



Decision Making in the Financial Investment Sector:
An Exploration

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**Decision Making in the Financial Investment Sector:
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(I wish to acknowledge the assistance of Ms. Ingrid Goodspeed)

**“If all the economists in the world were laid end to end, they would not reach a conclusion”
Martin Wolf, The Financial Times, 26 February 2010.**

1. The Invisible Hand of the Market, or, the hidden Hand of Capital?

Curiosity killed the cat. It is also giving us a severe headache. Curiosity has led us into a labyrinth of linkages which seem to have no structure. It is a labyrinth of financial flows which seem to reflect the invisible hand of the market. But there is some evidence of a hidden hand of decision makers who play a vital role in determining financial investment choices. Furthermore, while financial returns and risk aversion are primary explanations for financial investment decisions, there are certainly other factors which are not generally acknowledged.

This paper attempts to explore some of the intricate channels for financial investment and point to possible influences on decision making.

2. The difference Between Decision making and Decision Taking.

System analysts often distinguish between decision “making” and decision “taking”. A senior body, Cabinet or Board of Directors may take a decision, but the preparatory work on which the decision is taken, perhaps in the form of a position paper, is done elsewhere.

The senior body may well spend a great deal of time in “taking” that decision, it may not be a mere formality, but the research and recommendations are made by others.

In the case of financial investments, so much research and analysis is necessary that a large number of specialists are involved in analyzing data, assessing performance and selecting the most suitable instruments. Most of this work is done behind the scenes by very bright, often young experts, perhaps with little industry experience, who nevertheless have huge responsibilities. These young experts are hopefully generally overseen by more experienced, seasoned management.

In the main this area is not scrutinised in public and some of it is not regulated e.g., advisory services to pension fund trustees by asset consultants. The purpose of this paper is not to promote such regulation. Rather the paper arises from curiosity. It asks “who” decides what investments should be made, on what basis and in whose interest?

Decisions are based on the analysis and recommendations placed before the decision taker –on highest return for a targeted or budgeted level of risk. All available information in the public domain is discounted into the price of a financial security. Thus the market prices of financial securities such as shares follow a random walk i.e., an inherently unpredictable pattern. Ben – I hope I understood this correctly. Of course this is correct in a market economy, but is it the whole truth? Are there no external considerations other than risk/return which influence individual decision-makers? There is the notorious “herd effect” where brokers play safe by not going against the stream. But there are even more important influences such as an assessment of the sustainability of a firm or even a sector, the political climate, the anticipated role of government investment, e.g. in infrastructures, the expected values of the currency, interest rates, etc. All these play a part in decision-making.

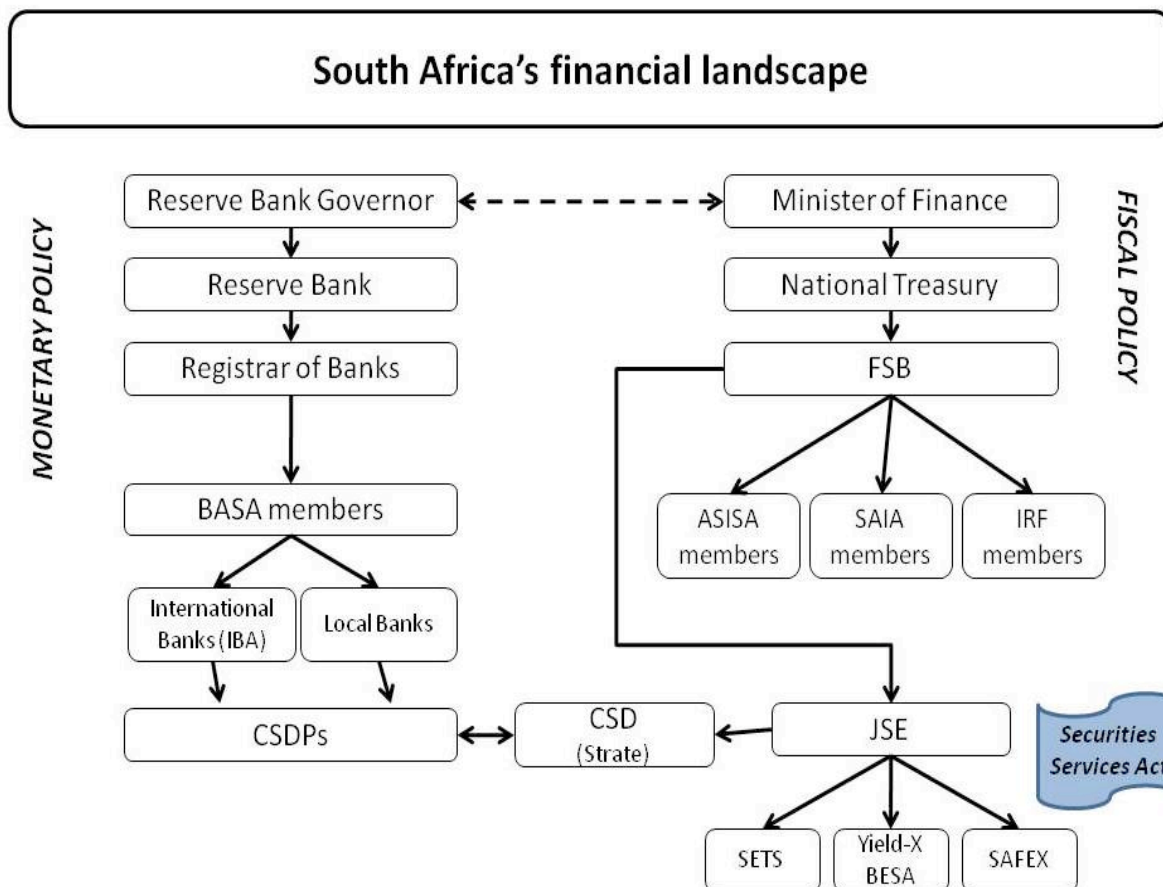
In the earlier times, before the current complex state of our economic system, it was enough to know who the owners of the top corporations were in order to understand the motivation for investment. In the 1980's we knew the top six corporations, and this was a sound basis for assessing where business interests lay.

But in the present period there is interlocking of ownership and globalization of companies, especially in the financial sector so that ownership is a poor guide to the motives underlying an investment decision. Rather, management is where power lies and management often depends on external advice. A large corporation may have a strategist but even then information is so dispersed that external advice is needed. Besides a Board may feel that the views of their in-house strategist may be biased by subjective factors, such as the policies of the organisation and its underlying value system.. In any event given the complexity of the market, only specialist firms, Asset Consultants and Investment Managers are generally able to guide investment decisions.

In the past, South African economists put a great deal of effort into examining the corporate structure of the large companies, who owned them and who played what role in the decision-making of that company. This was relatively easy, because there were a small number of top companies, Anglo American, De Beers, Barlows, come to mind, and in those companies individuals like Harry Oppenheimer, Anton Rupert, Punch Barlow, were so prominent that decision-making was relatively easy to identify. But in the modern world with the huge integration of companies with cross holdings, with the internationalisation of many corporations, it becomes much more difficult to identify. Indeed it is much less the owner, who is prominent, but the CEO, who may have shares in the company. So, one looks at other institutional mechanisms which might play a major role in both investment decision-making and decision-taking. What my research shows is that the Asset Consultants and Investment Managers in South Africa play an extremely important role.

To this end I've interacted with the Association for Savings & Investments South Africa (ASISA), which is a new Organisation and which is perhaps best placed to discuss the nature of decision-making and decision-taking in South Africa. They have advised me on the linkages which exist in the financial landscape of SA, which are something like the following:

Architecture of the Financial System



Note: The glossary at the end of the presentation has a full definition of all acronyms

The Minister of Finance interacts with the Reserve Bank Governor who in turn controls the Reserve Bank which controls the Registrar of Banks. The Registrar supervises the members of the Banking Association of SA (BASA) namely the banks directly (i.e., not via BASA). Both the branches of foreign banks or international banks (IBA) and local banks are members of BASA. Certain banks are Central Securities Depository Participants (CSDPs). Only CSDPs may interact with the Central Securities Depository (CSD).¹

The Minister of Finance controls the National Treasury which controls the Financial Services Board (FSB). The FSB supervises (once again directly) the members of the Association of Savings & Investments SA (ASISA) the SA Insurance Association (SAIA) and the Institute of Retirement Funds (IRF).

The FSB also supervises the capital markets i.e., the Johannesburg Stock Exchange (JSE). Trading in financial instruments on the JSE takes place via the Equity trading platform (SETS) (for equity or shares), the Interest-bearing instruments trading platform (Yield-X) BESA (e.g., bond and bond derivatives) and the

¹ JSE has implemented an electronic system called Share Transactions Totally Electronic (STRATE), which allows all share transactions to be settled electronically. A pre-cursor for such settlement is the dematerialization of paper share certificates. Dematerialisation is the process of replacing paper share certificates with electronic records of ownership in STRATE (the approved Central Securities Depository (CSD)), through a Central Securities Depository Participant (CSDP) or broker. Only CSDPs can liaise directly with STRATE. CSDPs have to qualify for their status by meeting certain criteria prescribed by STRATE and obtaining approval from the Financial Services Board.

