

ASISA CONFERENCE

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## **HAS THE SAVINGS AND INVESTMENT INDUSTRY LET SOUTH AFRICANS DOWN?**

**The reality of what the industry has delivered to all South Africans and the South African economy**

### **1. Introduction**

In order to address the question of whether the savings and investment industry (SII) has let South Africans down, I will look at three separate but related issues, namely:

- The **changes** in the industry, particularly since 1990;
- clarification of SII's **role and functions** in order to assess its performance;
- the **role of Asisa** in charting the course ahead.

### **2. A changing environment**

A defining characteristic of the savings and investment landscape in South Africa has been the changing environment and competitive landscape, mainly as a reaction to increased consumerism and regulatory change. This has led to numerous new entrants in SI space with much more, and more efficient, competition.

At the **retail** level, large insurance companies have dominated the SI space mainly owing to two factors, i.e. the barriers to access faced by individuals when buying shares directly, and the tax advantages linked to insurance policies *vis-à-vis* other types of SI products. With the introduction of electronic share trading platforms and the removal of tax benefits associated with insurance products, the playing field was levelled. This allowed several new players to successfully enter the market, eroding the dominant position of the three or four large life insurers.

At the **institutional** level, the balance of power moved from employers to employees with the advent of the virtually *en-masse* move from defined benefits to defined contributions. This led to the fragmentation of the employee benefit value chain with a single integrated provider of all EB-related services answerable to an employer being replaced by different specialist providers in the areas of consulting, administration, risk products and investments, answerable to individual investors and boards of trustees. In time, the investment space, in particular, went through massive change with the advent of new solutions and players, for example multi-managers, specialist asset classes, hedge funds, etc. Consumerism led to ‘value to the client’ being the major driver of change.

These changes in the environment led to the dominant position of life insurers and life insurance products being eroded substantially as new entrants came into the SI space, particularly from 1990 onwards. The life insurers with their expensive cost structures and rigid products initially found it increasingly hard to compete with smaller, and more flexible and nimble, focussed competitors. But they did survive, often by embracing exactly those tactics that the new entrants deployed in order to get a differential advantage.

The result is that today we have an SII that is much more competitive and client orientated with good value for money to clients. Also gone are the days where we have a ‘one size fits all’ approach. Client-centricity and choice are drivers in keeping up with the increased demands of well-informed consumers and their advisers.

### 3. **Role and functions**

At the **micro level** the function of the SII is to provide consumers with cost-effective products and solutions to their financial needs:

- The SII is renowned for its **innovation** in meeting client needs. The high level of competition in the industry ensures that businesses are sensitive to changing client needs and preferences. [SPF provides examples]
- The SII has been particularly adept at adjusting its product offering to serve the needs of the **emerging market** in addition to its traditional market. Its contribution to the promotion of financial literacy should not be underestimated.
- The past two years have highlighted the need for proper **risk management**. At an institutional level, SA institutions in the SII came through the financial crisis with flying colours. At no stage was the financial security of its clients at risk, providing them with enormous peace of mind.
- In addition, the SII has been at the forefront of advising consumers to tailor their investment portfolios to their **tolerance for risk**, and to provide them with the means to structure their portfolios accordingly. The value of **sound**

**financial planning** has been underlined by the financial crisis, and the appropriateness of trends in planning such as life cycle investing has been vindicated.

- Where there have been **disputes** between the SII and its clients, often with the involvement of regulators, the industry has demonstrated its willingness to acknowledge its mistakes and to accept responsibility for them.
- The inclination to vilify the SII for **high costs** and to reject all expenditure on marketing as unnecessary has been taken too far. The SII needs to watch costs closely to protect the value-for-money proposition, but marketing is essential in motivating consumers to save.

At the **macro-level** the SII plays a key role in financial intermediation, viz. the mobilising of savings and the allocation of those savings to competing investment alternatives:

- South Africa is a **capital scarce** country, making the mobilisation of capital an imperative. SA is dependent on inflows of **foreign capital** with all its accompanying instability, and the SII plays a key role in alleviating this constraint.
- The deterioration in Government's finances and the return to **dissaving** by the state will aggravate the savings shortage, requiring all other sectors to take up the slack. The SII can play an important supportive role in achieving this objective.
- The **competitive pressures** in the SII to provide clients with the best possible return at an acceptable level of risk plays an important role in the **efficient allocation** of capital in SA.

