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Pension Funds Evolution, Reforms and Trends in South Africa

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Abstract:
This paper gives a historical perspective of the South African pension fund sector using secondary data and desk review of existing literature. The paper shows various legislative frameworks passed by the South African government, spurring reforms in the sector. Providing a descriptive review of the trends of the type and number of funds, total assets under management and legislative reforms provides evidence of the significant developments in the pension fund sector. Analysis of available data shows the contribution of pension funds to the South African economy, the growth trends in funds contribution and the role of the state controlled Public Investment Corporation (PIC). The huge growth of pension funds industry, more particularly the PIC rekindles the debate on how the PIC and its share in the sector can be used for driving growth and employment in the economy.

Keywords: Pension Funds, South Africa, Historical, and Pension Reforms, Public Investment Corporation
1. Introduction

Pension funds in South Africa hold sizable bond and equity holdings. In the South African context the growth of assets under management has increased the liquidity and depth of the local bond and equities markets. Globally, pension funds are critical drivers of the development of the stock or local securities market (Chan-Lau, 2004). It has been shown that stock market development has a positive and significant correlation with growth (Levine & Zervos, 1998; Caporale et al 2005; Beck & Levine 2004). The authors show that investment levels, productivity and growth are significantly correlated with stock markets.

Levine (1997) argues countries with better developed banks and financial systems grow faster than those with weak financial systems. The ability to allocate capital, monitor and provide finance for investments, risk management, mobilization and pooling of savings are some of the benefits of well developed financial systems (Levine, 1997; Levine, 2004). Pension funds contribute to financial systems through capital markets by impacting savings rates, productivity growth and capital accumulation. Many scholars argue pension funds also contribute to capital market development, the extent to which pension savings induce behaviour on capital markets we must understand the reforms and structure of pension systems. This paper seeks to analyse current South African trends as there is a paucity of work in the related field in African economies. South African pension funds have been rising substantially in the last decade and stand out as the third fastest growing pension fund markets globally (Towers Watson, 2014). The focus of the paper will outline the contribution of pension assets to financial markets, the investment patterns and regulatory framework influencing behaviour. The paper is a descriptive piece with no empirical analysis.

In summary we are able to see the pivotal role of the regulatory framework in the development of pension funds. The overarching
legislation continues monitoring and overseeing the sector, whilst regulation of investment allocation and reporting clearly performed by the legislated role of the Pension Fund Regulatory body and Pension Fund Registrar and Adjudicator.

The South African pension system has undergone reforms that can be categorized into 4 phases namely Infancy, Institutionalization, Separation and its continuation, and Corporatization and Amalgamation. Each phase points to changes in the legislation, structure and systemic changes governing pension funds.

Infancy (1911-1958) was the period where institutionalization and establishment of the pension fund system occurred. Separation (1959-1985) followed with the Pension Act of 1956 leads us to a new era of legislation with appointment of Registrar of SA pension funds. The differentiation and growth of the first and third pillar, development of pension funds, stringent oversight gained momentum. Racial separation continued up until 1994 however we see that in the phase between (1985-1994) strengthened union mobility against legislative framework showed the strength of workers in our pension system. The increased influence of workers led to a systemic shift with union support of defined benefit funds versus defined contribution funds. Lastly, the corporatization and Amalgamation (1995–2015) of state funds into a new entity called the PIC and change in investment allocations Regulation 28 entered South African into privatization phase of state assets.

The objective of this paper is to summarize the reforms and trends of South African pension funds. In section two, we explore the linkages between pension funds and capital markets, including their welfare effects. Section three will summarize the contribution of pension funds to the development of South African financial markets. Section four will focus on growth trends and examine some stylized facts. Section five focuses on the role and magnitude of the state owned Public Investment
Corporation in pension assets. Section six concludes the paper with some recommendations.

### 2. Pension funds welfare effects and capital market development

Pension funds have been recognized to play a contributory role in the development of capital markets (Davis, 2006; Hu 2005; Walker & Lefort, 2002; Davis & Hu 2005; Irace et al, 2009). There are various channels through which institutional investors have developed capital markets, but it is important to note that there are necessary preconditions that must be met for pension assets to develop capital markets (Meng & Pfau, 2010). An important precondition is the level of financial development; the higher the level of financial development the more significant the impact of pension funds. The dynamic interaction between pension funds and the financial markets is stronger in a well developed financial market. Financial development determines the level of optimization that can be derived from pension funds. The indicators for level of development depend upon macroeconomic conditions, market efficiency, transparency and pension fund investment regulations and the legal framework (Vittas, 1999).