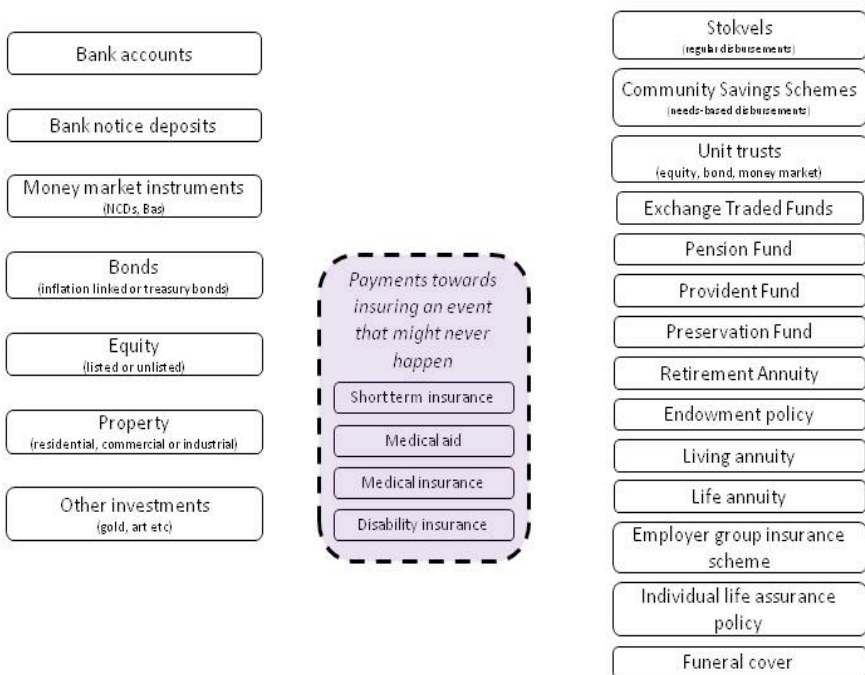
SA Futures Exchange (SAFEX) (derivatives).. All this relates to the financial industry and regulation and control mechanisms, but where do the funds for investment come from?

There are three main sources, namely (1) Individuals, (2) Corporates and (3) Government. A further source is the foreign sector. The decision making and taking of individuals are as follows:

What does the individual own and who makes the investment decision on the underlying security?

**Individual owns the underlying security
Individual makes the investment decisions on those securities or is advised on it**

**Individual owns a participatory interest in a structure (not the underlying asset)
Someone else makes the underlying security investment decision**



Individuals may decide to place funds as investments in bank savings accounts, bank notice deposits, money market instruments, bonds (which are inflation linked or treasury bonds), equity, property and other investments of a personal kind.

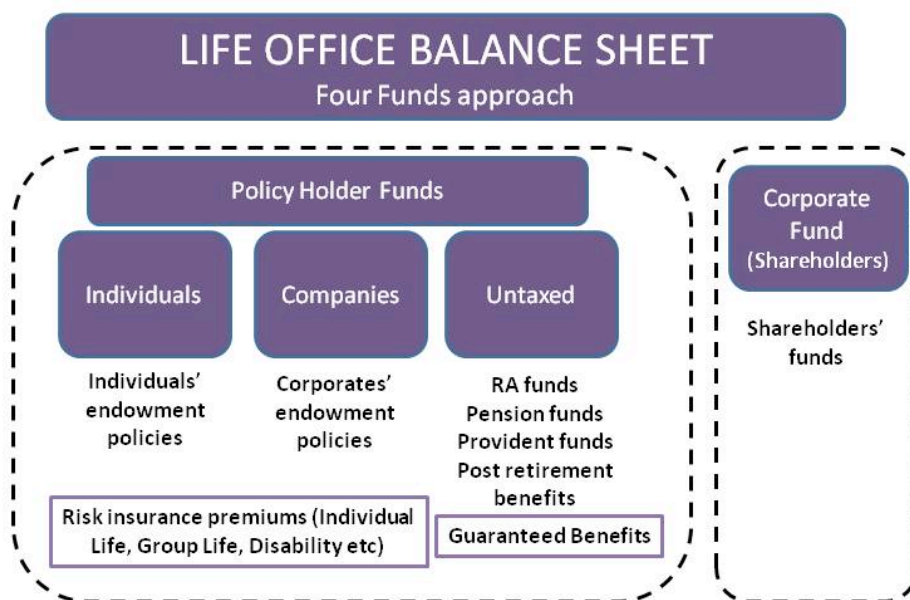
Individuals may participate in an institution which pools or aggregates money. This means that the individual decides on the pool of funds (e.g., a local equity, bonds, balanced pool) but loses personal control over the underlying investment decision i.e., what individual share or bond to invest in. The institution becomes a conduit for the funds and someone else makes the underlying security investment decision. Such institutions include stokvels, community savings schemes, unit trusts (which include equity, bond and money market), exchange traded funds, pension funds, provident fund, preservation funds, retirement annuity, endowment policy, living annuity, life annuity, employer group insurance schemes, individual life assurance policies and funeral cover schemes. In some of these Asset Managers do the actual investing.

The institutional framework of investment is quite complicated and the flow of funds takes many different channels. The main players are:

1. Life Offices which control R 1.5 trillion
2. Retirement Funds control R1.5 trillion
3. Unit Trust Funds control R 0.8 trillion . These funds are normally Collective Investment Schemes which normally include shares, bonds etc and are very liquid
4. Private assets about which information is not available. § (it is important to note that private portfolios are not regulated other than by law related to banks, insurance companies, collective investment schemes, JSE. Also there is investor protection law such as the Financial Advisory and Intermediary Services (FAIS) Act.)

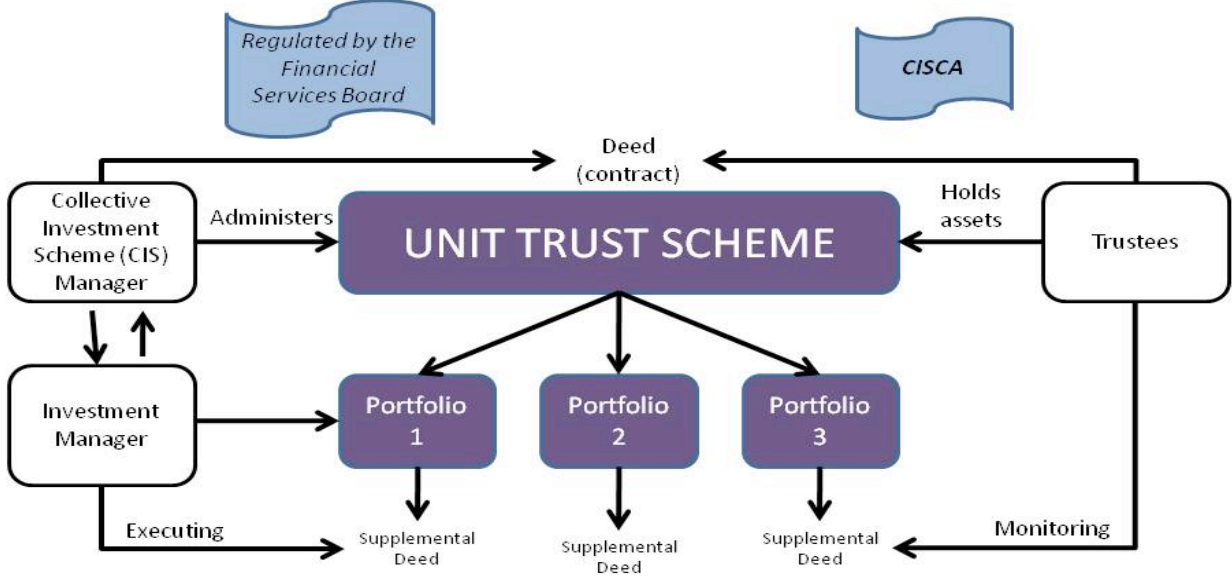
Where investment take the form of policies with life insurers, the insurer takes the decision about the

How is the Life Office balance sheet apportioned?

