dispatch

THE RETIREMENT INDUSTRY NEWSLETTER

TABLE OF CONTENT

LOCAL NEWS

INTERNATIONAL NEWS

OUT OF INTEREST NEWS

LOCAL NEWS

Shrug off your POPI fatigue to ensure data protection compliance

Local financial services businesses have been urged to wake from their Protection of Personal Information (POPI) Act slumber and begin implementing the changes in data collection, management, processing and storage necessary for compliance. A recent POPI seminar, hosted by Compli-serve and presented by Elizabeth de Stadler of Novation Consulting, revealed that many firms suffered from POPI Act fatigue due to the drawn-out implementation of the legislation. The Act was signed into law in 2014; it took until 2016 for the Information Regulator to be established; and the first regulations only saw the light of day in 2018. But the final push for POPI compliance is now underway.

On your data protection marks…

“President Cyril Ramaphosa’s June 2020 promulgation of most of the outstanding sections of the Act is the starting gun [for our race to compliance], said Richard Rattue, Managing Director at Compli-serve. “The industry now has a 12 month implementation period to ensure full compliance by 30 June 2021”. He observed that larger firms had set out on the compliance journey some time ago; but that smaller firms tended to put off data their protection initiatives due to the perceived cost and complexity. The time for delay is over. “Organisations have a year to bring their activities into line with the legislation,” said De Stadler, before promising to equip seminar attendees with the tools needed to get excited about the Act.

The seminar kicked off with a 15 minute overview of the essential building blocks of the legislation before offering a five step plan to ensure compliance in your advice practice. At the outset we learned that data discipline, as proposed in the legislation, was an underpin for an ethical and profitable business. De Stadler observed that definitions were an important starting point to understand the act, beginning with that of **personal information**. “If you cannot identify personal information, then you cannot protect it,” she said, before adding that “anything that your advice practice can relate back to a living, identifiable individual is considered personal information”. Personal information can be collected from a diverse universe of **data subjects** including clients, employees, suppliers, vendors and visitors.

Another important concept is that of the **responsible party**, or the organisation that is held accountable by the Information Regulator for any POPI Act compliance breaches. Those processing data on behalf of the responsible party could include data operators or data processers, who have fewer legal responsibilities.

How to source, store and use personal information

The POPI Act sets out how you source, store and use the personal information that belongs to the various data subjects that your business interacts with. "The Act is written around eight conditions of lawful processing of information against which you must assess your practice's processes," said De Stadler. As the seminar progressed, we realised there was no 'check box' shortcut to ensure compliance with the legislation.

What is required is that each business makes a careful assessment of its personal information-based business processes to ensure they meet the three critical components of Information Security Management (ISM), namely confidentiality, integrity and access. "Once you have an ISM framework in place you can begin to worry about the information privacy aspects, which determine what you are allowed to do, and how you are allowed to do it," said De Stadler.

How should financial advisers and short-term insurance brokers go about ensuring POPI Act compliance in their firms? The seminar offered a simple five step plan that will get your business most of the way there. The first step is to create an incident response team within the business, to define and monitor your responses to any POPI-related incidents that might occur. Step 2 is to conduct a Personal Information Impact Assessment (PIIA)to prevent you from introducing new personal data risks to your business.

Circumventing personal data risks

You will not find mention of the PIIA in the legislation; but it was introduced as a requirement in the 2018 regulations to the POPI Act. **The regulation requires: "An information officer must … ensure that … a PIIA is done to ensure adequate measures and standards exist in order to comply with the conditions for the lawful processing of personal information".**

This process must be performed whenever you consider using personal information for a new purpose; when you launch a new product or service; when you expand into other countries; after you implement new software or systems for data processing; and when you share data with outsiders. De Stadler said that it helped to think of the PIIA as an extension of your risk management function, where you continually establish context; then identify, analyse, evaluate and design treatments for risk; while at all times monitoring and reviewing the risk environment.

The third step towards POPI Act compliance is to implement strict access controls to both your physical premises and information technology infrastructure. This is of particular importance against the backdrop of data breaches, many of which result from lax security practices among your employees. ***Full Report:*** **https://www.fanews.co.za/article/compliance-**

regulatory/2/general/1082/shrug-off-your-popi-fatigue-to-ensure-data-protection-compliance/30606

FA News | 4 September 2020 | By Gareth Stokes

Preventing financial disaster in retirement – 8 pitfalls to avoid

After a lifetime of building up to the pinnacle of your wealth creation efforts – being the day you retire – you have to follow only one rule: avoid disasters that will cause the permanent loss of capital. The hard truth is that very few families manage to grow their wealth in retirement. And too many fall victim to scams or misfortune that materially threaten their financial future.