Pension assets differ from household assets as they have a long-term outlook. They provide long-term supply of funds to capital markets, especially in the bond markets, leading to financial development (Meng & Pfau, 2010; Davis, 2005). The size of pension assets enables them to hold greater proportions of equities and bonds than households (Davis, 2006). Empirical work by Hu (2005) found that increased size of pension assets encourage private bond finance in both the short and long run.

According to Walker and Lefort (2002) pension systems behaviour enable them to contribute to lowering transaction costs, diversifying risk and holding superior ability to process information. These characteristics enable the improvement of allocation of invested funds,
and financial intermediaries resulting in better resource allocation. These coincide with factors within the financial markets that lead to enhanced growth (Levine, 1997; Raisa, 2012). Stock markets also enhance growth by providing incentives for long run investments.

Pension funds contribute to the loan and securities market, improving competitiveness as they compete with the banking sector. It is argued that efficiency is improved as lending rates, and spreads are lowered reducing firm and household costs for accessing capital. The issue of qualitative impact of pension funds that trigger innovation in financial systems has also been identified as a benefit. New instruments, the modernization of infrastructure and improved regulations occur as a consequence of the development of pension funds resulting in the overall advancement of the financial sector through greater transparency and market efficiency (Davis, 2006; Davis, 1995). The contribution of pension assets to the lowering of prices in the market is linked to a variety of factors. Pension fund assets reduce dividend yields and increase price-to-book ratios, thereby implying a decrease in the cost of capital (Walker & Lefort, 2002).

Pension assets impact aggregate private savings (Barr, 2000). It is these savings that result in investment, this increased investment then leads to enhanced output. The pension system of a country determines the extent of the enhanced growth. Personal savings may be eroded by how the government finances pension reform, thus decreasing total impact of personal savings. Implicit debt is raised when governments move from Pay As You Go (PAYG) to Fully Funded Schemes (FFS). It is important to look at country specific debt raised, tax conditions and overall obligations before concluding that savings are automatic. Savings are automatic only when regulatory framework enforces conditions whereby pension contributions are compulsory (Bailliu & Reisen, 1997; Lopez & Musalem, 2004). They also confirm that forced pension savings will raise overall savings. This emphasizes the link between institutional capital and an adaptive legal framework.
Furthermore, empirical work shows that privately managed funded schemes increase personal savings, when in a fully funded context versus unfunded system (Balliu & Reisen, 1998; Bebczuk & Musalem, 2006; Irace et al 2009).

Pension assets are not only able to accelerate capital market development, but in addition improve welfare. Using the World Bank model for pension funds can be divided into three pillars (Hu, 2005; Rhodes & Natali, 2003; Holzmann & Stiglitz, 2001). The first pillar is a distribution pillar financed by taxes that is managed by the public sector as a means to eradicate poverty. The main aim of poverty alleviation and prevention constitutes a significant portion in South Africa’s state pension system. The assumption that the working age population was able to save whilst working, or even find work during the years of employment does not always hold globally, more so in South Africa. Job insecurity, income instability and informal employment make it even harder for workers to save for their old age (Uthoff, 2006). Van den Heever (2007) estimated 5.4 million people, an estimated 47.8% of the working population do not participate in contributory schemes though employed. This includes a large portion of informal workers who are excluded from participating in pension systems. Translating to a greater fiscal burden on the state through social grant reliance in times of retirement.

It can be argued South Africa has a strong privatized occupational system regime with private personal schemes (in both the public and private sector), and a wide reaching non-contributory public financed pension system that is intended for poverty alleviation. The private personal schemes contributing to the second and third pillars of a pension system exhibit a direct effect on financial system. Rhodes and Natali (2003) emphasize that the pension system adopted is also determined by the social risks and need for social protection. The demand for social protection is reflected in poverty and inequality
indicators and the ability of the state to meet the needs of its citizens will be tested by the overarching policy framework and the national budget.

South African financial markets exhibit universal plus occupational schemes and means tested public pension provision schemes. Pointing South Africa to a commodified privatized pension system which also exhibits strong signs of a decommodified pension system whereby tax financed pension provision takes a predominant role. Uthoff (2006) describes the main role of social pensions as providing the elderly poor with income, and stresses that great demand for social protection exists when a nation’s has high dependence ratios and low per capita income. South Africa exhibits both constraints, and in this context the welfare effects are enormous as it is the worlds most unequal society according to the Gini coefficient. South Africa’s social grant system comprises a total of 15.9 million beneficiaries, of that 2.9 million are old age pensioners (Sassa, 2014a). The national social grants expenditure on Old Age Grants was 40% of total expenditure as reported in the fourth quarter of 2014 at R44 billion of the total R109 billion total expenditure (Sassa, 2014b). The economic sustainability of social protection programmes is dependant on the national fiscus and covered by taxes, it has no linkages to contributions made. This factor determines the financial viability of pension programmes that carry significant costs but are designed to respond to labour market problems. The extent to which a country is able to finance the need for grants may lead to reforms in the sector, however high levels of unemployment, an old age population dependant on the state for assistance and the need to mitigate poverty and inequality will continue to be drivers propelling state funded social protection.