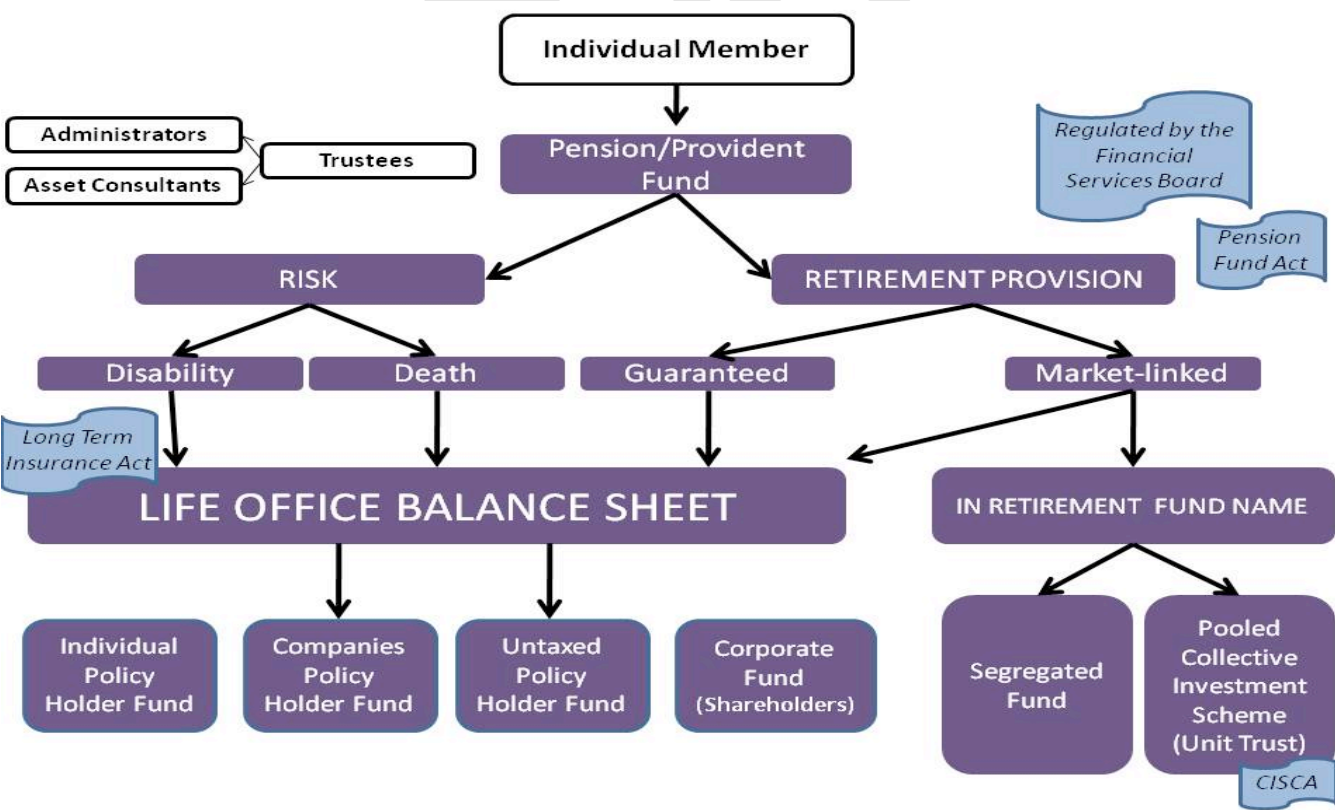


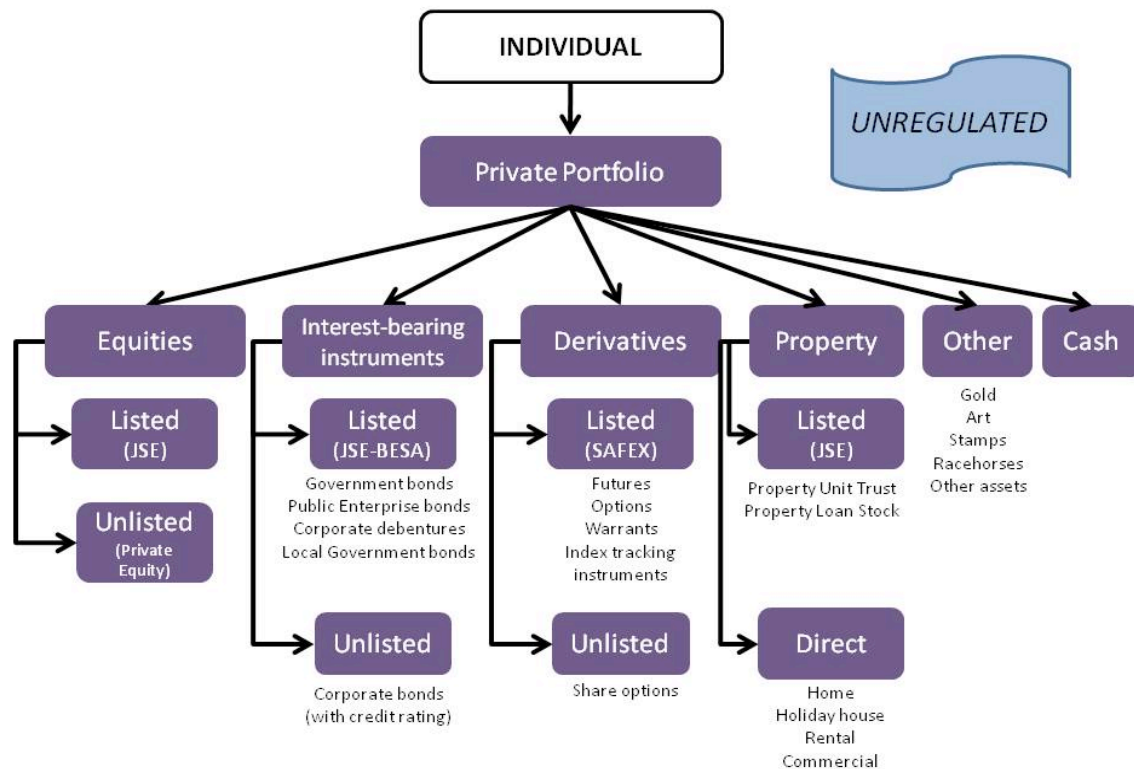
individual investment securities on behalf of the beneficiary (subject to regulation 28 in respect of pension and retirement funds).

How is a unit trust structured?



The **Life Office** balance sheet is structured in the following way – there are Policy Holder Funds on the one hand and there are Corporate Fund shareholders on the other.





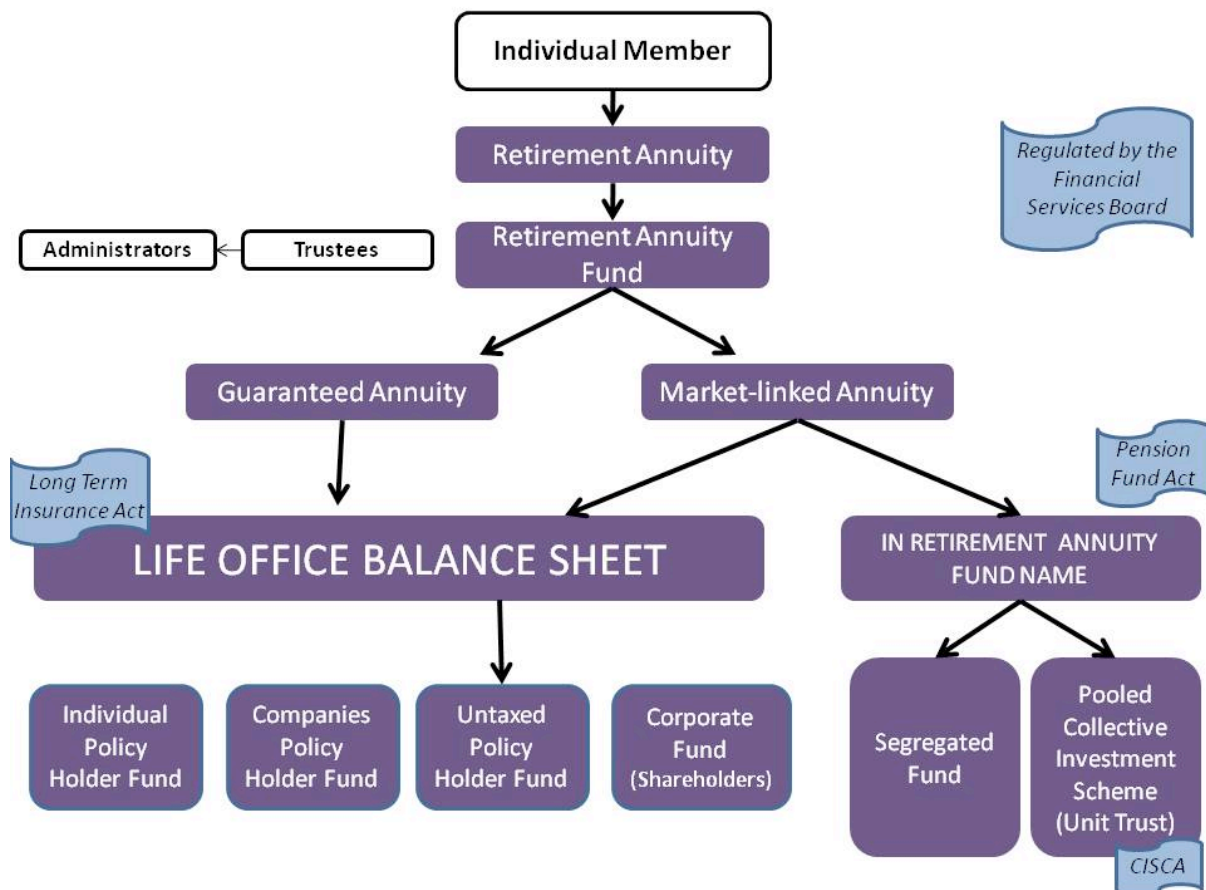
In the Policy Holder Funds, these are divided into *Individual*; *Companies* and *Untaxed* entities. Of the *Individuals* there are individual endowment policies; under the *Companies* there are Corporates' endowment policies and under the *Untaxed* there are RA funds, pension funds, provident funds, post retirement benefits, etc.