As we have seen in 2020, market volatility will always remain a risk that you have to manage. This problem is ever-present, even once you transition from accumulating your retirement savings to spending it. Strategies to mitigate these risks should form part of your financial plan, especially as these market risks are beyond your control.

Under normal circumstances, your retirement should remain secure if you have basic financial safeguards in place. But every so often, families find themselves in abnormal circumstances that threaten to undo their years of hard work and diligent saving.

Here are eight material risks to your retirement capital which, if you avoid them, will help you circumvent eroding wealth to a point where you can no longer achieve your retirement goals.

1. Overspending

Some families believe that investments will save them from their spending strategy. Unfortunately, it will not because investments aren't predictable. We think of spending as a percentage of your investable assets. In order for this pool of assets to see you through retirement from your mid-sixties, we work on a rule of thumb of withdrawing no more than 5% a year. Anything less than 4% per year means you should have a very good chance to sustaining your wealth throughout your lifetime.

Managing your spending risk means managing for inflation, so your portfolio has to include inflation-beating assets and you have to be flexible in your spending. And then, of course, you need to manage your household overheads, which can sometimes be done by downscaling.

2. Family dynamics

An often-overlooked risk is failure to inform family and loved ones of your financial and legacy plans. This makes succession planning so important if you have business assets that you want to pass on to the younger generations.

But the biggest risk in most families is if one, dominant person makes all the decisions. This is compounded if that person fails to groom younger family members to continue the business, or they are not aware of what the legacy plan involves.

3. Concentration risk

This is probably the most important aspect of financial planning when you enter retirement. This can take many guises, whether an over-concentration of assets in a particular stock, or market or property.

The threat is that one cataclysmic event can change the rest of your life. And COVID-19 is a prime example of the type of "Black Swan event" that you need to look out for.
So, you have to diversify your assets wherever possible.

4. Gearing

One other way your retirement assets are threatened is if you are highly leveraged. Should some disaster happen, the income you derive from a rental property might dry up or the value of shares held by a bank as collateral on a loan might fall off a cliff. If you are a forced seller in these circumstances, to extract yourself from the debt, you have no choice but to absorb the losses. Under normal circumstances you would be able to wait for prices to recover before selling, and thereby avoid the losses.

5. Taxes

Failure to plan properly can result in sacrificing some assets that an efficient tax plan would otherwise have avoided. Common reporting standards and the international clampdown on tax havens means there is nowhere left to hide. And depending on where your assets are held, you could be liable for taxes ranging from income, wealth and capital gains taxes to estate duties and inheritance taxes.
This is particularly relevant when assets are held in a business structure. You have to be aware of the complexity, flexibility and liquidity offered by ownership structures. Are you giving up control for the sake of tax?

In either event, you can turn complexity to your advantage by consulting advisors who can show you the best way to minimise your tax or using tax-friendly jurisdictions.

6. Scams, scandals and Ponzi schemes

These happen all the time, and South Africans have not been spared attempts to separate you from your hard-earned money. Pensioners are an obvious target because they are forever searching for higher returns.

It is no wonder then that people are attracted to schemes that offer higher "guaranteed" returns. But be aware that if the return is too good to be true, it is almost certain to be a scam.

7. Currency risk

A material risk that South Africans will be familiar with is the volatility of the currency.

If you find yourself at the wrong end of a currency movement, it can significantly affect your wealth. For example, in 2001 the rand lost 50% in about two months, to over R13 per US dollar. But then it appreciated by 50% to R6 per dollar and 10 years later it was still R7 per dollar.

We suggest that you choose a currency of reference. If you travel or plan to live in a different country then it makes sense to invest in assets that match the liability.

8. Sovereign risk

This threat of assets in a particular country losing value is not unique to South Africa because it happens across the world. Radical tax increases, expropriation, and exchange controls are examples of what governments can do. Reckless fiscal and monetary policy will create hyperinflation. Venezuela is an example of how a populist government turned a once-flourishing economy into one of the greatest humanitarian tragedies in a hundred years for a country not involved in war.