In summary pension systems display unique characteristics based on the country specific labour market nuances, stage of demographic transition, public finances and growth levels. There are different needs in an economy with the mix between public and private pension schemes positioned to service that. Pension assets dependent on the prevailing
economic conditions of a country, are able to improve welfare conditions and positively impact capital market development and growth through reduction of transaction costs, market volatility and the reduced cost of capital for firms. This is also enhanced when concurrently, increased corporate governance and liquidity is experienced. Increased specialization occurs as a spinoff usually leading to diversified financial instruments (Raisa, 2012).

3. The evolution of South African pension funds

The South African financial sector has strong banking and non-banking financial institutions. The robustness and financial depth of the banking sector is arguably one of the most sophisticated in the world, with influence on the financial development and growth. Bisignano (1998) observes that the size of the banking sector has shrunk relative to total financial assets. One of the reasons for this shrinkage in proportion of total assets held by banks is the rise of institutional investors, particularly in the last three decades, see Figure 1 (Sibanda & Holden (2014). Institutional investors manage innovative securities, surplus funds and savings. These institutional investors take the form of pension and provident funds, short and long term insurance companies, mutual funds or collective investment schemes.

The South African pension fund sector was highly segregated and different systems were in place due to the legacy of apartheid. This meant that the South African government differentiated pension schemes between independent states or homelands and the Republic of South Africa. Each had their own separate pension schemes divided on racial grounds (Hendricks, 2008). The regulatory bodies managing pension schemes also evolved over time, with several pieces of legislation affecting the management of pension schemes. These will be discussed in the different phases of reform.
The pension fund sector total assets under management contribute a staggering R2.7 trillion to the South African economy (Financial Services Board, 2012). According to Sibanda and Holden (2014) the level of total assets of institutional investors as a % of GDP had reached 186% in 2009 from a level of 125% in 1994. The increasing contributions of institutional assets in the financial sector see it playing a more significant role. It is important to note that South Africa’s total pension assets are recognized as one of the largest pension markets in the world. According to the Towers Watson global assets pension study they are ranked at number 10 in size, and make a small contribution of 0.7% to the total world’s pension assets (Towers Watson, 2014). This translated to $236 billion in total assets as at year-end in 2013, bigger than France, Hong Kong and Ireland’s pension market share.

Table 1: Banking and Non Banking Sector Financial Assets

<table>
<thead>
<tr>
<th>Year</th>
<th>GDP [R millions]</th>
<th>Total Bank Assets [R millions]</th>
<th>Total Bank as % of GDP</th>
<th>Total Assets: Non Bank [R millions]</th>
<th>Total Non Bank as % of GDP</th>
<th>Total Non Bank assets: Assets Non banking</th>
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<tr>
<td>2001</td>
<td>2 008 181</td>
<td>1 050 068</td>
<td>52%</td>
<td>1 715 002</td>
<td>85%</td>
<td>61%</td>
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<tr>
<td>2002</td>
<td>2 081 837</td>
<td>1 102 860</td>
<td>53%</td>
<td>1 739 310</td>
<td>84%</td>
<td>63%</td>
</tr>
<tr>
<td>2003</td>
<td>2 143 232</td>
<td>1 381 843</td>
<td>64%</td>
<td>1 919 677</td>
<td>90%</td>
<td>72%</td>
</tr>
<tr>
<td>2004</td>
<td>2 240 847</td>
<td>1 498 619</td>
<td>67%</td>
<td>2 272 156</td>
<td>101%</td>
<td>66%</td>
</tr>
<tr>
<td>2005</td>
<td>2 359 099</td>
<td>1 677 652</td>
<td>71%</td>
<td>2 768 288</td>
<td>117%</td>
<td>61%</td>
</tr>
<tr>
<td>2006</td>
<td>2 491 295</td>
<td>2 075 157</td>
<td>83%</td>
<td>3 415 389</td>
<td>137%</td>
<td>61%</td>
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<tr>
<td>2007</td>
<td>2 624 840</td>
<td>2 546 788</td>
<td>97%</td>
<td>3 867 503</td>
<td>147%</td>
<td>66%</td>
</tr>
<tr>
<td>2008</td>
<td>2 708 600</td>
<td>3 166 502</td>
<td>117%</td>
<td>3 797 520</td>
<td>140%</td>
<td>83%</td>
</tr>
<tr>
<td>2009</td>
<td>2 666 939</td>
<td>2 962 613</td>
<td>111%</td>
<td>4 254 613</td>
<td>160%</td>
<td>70%</td>
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<tr>
<td>2010</td>
<td>2 748 008</td>
<td>3 121 782</td>
<td>114%</td>
<td>4 815 447</td>
<td>175%</td>
<td>65%</td>
</tr>
<tr>
<td>2011</td>
<td>2 836 286</td>
<td>3 405 067</td>
<td>120%</td>
<td>5 124 252</td>
<td>181%</td>
<td>66%</td>
</tr>
<tr>
<td>2012</td>
<td>2 899 248</td>
<td>3 648 222</td>
<td>126%</td>
<td>6 011 956</td>
<td>207%</td>
<td>61%</td>
</tr>
<tr>
<td>2013</td>
<td>2 963 389</td>
<td>3 836 199</td>
<td>129%</td>
<td>6 921 203</td>
<td>234%</td>
<td>55%</td>
</tr>
</tbody>
</table>