Retirement Funds. Contributions for retirement go to the following:

- Pension funds;
- Provident funds;
- Annuity funds and
- Preservation funds

Then we look at how the **Unit Trusts** are structured

The Unit Trusts (or CISs) hold funds of R789 billion. Of this about R 260 billion (source: ASISA CIS statistics) is in money market instruments with less than one year maturity. 60% is in shorter than 3 months maturity, showing asset holders' risk aversion and preference for liquidity by. This must be a cause for concern as it is money which could be invested in productive enterprise. A large proportion of these funds are deposited with the banks, which means that banks use these short term funds to fund long term lending like mortgage bonds. This poses liquidity risk for banks. Banks generally have sophisticated liquidity risk management frameworks including cash flow management systems and liquidity contingency plans to manage the risk.

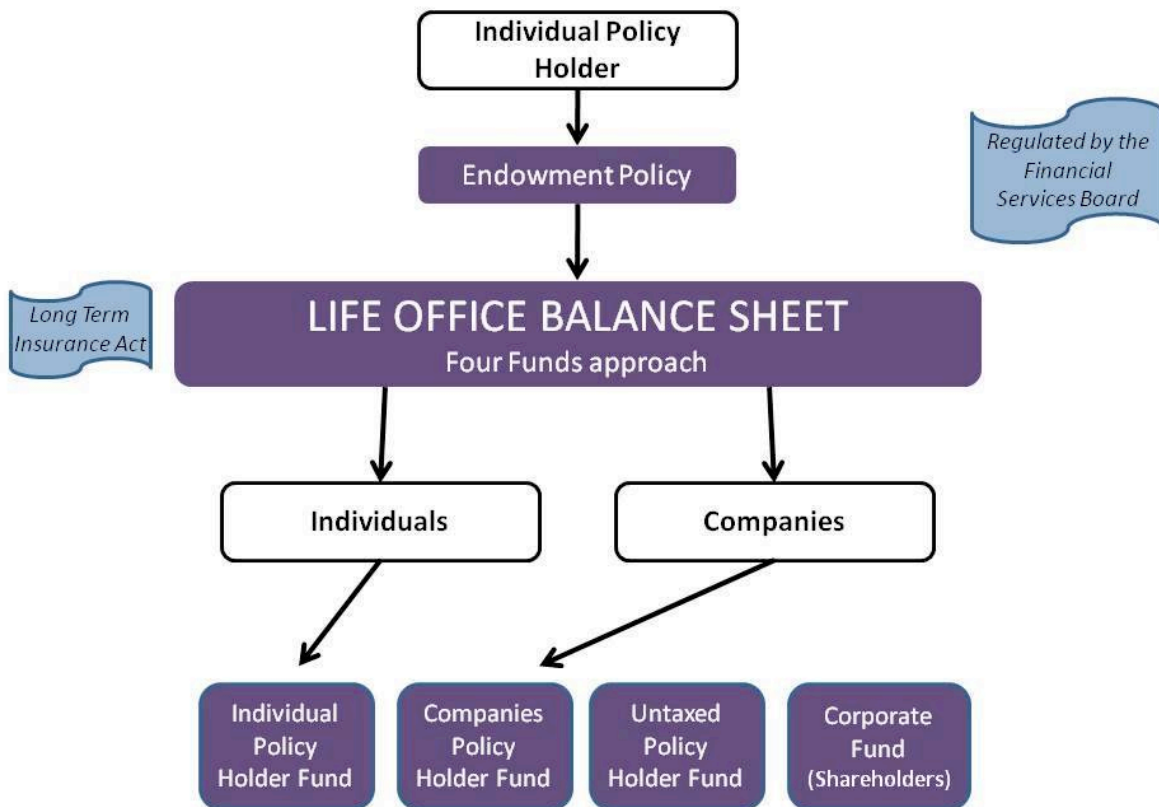


–Unit Trusts (or CISs) are regulated by the FSB in terms of the CIS Control Act (CISCA). Although the CIS Act does not prescribe the legal form of a CIS, typically the assets are held in the form of a trust. The trustee oversees the operations of the CIS and ensures good governance, fiduciary and regulatory compliance and the protection of interests of CIS investors including the safekeeping of CIS assets. The CIS manager is authorised in terms of the CIS Act to administer a collective investment scheme. It handles administration, operations, marketing and sales of the CIS and has responsibility for operating the fund in accord with the CIS Act and regulations and the rules of the fund.

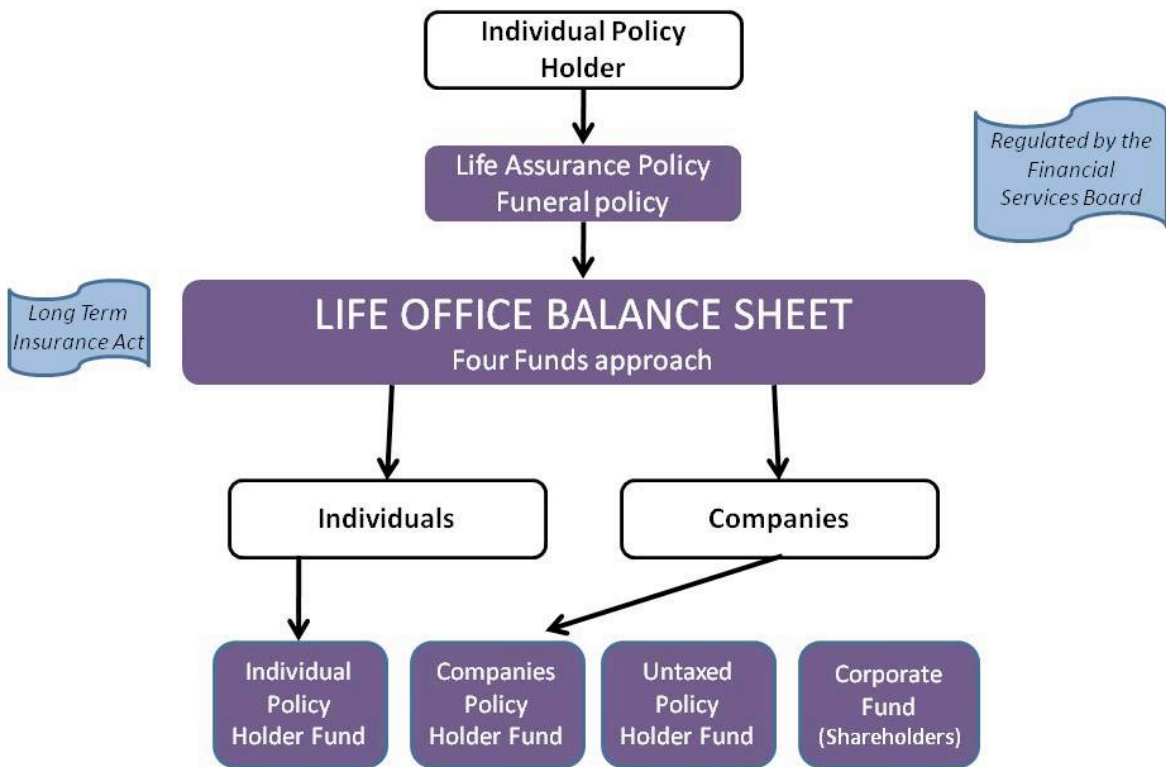
In their simplest form, retirement funds are nonprofit institutions that collect, invest and administer monies contributed to them by individuals and companies. One could also consider retirement funds as regulated (for individuals’ protection) savings pools that enable people to save (cost and tax efficiently) for their old age.

Retirement funds are regulated by the FSB in terms of the Pension Fund Act. There are various avenues for pension funds: life insurance policies (guaranteed); and market-linked such as Segregated Funds or CISs. The use of CISs and life insurance policies as investments is quite common in South Africa, especially by smaller retirement funds. Regulation 28 allows the use of these investment vehicles, but on the basis that the underlying investments conform to the regulations.

DO NOT SEE THE POINT OF DESCRIBING THESE ALL SEPARATELY – they are essentially the same _



Individual Policy Holder may also link to an Endowment Policy which is regulated by the FSB which then links to the Life office Balance Sheet and there are four Funds there and this is regulated in terms of the Long Term Insurance Act. Here again you have the break into *Individuals* who link to Individual Policy Holder Funds and on the other side you have *Companies* which link to Companies Policy Holders and there are also Companies Policy Holders. There are also Untaxed Policy Holders and Corporate Fund shareholders.