The most effective way to minimise sovereign risk is to diversify your physical assets across multiple jurisdictions.

Preserving your wealth through retirement means actively avoiding these pitfalls. One way to do so is to partner with a wealth manager who is able to guide you and prevent you from losing your hard-earned capital.

FA News | 4 November 2020

Are prescribed assets bad for the country?

The short answer is yes, but it is a little more complicated than that, as there could be benefits too. Contrary to popular perception, prescribed assets are not a process by which Government takes a portion of your retirement funds and the fund value drops.

Instead, it is a requirement by Government for an institution (most notably retirement funds, but the scope could be wider) to invest a stated percentage of their funds into specific assets. In most cases, these prescribed assets are likely to be loans to Government and state-owned enterprises (SOEs). The institution will still receive a return on its investment in the prescribed asset, and the investor could well receive a higher return than the return on any other asset. However, the risk is that Government or the SOE may be unable to repay the loan when it matures, and then the investment is lost.

The benefit for Government and SOEs is that more money will be available for investment and, as a result, the interest rate they will have to pay will be lower. This frees up funds for other projects that could increase the profitability of the SOE and, in the case of Government, decreases the need to increase tax rates.

And since prescribed assets are still earning a return, prescribed assets will be much less detrimental than increases in tax rates at this stage. Any increase in tax rates will result in less employment and economic development, which in turn will decrease future tax collection.

The risks associated with prescribed assets, however, outweigh their benefit. If Government and SOEs know there is a guaranteed source of funding, there is little incentive to improve their operations and the risk of maladministration continues. The main concern, however, is that available funds are not unlimited. If specific investments are prescribed, funds will have to be withdrawn from other investments that could have provided a better future for South Africa. It therefore prevents the optimal allocation of funds and reduces the potential economic growth the country can achieve.

What is Government and the ruling party's stance?

Currently, there is no project on the go from either Government or the ANC to force prescribed assets. While many statements have been made by members of the tri-partite alliance, Government itself has not provided a clear policy stance on the matter to date. On 17 August 2020, Mr Enoch Godongwana, chairperson of the ANC's subcommittee on economic transformation, stated that the ANC is not proposing that pension funds be used to bail out state-owned enterprises or to create a state-owned bank, but it wants pension funds to be used to fund profitable infrastructure projects.

Over the past few months, the ANC and National Treasury have been in discussion with the private pensions industry on the best way forward to allow pension funds to invest directly in infrastructure projects. Due to the size, liquidity and long-term nature of infrastructure projects, it is currently impossible for pension funds to invest in such projects.

The current discussion is therefore focused on how to change Regulation 28 under the Pension Funds Act and how best to structure the projects to access the funding available in pension fund schemes for these projects. If this can be achieved and profitable infrastructure projects are identified, this could provide pension funds with a great growth opportunity and increase the future GDP of the country. This process is nearing finality as announced during the MTBPS, and we will only be in a position to analyse the proposed changes in more detail once published.

It is, however, also very clear that the total funds required by infrastructure projects are significantly higher than the funds available within South African pension funds. Regulation 28 will therefore not be a silver bullet for our economy. A strong focus on persuading offshore investors to provide fixed investments to South Africa will be needed.

FA News | 30 October 2020

Annuitisation - Social Protection and NEDLAC - Compulsory preservation

Annuitisation from March 2021

Speech:

"In the area of social protection, we are happy to announce a historic agreement with all NEDLAC constituencies for the annuitisation of provident funds beginning in March 2021, which will enable all workers to continue to enjoy tax deductions on their contributions. We thank the labour constituency for identifying appropriate annuity products for low income workers."

Commentary from Rowan Burger:

The P Day and T Day proposals to try to streamline pension and provident funds finally have effect. Given the generous concession given, the purchase of annuities only applies to future contributions and persons younger than 55 now, meaning the benefit of this proposal will take a long time to be seen in our annuity sales. We had asked for a communication plan to alert pension fund members to this change but there is no mention of this.

Social Protection for Informal Workers

Speech:

The NEDLAC constituencies also agree to accelerate the introduction of auto enrolment for all employed workers, and the establishment of a fund to cater for workers currently excluded from pension coverage, as an urgent intervention towards a comprehensive social security system.