- It must always be remembered that the SII invests its clients' money according to an **agreed mandate**. It is an illusion that the asset manager has complete freedom in deciding where to invest; it responds to client needs, which include socially responsible investment.
- The SII has acted as a **counterforce to easy credit** that encouraged consumers to spend more than they earned and could afford. The latter caused the household savings rate to turn negative for the first time in Q4 2005, where it has languished ever since – had it not been for the SII, the situation would have been even worse.
- The role of the SII in supporting other industries in their **growth and development** should be acknowledged more openly. The impression one gains for example from Government's new Industrial Policy Action Plan is that the financial sector is regarded as “unproductive”.
- The idea that **Government has to meddle** in the investment practices of the SII in some way to promote “productive” investment rests on an erroneous understanding of how **financial intermediation** works. The creation of a favourable investment climate will generate profitable investment opportunities to which capital will then flow, not the other way around (viz. that capital is first raised, which then goes out to create its own investment opportunities). If certain projects were to remain unfunded it would be because they offered lesser returns, and the only way to accommodate them would be by enlarging the savings pool and lowering the hurdle rate. Prescribed asset requirements, whether hard

or soft in nature, would merely imply the re-allocation of capital in a sub-optimal manner.

- The idea that investing in **shares listed on the JSE** is somehow unproductive, needs to be addressed. It disregards the linkages between the primary and the secondary capital market. The primary capital market can only do its job properly if it is supported by an active secondary market that provides the necessary exit opportunities and/or liquidity and mechanisms for pricing and/or valuing securities.
- Along with the rest of the financial sector, the SII has been a major **creator of new jobs** in recent years (it increased employment even in the midst of the recession in 2009).
- The South African SII is rapidly expanding into **Africa**, giving citizens access to sophisticated financial services products. South Africa is well positioned to be the financial hub of Africa.

#### 4. **Conclusion: Answer to the question**

The SII has served SA well, both at the level of the individual and also nationally. Competition has increased, costs of saving have come down and the ability to choose has improved. In short, more bang for the client's buck! But why then the questions raised about SII's contribution if the answer is relatively straightforward?

The answer lies, at least partly, in the way the SII has presented itself. In 2008, our industry, our regulator and our policymakers were still dealing with four trade associations representing and

promoting different aspects of the savings and investment industry, often pulling in opposite directions.

Just over a year later we are one under the ASISA banner! Our industry now speaks with one voice and represents the unified goal of ensuring that the South African savings and investment industry remains relevant and sustainable into the future in the interests not only of ASISA and its members, but also the country and its citizens.

Why is it so important that ASISA drives this goal with vigour? ASISA represents the majority of companies active in the biggest sector of South Africa's economy, namely the savings and investment industry. A total of 154 ASISA member companies hold assets of more than R2.6 trillion. A substantial portion of these assets belongs to the citizens of this country. This industry also channels significant amounts of money into critical delivery areas through public/private partnerships.

It is therefore in everyone's interest that this industry remains successful into the future. We fully recognise that the paradigm under which we operated in the past has shifted, and continues to shift. It therefore needs to be renegotiated continuously. ASISA is busy doing just that. The association is a pro-active and committed partner to Government in designing solutions that will hold long-term benefits for all our stakeholders, including the consumer.

With ASISA up and running, our first priority has been to put in place a solid strategy which carries the approval of the ASISA Board. This process has recently been completed and I am pleased to report that the ASISA strategy reflects the priorities of our country, as well as international direction.

As an industry we also need to be cognizant of the fact that our world has changed for the better. The global financial crisis that

started gripping the world in the third quarter of 2008 severely shook the foundations of the various systems under which we operated. South African financial services institutions may have escaped ruin, but nevertheless many of us rushed to re-evaluate the way we do business. And none of us have escaped the dip in consumer confidence.

We need to accept that it is our responsibility as an industry to ensure that appropriate checks and balances are put in place to ensure the principles of good corporate governance are adhered to at all times. Our industry, as represented by ASISA, is also working together with our regulator and policy-makers to ensure robust regulatory structures.

Following the global events of the past 18 months, consumers have been left frustrated and disappointed. South African financial institutions may have survived the meltdown, but South Africa was not spared the pain. For the first time in 17 years, South Africa went into recession in 2009, mainly after a decline in demand for commodity exports as a result of the global economic downturn. In addition, spiralling Eskom tariff increases and job losses put further pressure on inflation. South Africa suffered close to one million job losses.

Unfortunately, some of the negative sentiment has been directed at our industry. There is a common belief in some quarters that the financial services industry has failed the consumer. While I acknowledge that South Africans have certainly shared in some of the pain caused by the global meltdown, I do not believe that the negative sentiment towards our industry is warranted.

Throughout the meltdown the financial services sector maintained its position as the single biggest contributor to the country's GDP and the most important mechanism through which the nation's savings are channelled. Our industry braved the fallout from the

crisis and there was not a single casualty. The only money lost was as a result of extreme volatility in the equity markets, something that we can never influence.

ASISA therefore also faces the challenge of advocating the important role that our industry holds as custodian of our nation's savings and investment, and must help change the perception that the industry has failed the citizens of this country. With our strategic direction clearly mapped out, I am positive that we will succeed in steering the savings and investment industry on to a path of sustainable growth to the benefit of our country and its citizens.

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