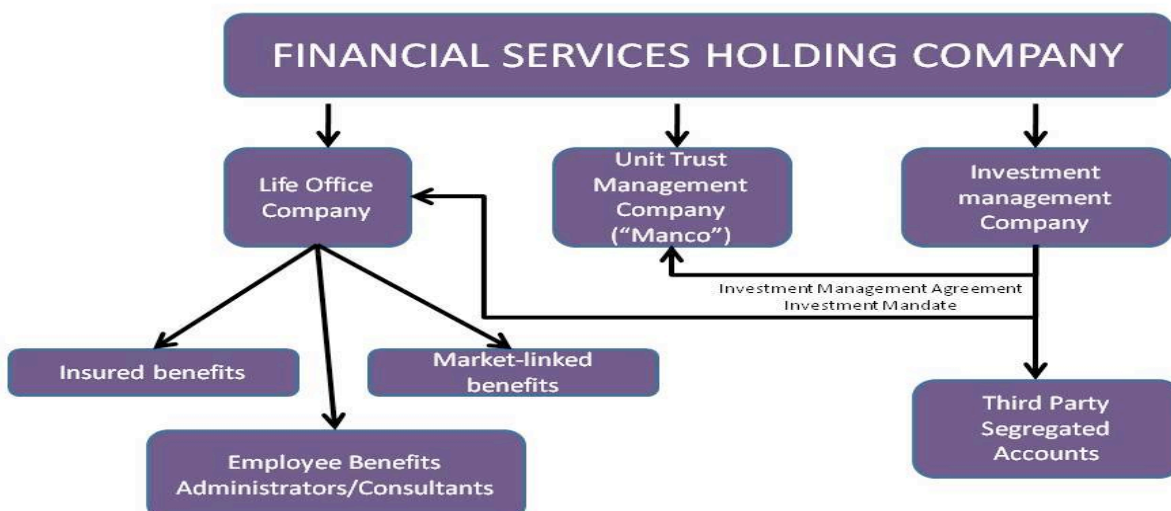


The Individual Policy Holder may also link to a Life Assurance Policy

(a funeral policy) which is regulated by the FSB, which again is regulated by the Life Office Balance Sheet where there are four Funds and this is regulated by the Long Term Insurance Act. That too can break down into *Individuals* who link to Individual Policy Holder Funds and on the other side you have *Companies* which link to Companies Policy Holders and there are also Companies Policy Holders. There are also Untaxed Policy Holders and Corporate Fund shareholders.

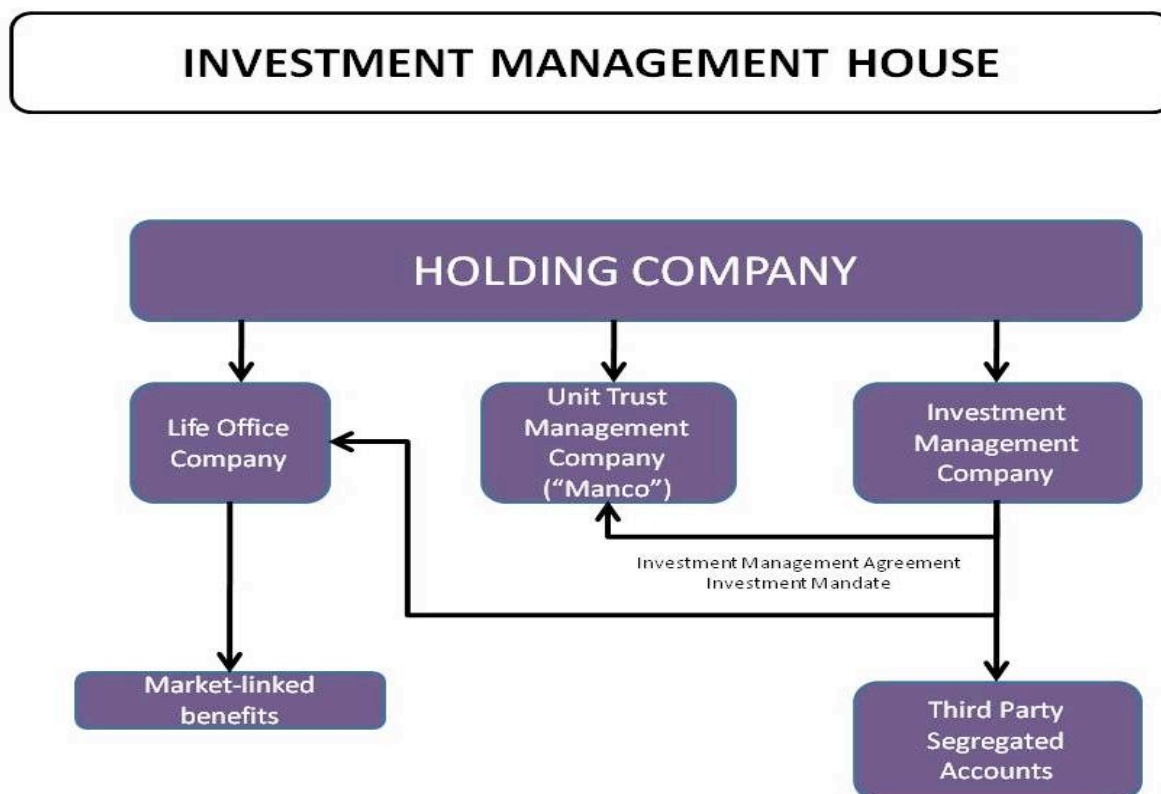
Then there's the Financial Services Conglomerate which is one of the older institutions and offers a wide range of services. The Financial Services Holding Company breaks down into three [*Life Office Company*; a *Unit Trust Management Company ("Manco")*] and there's an *Investment Management Company*. The Life Office Company is linked to Insured benefits; Employee benefits with Administrators and Consultants and Market-linked benefits. The Unit Trust Management Company links to Third Party Segregated Accounts as does the Investment Management Company.

FINANCIAL SERVICES CONGLOMERATE



DRAFT

The Investment Management House is a newer form of institution. I do not understand the difference between houses and companies. Perhaps ASISA could clarify



There is a holding company and they link to a *Life Office company* and Market-linked benefits. Secondly to Unit Trust Management company (“Manco”) and thirdly, to an Investment Management Company with Third Party Segregated Accounts.

Then we go back to the Individual and the Private Portfolios . Private Portfolios can be invested in *Equities; Interest-bearing Instruments; Derivatives; Property; Other(e.g., diamonds)* and *Cash*. *Equities* can be listed on the JSE and unlisted namely Private Equity. *Interest-bearing Instruments* can listed on the JSE’s interest rate division and these include Government bonds; Public Enterprise bonds; Corporate debentures and Local Government bonds and listed Corporate bonds. *Derivatives* Listed on SAFEX and could be Futures; Options; Warrants; Index tracking instruments and listed Share options. Over-the-counter or unlisted derivatives are also available. *Property* investment may be Listed (JSE); Property Unit Trust; Property Loan Stock. Investors may invest directly in property in the form of Homes; Holiday Houses; Rentals and Commercial properties). *Other* Investments are in Gold; Art; Stamps; Racehorses and finally there is *Cash*.

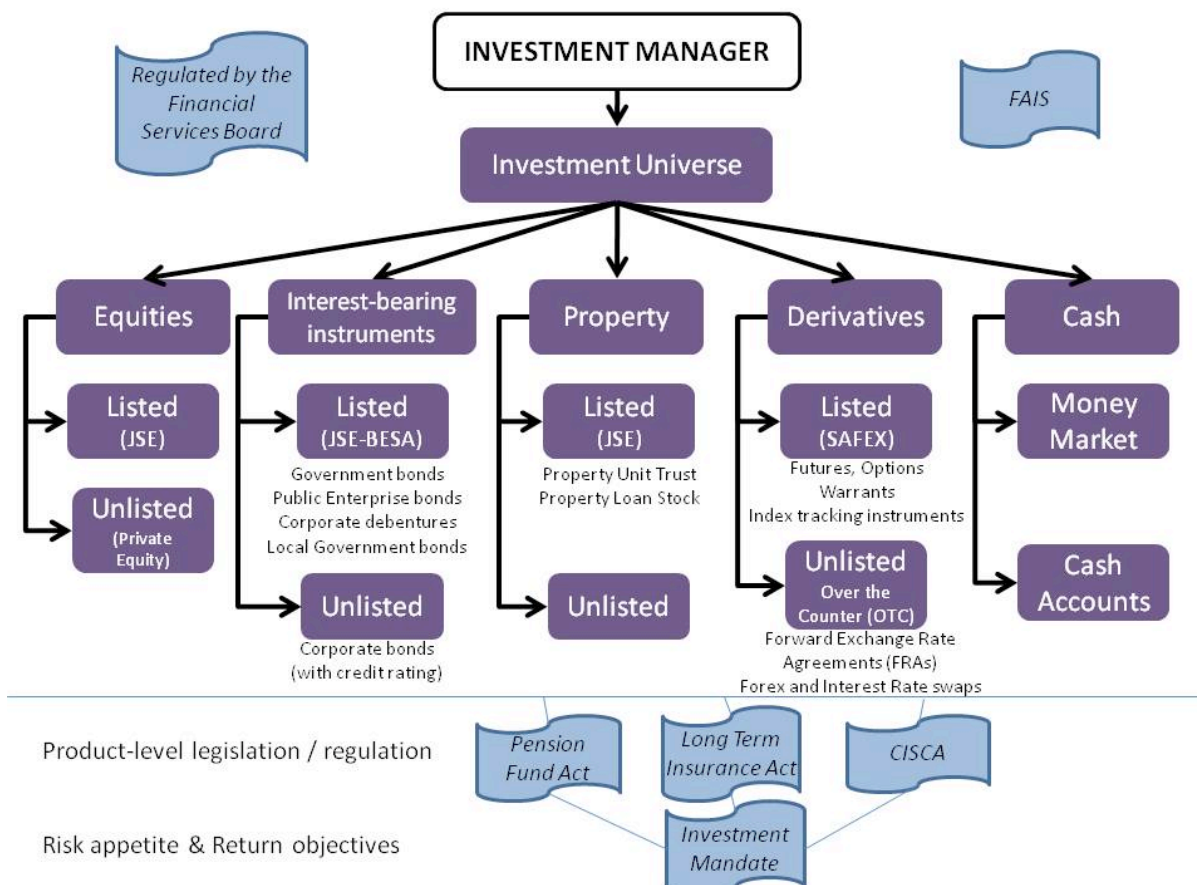
Who are the role players?