Commentary from Rowan Burger:

Treasury have for a number of years believed auto enrolment would improve coverage. We have highlighted that the coverage gap is primarily informal and atypical workers. This fund is seen by those in Department of Social Development as a pre cursor to the National Social Security Fund. From a Business perspective we recognise we simply cannot provide a low cost solution in this space but need the boundaries to protect the existing system.

Introducing Partial Compulsory Preservation

Speech:

Government will present legislation next year to allow for limited pre-retirement withdrawals under certain circumstances linked to mandatory preservation requirements.

Commentary from Rowan Burger:

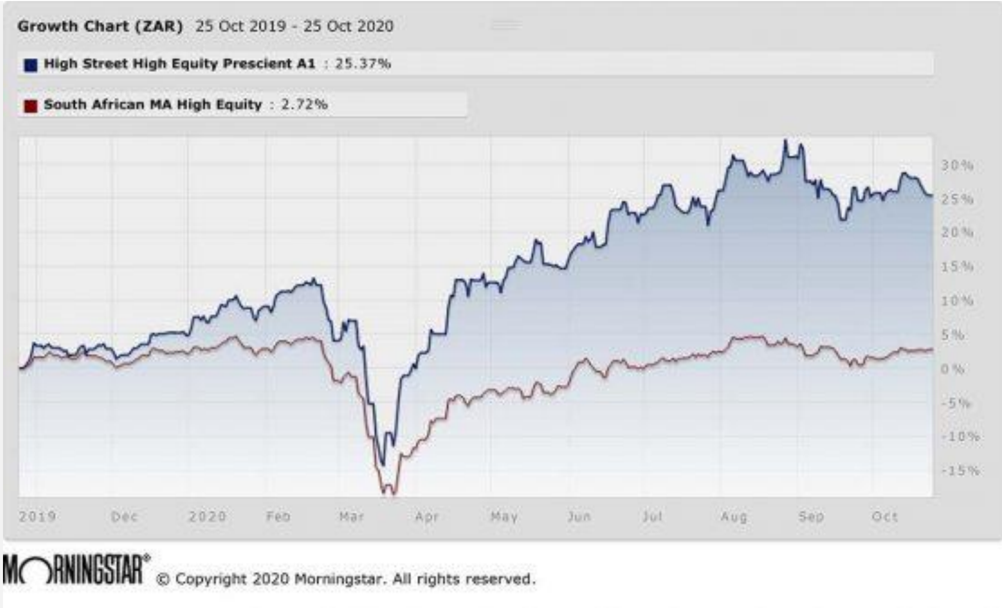
The request by Labour for immediate access to retirement savings over the initial COVID period highlighted a rigid system that could not easily allow for this. It did however present an opportunity for a future system that allows access but then also compels preservation. From the positivity in the statement it seems to have received broad support from labour.

FA News | 29 October 2020

The Reg 28 fund that has almost no exposure to South Africa

The High Street High Equity Prescient Fund – and it's been a top performer over the past year.

Over the past 12 months, the average return from South African multi-asset high equity funds has been 2.7%, according to figures from Morningstar. Over that same period, the High Street High Equity Prescient Fund has gained 25.4%.



The portfolio has almost no bond exposure, at just 0.1% of assets. It also carries a high weighting to property, with 17.5% invested in this sector.

Approach

The reason for this is that Beckley's target is to allocate in such a way that the fund maintains an 80% to 100% rand hedge bias. The intention is to offer a Regulation 28-compliant vehicle into which South African investors can invest in rands, but is minimally exposed to the local environment.

"We don't oscillate between deciding whether to be bearish or bullish on South Africa," says Beckley. "We leave that up to the investor.

"Currently, the fund will only invest in rand hedge instruments or, at a bare minimum, counters with a material offshore component. Currently, Mix Telematics is the holding with the lowest offshore component of approximately 40%.

"A rand hedge bias of 80% to 100% is the existing target," says Beckley. "However, this is subject to change should retirement regulation be amended, or it becomes infeasible because our investment universe shrinks to a level where it becomes imprudent to simply focus here. Our mandate allows us to change tack should either of these scenarios unfold."

Allocation

He estimates that the rand hedge component of the fund is around 90% of the portfolio at the moment. The first part of achieving that is through making full use of the fund's 30% offshore allocation allowance.

“Typically, that 30% offshore allocation will predominantly be in equity,” says Beckley. “We look for exposure to companies and sectors that we don’t have in our local market.” This includes investments in mega-cap growth stocks like Microsoft and Alibaba, but also more nuanced positions in companies like Lockheed Martin.