ROLE PLAYER	EXAMPLES
Asset consultants	Alexander Forbes, Fifth Quadrant, Novare, Riscura
Financial Services Conglomerates	Old Mutual, Sanlam, Liberty, Momentum, Metropolitan
Investment Management Houses	Allan Gray, Coronation, Investec Asset Management, Cadiz, Prudential et al
Investment Management Companies**	Allan Gray, Coronation, Investec Asset Management, Cadiz, Prudential OMIGSA, SIM, RMBAM, Stanlib, MetAM et al

****NOTE**

1. There is an arms' length agreement between the investment management companies and their clients (life office, Collective Investment Scheme Management Company (Manco) and third party clients / segregated portfolios). This agreement is evidenced by an Investment Management Agreement and Mandate.
2. Investment Management Companies never own the assets. They manage under power of attorney provided by the client.
3. The Investment Management Companies compete with one another.

DR



The Investment Manager is regulated by the FSB under the Financial Advisory and Intermediary Services Act (FAIS). The Investment Manager has an Investment Universe to choose from: *Equities* (JSE-listed or private equity) *Interest-bearing Instruments* listed on the JSE's interest rate division (used to be BESA or Bond Exchange of South Africa) *Property* (listed or direct investments) and *Derivatives* (listed or over-the-counter). OTC derivatives include Forward Rate Agreements (FRAs) and Forex and Interest Rate swaps. Then finally there's *Cash*, which could be invested in Money Market instruments such as Treasury bills or in Cash (usually bank) accounts. Different regulatory mechanisms are in play here. There are the Pension Fund Act; the Long Term Insurance Act, CISCA and the Mandate given by the client (e.g., pension fund) to the investment or Asset Manager.

I should add that in many cases the Asset Consultants are very important since they give advice. Who are these role players? Among the *Asset Consultants* you'll find firms like Alexander Forbes, Fifth Quadrant, Novare and Riscura. Under the Financial Services Conglomerates you'll find Old Mutual, Sanlam, Liberty, Momentum and Metropolitan. Under Investment Management Houses you'll find Allan Gray, Coronation, Investec Asset Management, Cadiz, Prudential et al. Under Investment Management Companies you have Allan Gray, Coronation, Investec Asset Management, Cadiz, Prudential, OMIGSA, SIM, RMBAM, Stanlib, MetAM et al. What is the difference between investment management houses/companies

Firstly, it is important to note that there is an arms' length agreement between the investment management companies and their clients (for instance, the life office, Collective Investment Scheme Management Company (Manco) and third party clients and segregated portfolios). This agreement is evidenced by an Investment Management Agreement and Mandate. Secondly, Investment Management Companies never own the assets. They manage under power of attorney provided by the client. Thirdly, the Investment Management Companies compete with one another.

How would a Corporate deploy its savings? Corporate Savings may take the form of Net Profit after Tax less dividends and could be utilized to :

1. fund organic growth
2. make acquisitions
3. return to shareholders
4. invest to grow reserves

Curiously there is very little analytical or academic literature available on how Asset Managers work and one is dependent on anecdotal evidence. Yet it is obvious that there is a huge research effort behind investment decisions and some very knowledgeable bright individuals are involved.

In a personal interview Mr Sandy McGregor of Allan Gray stated that his company manages some R 250 billion. He differentiated between investment by companies in their own firms for a variety of purposes, and investment in the financial world which is far more difficult and complex and where decisions are difficult due to incomplete information.

Managing money is quite different to running a company and requires special research and skills.

Where an Asset Manager manages a pension fund there is usually a standard mandate, but once the funds are transferred the Manager has total control. The mandate usually refers to the investment ratio between equities, bonds, derivatives etc and provides a bench mark of the level of risk.

The Asset Consultants who are generally actuaries, or accountants normally serve pension funds. They advise pension funds trustees who may well be lay people.

The Investment Management firms obtain their funds from such entities as Unit Trust Funds, Pension Funds or high net worth individuals. Once an agreement is signed the Manager has total discretion. The first rule is "not to lose money", and they strive to outperform the market, in a highly competitive arena.

I was informed that in the Investment Firms individual managers with special expertise in a specific area are given total freedom with little oversight. They are backed by substantial research to identify which companies equities are to rise in value for later sale to realize a profit, where there are outstanding individual leaders in the business, where there is good cash flow, and generally good performance. The emphasis in these firms, it is suggested, is on good performance in the individual firm rather than more general considerations.

It is argued in the Asset Management industry that good returns are the major driver of investment and that market forces are supreme. Prices of equities are determined by the levels of buying and selling in a totally free for all where no other forces can intervene. More, since South Africa is totally integrated into global markets, equities and bonds are wholly at the mercy of global markets. There is no scope whatsoever for our government to intervene (perhaps short of re-imposing exchange controls). Hence the Investment Managers do not try to set prices, they follow world price trends and try to outperform global markets.

In response to questions about the degree of influence these Asset Managers may have over broad economic decisions, the answer is that they have very little direct power since these firms do not "own" the assets, and investment decisions are individual actions based solely on profit considerations. The flexibility in the system disciplines individuals and the market kills off people who fail. An Investment Manager who learns of mistakes in a firm will immediately sell their shares in that firm.

Also, there are intricate checks and balances, especially with respect to JSE listed companies.

Checks and Balances

We were informed by ASISA that some fifteen years ago the Johannesburg Stock Exchange (JSE) was a kind of "Wild West". Regulation was poor and the Financial Service Board did not exercise proper control. But new professionals

entered the scene and now it is suggested this is the best regulated Exchange in the world. Part of the explanation for the improvement is the new capabilities offered by new technology, the de-materialisation of shares, the need to be competitive globally, and the oversight role of the Competition Commission.

Part of the reason for the change is increased competition between Investment Management firms especially those which operate in the listed market where there are many legislative controls, firms have to be registered and their conduct is monitored systematically. There are also several other controlling factors such as the establishment of Custodians, Trustees, third party administrators, regulators, and the Strate system of the JSE.

Collective Investment Schemes (CIS)

Collective Investment Schemes generally consist of mixed asset portfolios consisting of CISs and other types of assets as determined by the relevant Asset Manager.

Presently CISs control R789 billion

Over-the-counter markets

It is conceded that the over-the-counter markets are imperfect and where much of the problems arise. The culprits are certain commercial and investment banks which create financial instruments without proper controls and their misconduct has a huge contagion effect. Among these are "over the counter" deals such as buying oil futures, Forward Rate Agreements, Forex and Interest Rate swaps and other similar instruments.

In terms of private equity only between 5% and 10 % of a portfolio may go into unlisted entities.. Such investments are generally diversified i.e., in more than one entity.

Hence ASISA wants stronger controls over these sectors. ASISA would like to see clear price discovery which identifies fair prices, transparency, regulation, proper valuation, liquidity, and guaranteed settlements.

The Financial Services Board

According to personal communication from the Financial Services Board, I was informed that the Investment Managers and Asset Consultants in the financial services industry do play an important role.

The Financial Advisory and Intermediary Services Act, No. 37 of 2002 ("the FAIS Act) is administered by the FAIS department of the Financial Services Board ("FSB"). It regulates the licensing and conduct of Investment Managers and who are generally called financial services provider.

The following are four categories of licenses under the FAIS Act:

Category I

A financial services provider who gives advice or renders an intermediary service (e.g. assist a client to enter into a transaction, administering of financial products, collection of premiums etc).

Category II-Discretionary FSP

A financial services provider that renders intermediary services of a discretionary nature as regards the choice of a financial product. Intermediary services will relate to the management of clients assets (financial products}.

Category II A-Hedge Fund FSP

A hedge fund FSP renders intermediary services of a discretionary nature in relation to a particular hedge fund, or fund of hedge funds, in connection with a particular financial product.

A hedge fund means a portfolio which uses any strategy or takes any position which could result in the portfolio incurring losses greater than its aggregate market value at any point in time. Strategies employed or positions taken include but are not limited to leverage or net short positions.

Hedge in relation to a hedge fund, means to enter into transactions that protect against adverse price movements and limit exposures to specific risk.

A fund of hedge funds means a portfolio that, apart from assets in liquid form, consists of an interest, holding or investment in one or more other hedge funds.

Category III-Administrative FSP

A financial services provider that renders intermediary services in respect of financial products through the method of bulking.

Bulking means the aggregation of clients' funds when buying or investing in financial products on behalf of clients and the subsequent allocation of such financial products separately in the records of the financial services provider.

Category IV-Assistance Business FSP

Category IV in relation to a financial services provider, means all persons who require licences as Assistance Business FSP.

Assistance Business FSP means a financial services provider that renders intermediary services in relation to the administration of assistance policies on behalf of an Insurer to the extent agreed to in terms of a written mandate between the Insurer and the Assistance Business FSP.

The applicant must indicate which financial products in each subcategory it wants to render the financial services on.

In terms of the determination of "fit and proper" the applicant must prove that it has at least one person that will render the services that meet competency requirements as stipulated in Part 3 of the Determination.

Licensed financial services providers are required at all times to comply with fit and proper requirements in respect of the following:

Honesty and integrity:

A key individual must be a person who is honest and has integrity. Such person must be candid and accurate and must of his/her own accord disclose all facts or information which may have an impact on the evaluation, by this Office, of its good character and integrity.

The Determination lists six factors to be taken into account in the fit and proper consideration. If any factor applies to an applicant that would indicate (*prima facie*) that the applicant falls foul of the honesty and integrity requirement. Five of the six factors are time-related (over a five year period) to incidents (e.g. criminal conviction or finding in civil proceedings that impact on a person's honesty. In addition to the six

factors an applicant must make full disclosure of any fact or information which may, even remotely, have a bearing on his/her honesty and integrity.

From the answers provided to the questions in the application this Office can determine whether an applicant *prima facie* meets the requirements of honesty and integrity. . However such determination by this Office remains one with an element of discretion, and as a check and balance measure. this Office's decision is subject to the concurrence of the FSB Licensing Committee. (This is a Committee of the FSB Board whose members constitute both Board members and outside appointees). If, after a license has been granted, this Office obtains information which serves to indicate that the honesty and integrity requirements have not been complied with (whether in the meantime or before the license was granted) the necessary remedial action will be taken. which can lead to the withdrawal of a license. Any such decision is subject to an appeal by the applicant.

This Office also performs additional reference checks and, where necessary, criminal checks on applicants. The FSB has build up a comprehensive database relating to persons and entities that have had regulatory action taken against them. All individuals are checked against the database.

An applicant must furnish this Office with certified copies of his/her qualifications and this Office may require references from previous employees to confirm the applicant's experience.

Competence:

The competence requirements consist of:

- a. relevant experience;
- b. a recognized qualification(s); and
- c. the writing and passing of regulatory examination(s) as applicable to the regulatory role of the key individual.

Experience:

Key individuals are required to have at least one (1) year practical experience in the management and oversight of a business. Where a key individual also fulfills the role of the representative, he/she is also required to have a minimum level of experience in respect of all the specific financial products in which he/she intends to render financial services.

Key individuals that only manage and oversee must have completed the Regulatory Examination level 1 at the time of application for approval as a key individual.

The key individuals that manage and oversee the business and in addition, render financial services and give advice (this includes fulfilment of the role of the representative), must meet the same competence requirements as for a key individual. In addition they are required to meet the competence requirements for a representative as stated in the fit and proper requirements.

Operational ability

A key individual must have the operational ability to fulfil the responsibilities imposed by the FAIS Act on financial services providers. This includes oversight of the financial services rendered by the representative.

There are Codes of Conduct for financial services providers and their representatives which include the following:

Codes of Conduct

The FAIS Act makes provision for a Code of Conduct ("Code") for financial services providers. The aim of the Code is to ensure that clients, to whom financial services are being rendered, will be able to make informed choices; that their needs will be appropriately and suitably satisfied; and that the providers and their representatives are obligated to do the following:

Act honestly and fairly, and with due skill, care and diligence in the interest of clients and the integrity of the financial services industry;

Have and employ effectively the resources, procedures and appropriate technological systems for the performance of professional activities;

Seek from clients appropriate and available information regarding their financial situation and financial product experience;

Act with circumspection and treat clients fairly in a situation of conflicting interest; and

Comply with all applicable statutory or common law requirements relevant to conduct of the business.

Besides the Code, there are specific codes of conduct which are applicable to specified providers:

Code of Conduct for authorised financial services providers and their representatives, involved in forex investment business; General Code of Conduct ("General Code") for authorised financial services providers and representatives; Codes of Conduct for administrative and discretionary FSPs; Specific Code of Conduct for authorised financial services providers and representatives conducting short-term deposit-taking business.

All authorised financial services providers are required to comply with the General Code, which imposes specific duties on authorised financial services providers.

In terms of the General Code, the FSP is required at all times to render financial services honestly, fairly, with due skill, care and diligence, and in the interest of clients and the integrity of the financial services industry.

The specific duties of the FSP are the following:

- Representations made and information provided to a client must: -be factually correct; -be provided in plain language, avoid uncertainty and not be misleading; -be adequate and appropriate taking into account the level of knowledge of the client; and -be provided timorously.

There must be disclosure to a client of the existence of any personal interest in the relevant service, or circumstances that give rise to conflict of interest.

There must be disclosure of Non cash incentives.

Transactions of a client must be accurately accounted for.

It is not clear what is referred to by "Asset Consultants". However to the extent that this refers to financial advisors and intermediaries, these will be covered under the above mentioned licensed categories.

Governing the registered funds, there is a Regulation 28, which deal with registered funds and provide for:

(1) Subject to the provisions of sub regulations (2). (3) and (4) and the Annexure to this regulation, a registered fund may invest only in an asset referred to in column 1 of the Annexure to the extent to which the fair value of the investment, expressed as a percentage of the total fair value of the total assets of the fund, does not exceed the percentage listed in column 2 of the Annexure in respect of such asset: Provided that the total fair value of investments in assets

- (a) referred to in items 6 and 7 in column I of the said Annexure, expressed as a percentage, shall not exceed 90%: and
- (b) excluding those referred to in items 1, 2, 3, 4, 5 and (c) and (d) in column I of the Annexure, expressed as a percentage, shall not exceed 95%, and
- (c) in territories outside the Republic referred to in column I of the Annexure, expressed as a percentage, shall not exceed 15% of the total fair value of the total assets of the fund. [Subreg. (c) substituted by GN R2324/93, GN R1667/96. GN R1154/98 and corrected by GN R/218198]

(2) (a) In the application of this regulation with regard to the total assets of a fund

(i) not exempted in terms of section 2 (3) (a) of the Act, units in a unit trust scheme as defined in the Unit Trusts Control Act, 1981 (Act No. 54 of 1981), in respect of which the fund obtained a certificate or certificates that the scheme has met, throughout the period covered by its income and expenditure account, the distribution requirements of assets referred to in the Annexure;

(ii) inclusive of a fund exempted in terms of section 2 (3) (a) of the Act, a policy issued to the fund by an insurer carrying on a long-term insurance business as contemplated in the Insurance Act, 1943 (Act No. 17 of 1943), which-

(b) In the case of a linked policy, in respect of which no certificate as referred to in sub-regulation 2 (a) (ii) has been obtained, the fund shall obtain a statement in writing containing particulars of the extent to which the value of the benefits under such policy is determined by the market value of assets referred to in the Annexure, and the market value of such assets shall be deemed to be assets of the fund and, in the case of a fund exempted in terms of section 2 (3) (a) (ii) of the Act, the certificate shall furnish the reasons for not complying with the aforementioned distribution requirements of assets as referred to in the Annexure.

(c) The certificate or certificates referred to in sub regulation (2) (a) (i) shall be furnished to the fund by the auditor appointed in terms of section 11 of the Unit Trusts Control Act, 1981, at the end of each financial year of the fund and the certificate and statement referred to in sub regulation (2) (a) (ii) and (b) shall also be furnished to the fund at the end of each financial year of the fund or, in the case of a fund which is exempted in terms of section 2 (3) (a) of the Act, at the end of the insurer's financial year by the valuator of the insurer concerned or by the valuator's delegate.