Listed locally, focused internationally

For the 70% that has to be invested in South Africa, High Street looks for companies that are either dual-listed on the JSE or make a large proportion of their revenues from international operations. This includes prominent large cap stocks like Naspers, Prosus, AB InBev and Mondi, but also allocations to small caps like Mix Telematics and Master Drilling.

“We are not a small cap fund, but we are small enough to play in that area,” says Beckley.

As a multi-asset strategy, the fund does consider the importance of yield. However, Beckley is not currently prepared to invest in local government bonds. He could do so and stay within the fund’s objective of maintaining an 80% to 100% rand hedge bias, but he believes that the risks are too high.

“We could hold South African government bonds if we wanted to,” he says. “But we would have to see a major shift in the underlying environment before we ventured there.”

Yield

As a proxy, he therefore prefers to invest in British American Tobacco, which is currently trading on a dividend yield of 8.1% according to Bloomberg.

The fund also takes advantage of the relatively high number of locally-listed property counters that have assets offshore. Three of the top 10 holdings in the portfolio are real estate stocks – MAS Real Estate, Sirius Real Estate, and RDI Reit.

“We have to have a relatively high weighting to property, because our equity universe is so limited and for the yield,” says Beckley.

Restricted

This highlights a key challenge that he faces in managing this portfolio. If the intention is to only invest in companies with high exposure to offshore earnings, the opportunity set on the JSE is extremely limited.

“Our investible universe is about 10 to 12 names in South Africa, plus the property stocks,” says Beckley. “At the moment, given the strategy of the fund, it is very unlikely that we are we going to be holders of local banks or local retailers. That eliminates a significant part of the JSE.

“But we are utilising all of the asset classes available to us. We are currently increasing our exposure to gold, and we do have a position in platinum.”

Moneyweb | 30 October 2020

INTERNATIONAL NEWS

Unlock UK pension funds to speed recovery and boost savers

It has been almost 100 years since economists including John Maynard Keynes identified the “Macmillan gap”. The term tracks the funding shortfall that starves small- and medium-sized British companies of the finance they need to grow. The gap can widen to a chasm in times of crisis, such as today. But there is, I believe, a way to close it and prevent deep economic scarring across the UK, by unlocking the firepower of British pension funds. Across the economy, just about all of the short-term measures that can release cash to companies have already been used. Most of them are based on credit — from the government’s Coronavirus Business Interruption Loan Scheme to companies adjusting their balance sheets or deferring liabilities. But debt is never a sustainable solution. The UK needs to find longer-term solutions to fuel economic recovery, or risk disaster. The most acute funding challenges concern “growth economy companies”. There are around 21,000 of these in the UK, according to research for the Business Growth Fund, the investment company set up by British banks after the 2008 financial crisis, which I run.

They make up the dynamic midsection of our private sector. Highly profitable and fast-growing — on average increasing revenues at twice the pace of economic growth — they are our future. However, they are generally too small to be funded by public markets, while often having outgrown venture capital. The solution to this problem is the creation of a UK National Renewal Fund, with £15bn of equity capital, to channel patient capital to these companies. This pool of capital will be made up of equity investment from the pensions industry, insurance companies, quoted investment trusts, sovereign wealth funds, private clients and, as an extension of the government’s Future Fund, state funding where appropriate. Funds will be deployed locally and on a commercial basis.

They will help to level the country up, not down. The pension fund component would be transformative, by unlocking vast pools of capital. Generally speaking, trustees of defined benefit schemes already have enough flexibility to invest growth funds in growth companies.

But over time this funding will diminish as such DB schemes run off. In contrast, regulatory change is needed to allow the fast-growing defined contribution schemes to make such investments at scale. I believe this could be game-changing, given that a growing proportion of UK pension assets are held in such DC schemes. The opportunity is to unfetter trustees and allow them to follow broader investment strategies that can deliver higher returns and support the growth economy.

It would join a nation of savers to a small army of entrepreneurs and innovators. It is clear that this type of investment could benefit scheme members too. According to the British Business Bank, the UK state development bank for SMEs, a 22 year-old could increase the value of his or her final retirement pot by between 7 and 12 per cent if they invested 5 per cent of their pension in venture capital and growth equity. But smart regulatory thinking is required so that pension trustees can invest in growth capital on their behalf. Here is how that could be done. At the moment, trustees generally require support from investment managers to create the portfolios they want.