[Para. (c) Substituted by GN R 1 667; 96]

(3) Where the membership of a fund, including any fund exempted in terms of section 2 (3) (a) (ii) of the Act, is not compulsory and the fund operates by means of individual policies or certificates issued in respect of each member of the fund by an insurer carrying on long-term insurance business as contemplated in the Insurance Act, 1943 (Act No. 27 of 1943), such policies or certificates shall not be subject to the provisions of this regulation if the assets held by the insurer in respect of his net liabilities under the said policies or certificates comply with the requirements of regulation 34 of the regulations made under the Insurance Act, 1943 (Act No. 27 of 1943).

(4) In this regulation-

(a) "bank" means a public company registered provisionally or finally in terms of the Banks Act, 1990 (Act No. 94 of 1990); [Para. (a) substituted by GN R1154198]

(b) "linked policy" means a contract under which no investment guarantees are given by the insurer, either explicitly or implicitly, and in respect of which investment benefits are determined solely by reference to the value of specific assets to which the contract is linked and which assets are actually held by or on behalf of the insurer in terms of section 20 (1) of the Insurance Act 1943;

(c) "fair value", in relation to-

(i) the value of every listed asset, means the price at which it was quoted on the Johannesburg Stock Exchange or the Bond Exchange of South Africa within a period of three months immediately preceding the date to which the statement relates, which value shall be shown in the statement at an amount not exceeding the value determined according to the price so last quoted: Provided that if such quotation relates to a date other than the date to which the statement of assets relates the said amount shall be properly adjusted in the case of-

(aa) any interest-bearing asset, by the difference between the amount of the interest which had accrued in the period from the last date on which interest was payable up to the date of the quotation, and the amount of interest accrued for the period to the date to which the statement relates; and

(bb) any share on which dividends have been declared, by the difference between the amount of any dividend which had been declared but not paid on the date of the quotation and the amount of any dividend which had been declared but not paid on the date to which the statement relates:

(ii) assets to which the provisions of sub regulation 4 (c) (i) do not apply, means the value determined in accordance with section 19 (SA) of the Act;

The definition of "fair value" applies *mutatis mutandis* to investments outside the Republic and in such application the reference to the "Johannesburg Stock Exchange or the Bond Exchange of South Africa" in subparagraph (i) must be construed as a reference to "any exchange recognised by the registrar" and the reference to "the Republic" in section 19 (SA) of the Act as a reference to "any territory recognised by the registrar." .

[Para. (e) substituted by GN R1667J96]

(d) "mutual bank" means a juristic person that is provisionally or finally registered as a mutual bank in terms of the Mutual Banks Act, 1993 (Act No. 124 of 1993);

[Para. (d) substituted by GN R1154f98]

(e) "Post Office Savings Bank" means the Post Office Savings Bank constituted in terms of section S2 of the Post Office Act, 1958 (Act No. 44 of 1958);

(f) "property company" means a company-

(i) of which 50% or more of the market value of its assets consists of immovable property, irrespective of whether such property is held directly by the company as registered owner or indirectly by way of ownership of the shares of the company which is the registered owner of the property or which exercises control over the company which is the registered owner of the property; or

(ii) of which 50% or more of its income is derived from investments in immovable property, or from an investment in a company 50% or more of the income of which is derived from investments in immovable property;

(g) "territory outside the Republic" means a territory recognised by the registrar and will include the territories in which the recognised exchanges operates.

[Para. (g) inserted by GN R1154/9S]

(5) The registrar may on prior written application by a fund grant such fund exemption from any of the provisions of this regulation upon such conditions as he may impose.

ANNEXURE TO REGULATION 28

Column 1	Column 2
Item Categories or kinds. of assets	Maximum percentage of aggregate fair value of total assets of fund
1. (a) Inside the Republic- Deposits and balances in current and savings accounts with a bank or a mutual bank, including negotiable deposits, and money market instruments in terms of which such a bank or mutual bank is liable. Paid-up shares of a mutual bank, or, I deposits and savings accounts with the Post Office savings bank, as well as margin deposits with Safex:	100%
(i) Per bank	20%
(ii) Per mutual bank	20%
(iii) Post Office Savings Bank	20%
(iv) SAFEX	5%
(b) Territories outside the Republic-	
Deposits .and balances in current and savings accounts with a bank including negotiable deposits and money market instruments in terms of which such. bank is liable	15%
2. Krugerrands	10%
3. Bills, bonds and securities issued or guaranteed by and loans to or guaranteed by-	100%
(a) inside the Republic -	
(i) a local authority authorised by law 10 levy rates upon immovable property - per local authority	100% 20%
(ii) Development Boards established under the Black Communities Development Act, 1984 (Act NO.4 of 1984)	20%
(iii) Rand Water Board	20%
(iv) Eskom	20%
(v) Land and Agricultural Bank of South Africa	20%
(vi) Local Authorities Loans Fund Board	20%
(b) territories outside the Republic-the foreign Government concerned	15%
4. Bills, bonds and securities issued by and loans to an institution in the Republic, which bills, bonds, securities and loans the Registrar approved in terms of section 19(1) (h) of the Act before the deletion of that section by section 8 (a) of Act No. 53 of 1989, and also bills, bonds and securities issued by and loans to an institution in the Republic, which institution the Registrar likewise e approved before such deletion:	100%
-Per institution	20%

5. Bills, bonds and securities issued by the government or by a local authority in a territory other than the Republic, which territory the Registrar approved in terms of section 19 (1) (i) of the Act before the deletion of that section by section 8 (a) of act No.53 of 1989, and also bills and securities issued by an institution in such an approved territory, which institution the Registrar Likewise approved before such deletion:	100%
-per authority	20%
Immovable property and claims secured by mortgage bonds thereon. Units in unit trust schemes in property shares and shares in, loans to and debenture both convertible and non-convertible	25%
(a) inside republic	25%
Per single property, property company or property development project	5%
(b) territories outside the republic	10%
per single property, property company or property development project	
7. Preference and ordinary shares in companies excluding shares in property companies. Convertible debentures, whether voluntarily or compulsorily convertible and units in equity unit trust schemes. which objective is to invest their assets mainly in shares	75%
These investments are subject to the following limitations:	
(a) inside republic-	75%
Unlisted shares, unlisted convertible debentures and shares and convertible debentures listed in the Development Capital Sector of the Johannesburg stock exchange	5%
Shares and convertible debentures listed on the Johannesburg Stock Exchange other than the Development Capital Sector	75%
(aa) per one company with a market capitalisation of R2 000 million or less	10%
per one company with a market capitalisation of more than R2 000 million	15%
Territories outside republic	
Preference and ordinary shares in companies, convertible debentures, whether voluntarily or compulsorily convertible	15%
(i) Unlisted shares and unlisted convertible debentures	2.5%
(ii) Shares and convertible debentures listed on any recognised foreign exchange	15%
(aa) per one company with a market capitalisation of R2 000 million or less	10%
(bb) per one company with a market capitalisation of more than R2	15%

000 million.	
8. Listed and unlisted debentures, units in a unit trust scheme with the objective to Invest. income generating securities and any secured claim against individuals and companies	25%
(a) inside the Republic-	25%
(i) claims against anyone individual	0.25%
(ii) Claims against any single company	5%
Territories outside the republic-	15%
(i) claims against anyone individual	0.25%
(ii) Claims against any single company	5%
9*. Investments in the business of a participating employer inside the Republic in terms of:	
section 19 (4) of the Act; or	5%
(b) to the extent it has been allowed by an exemption in terms of section 19 (4A) of the act	10%
10. Any other assets not referred to in this Annexure, excluding-	2.5%
money in hand in the Republic;	
(b) loans granted inside the Republic to members of the fund concerned in accordance with- the provisions of section 19 (5) of the Act; and such exemptions as may have been granted to the fund in terms of section 19(16) of the act	
(c) bills, bonds or securities issued or guaranteed by, or loans to or guaranteed by the Government of the Republic or a provincial administration;	
(d) units in a unit trust scheme as defined in the Unit Trusts Control Act, 1981, the underlying assets which consist only of- (i) assets referred to in paragraphs (i), (ii) and (iii) of item 1 (a) of this Annexure; (ii) assets referred to in paragraph (c) of this item; or (iii) assets referred to in items 3, 4 and 5 of this Annexure	
*Effective on promulgation of section 19 (4)	

[Reg. 28 and Annexure added by GN 1920/89 and substituted by GN R1910i89, GN R2361/91 and GN R1667196]

[Annexure substituted by GN R 1154/98 and amended by GN R1218/98]

Glossary of acronym

<u>Term</u>	<u>Description</u>
ASISA	Association of Savings & Investments South Africa
BASA	Banking Association of SA
CIS	Collective Investment Scheme (unit trust)
CISCA	CIS Control Act
CSD	Central Securities Depository
CSDPs	Central Securities Depository Participants
FAIS	Financial Advisory & Intermediary Services Act
FSB	Financial Services Board
IBA	International Banking Association
IRF	Institute of Retirement Funds
JSE	Johannesburg Securities Exchange
SETS	Equity trading platform
SAFEX	Derivatives trading platform
Yield-X	Interest-bearing instruments trading platform
SAFEX	SA Futures Exchange
SAIA	South African Insurance Association (short term insurers)
SARB	SA Reserve Bank

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