That means they must also pay the managers for their expertise and time. But there is a hurdle: the so-called charge cap. This imposes a limit of 75 basis points to the total fees charged to any individual in a DC scheme's default fund. As such, it also limits what trustees can spend on investment and administration. This makes it almost impossible for them to invest in venture capital or growth equity, despite the higher absolute returns this should generate. To address this, the government should exclude performance fees from the charge cap for relevant growth equity and venture capital investments, and let trustees make decisions based on absolute returns.

Such carve-outs could be certified by the BBB — as it does for the growth equity funds it backs. Until this happens, trustees will remain discouraged from making such investments. Unlocking the firepower of UK pension funds could provide fast-growing smaller businesses with the financing they need to grow, employ and invest. It is obvious that we cannot sit idle and hope for the best in the long term. Instead, the government and British financial institutions must be bold. For nearly a century, the Macmillan gap has been a major flaw in the UK financial system. We now have an opportunity to close it and get on the road to recovery and a brighter future.

Financial Times | 31 October 2020

OUT OF INTEREST

Are you sitting on savings you could be investing?

The COVID-19 pandemic has affected people's finances in very different ways. While it has highlighted the need for emergency savings as a buffer against tough times, it has also created anxiety and uncertainty for those worried about job security and market volatility, causing some to sit on extra cash that would normally be invested.

“Lockdown resulted in an enforced reining in of spending, with eating out, shopping and travel severely curtailed and day-to-day costs like fuel and transport reduced by working from home,” explains Nomi Bodlani, head of Strategic Markets at Allan Gray. “While the economy is now more open, many are relooking their spending habits, hoping to make more permanent changes.”

Although there is little evidence of what habits South African investors will adopt post-pandemic, especially in light of an ailing economy and dismal household savings rate,consumer spending is likely to be fundamentally different for many months to come, and so too will people’s spending and saving habits.

“The pandemic has had many financial consequences. If you are fortunate enough to have found yourself with additional savings, and if you want to make adequate preparations for a financially fit future, now is a great time to get started or to accelerate your investment efforts,” says Bodlani.

She adds that many investors sitting on extra cash – whether from deferred spending or from that holiday that never happened in 2020 – are feeling jittery about the markets. The latest data released by the Association for Savings & Investment South Africa (ASISA) echoes this sentiment, showing that many investors are opting for the perceived safety of money market funds, despite the fact that interest rates have headed south.

“While it is understandable that investors are shying away from risk at this time, in an environment of lower interest rates, investors looking for long-term growth need to make sure that a portion of their portfolio is exposed to growth assets, such as equities, which have proven to deliver growth over the long term,” Bodlani explains.

Adjusting for inflation, equities have returned7.5%per year versus bonds at4.3%and cash at2.5%over the last two decades."It is therefore important to have an appropriate amount invested in equities to generate potentially higher real returns," she says. The other piece of the puzzle not to overlook is an element of offshore exposure.

"Investing offshore gives you exposure to different economies and geographies and allows you to access sectors and companies that aren't available in South Africa. It also helps you to shield your portfolio from rand weakness and protect the buying power of your cash."
However, Bodlani cautions against simply investing offshore in response to news headlines and market noise.

"Investors' appetite for offshore assets seems to be at its strongest when the South African narrative, and the rand, are at their weakest. This is understandable, but expensive as you use a weak currency to buy expensive offshore assets. The decision to invest offshore should be part of your long-term investment strategy and should align with your long-term investment goals."

She explains that you should figure out how much of your investment portfolio you want to place offshore, and what you are trying to achieve, and then formulate a plan to invest as regularly as possible in carefully selected assets.

"If you don't know where to start, or if you are feeling overwhelmed, chat to an independent financial adviser who can help you decide on the best course of action for your extra cash. He or she will be able to help you choose appropriate investments to meet your long-term investment goals, and make sure that your choice is appropriate for your needs and circumstances. He or she can also guide you through periods of uncertainty – like we are currently experiencing – and make sure you get the most out of your investments," she concludes.

FA News | 29 October 2020

Switchboard: 011 450 1670 / 081 445 8722
Fax: 011 450 1579
Email: reception@irfa.org.za
Website: www.irf.org.za

2nd Floor Leppan House
No 1 Skeen Boulevard
Bedfordview 2008