Source: (Authors own compilation using data from the South African Reserve Bank, Financial Services Board, 2001-2014)  

3 Total Non Bank assets refers to Non Banking financial institutions outlined in footnote 5  
4 Significant contribution to banking assets is largely from cash and balances with central bank, loans, investment of all types, pledged assets, intangible and non-current assets. Total banking
The levels of non-banking versus banking assets from 2001 to date has been higher coupled with the rate at which non-banking assets grow far exceeding bank assets growth. The assets in relation to GDP confirm the trend. Secondly, the total non-banking assets are considerably larger at R6.92 trillion versus banking total assets of R3.84 trillion in 2013. This points to institutional investors playing a more pivotal role in financial markets.

Figure 1: Banking and Non Banking Assets (as % of GDP)

![Financial Structure: Banks and Non banking assets: GDP](source)

Source: (Authors own compilation using data from the South African Reserve Bank, 1994-2014)\(^5\)

\(^5\) Figure 1 shows the trend in financial assets in relation to GDP. Non banking assets include Institutional investors, comprise of unit trusts, the Public Investment Corporation (PIC), long and short term insurers, public and private pension and provident funds, participating mortgage bond schemes, finance companies and non monetary public financial corporations.
3.1 Infancy: At the beginning (1911-1958)

According to Van der Berg (2002) South Africa’s first pension fund was introduced in the Transvaal Republic in 1882. The institutionalization of South Africa’s pension funds dates back to 1911 when the Public Debt Commissioners Act of 1911 was passed. The Public Debt Commissioners Act marked the beginning of the presently known PIC. The new Act made provision for holding state assets and using them to finance government budget deficits (Hendricks, 2008). Its functions over the next few decades expanded to the provision of loans to government and state entities such as Rand Water Board and Eskom. It also provided funds to provincial administrations (FSB, 1959). This was a single government entity that was able to manage and control government funds. The pool of government money was a tool for government to also borrow from itself.

Amongst these funds were Industrial agreements that were entered into with Industry Councils binding employers to offer competitive benefit packages to its employees (Van der Berg, 2002). A total of 2771 funds existed with a total membership of 675 404 in 1958. This comprised of eleven state controlled funds, 599 privately administered funds, with the majority 2147 underwritten funds (FSB, 1959).

3.2 Separation (1959-1984)

The second phase in the evolution of the pension fund sector was when the Pension fund registrar was appointed. The institutional and regulatory framework for the sector experienced further improvements. The first Annual Report (1959) published by the Registrar of South African pension funds states that the existence of such a body was to manage and play an oversight role for pension funds. The passing of the Pension Act of 1956 and establishment of a regulatory institution is deemed to be pioneering. The Registrar states in that era it was globally one of the most comprehensive and detailed regulatory tools managing pension funds. It set in place the classification of various types of pension funds that are still used to differentiate pension funds in the
market. The annual reporting of all fund assets and liabilities, number of funds, members, amounts paid out as annuities and gratuities across privately administered, state controlled, foreign and exempt or underwritten funds was established. Official statistics and trends have been recorded from 1959 to date, and it provides fund trends in the South African context.

The Pension fund Act that was the first of its kind globally. It is for this reason it was said to be somewhat experimental in the first Annual report. Where the Act was found to be impractical the necessary adjustments would be made to the Act as it was implemented (FSB, 1959). Registration as a pension fund would be conditional upon complying to the Act’s definition and meeting the stringent requirements of being financially sound. Once the Office of the Registrar was satisfied that a pension fund met its requirements it was registered, failing which registration was halted whilst arrangements were made to the Office of the registrar to enhance readiness to its satisfaction. The cancellation of funds for various reasons, amongst them fraudulent activities would be imposed as part of the Act. Pension funds would annually provide audited financial statements outlining their financial condition. These conditions contributed to the strengthened regulatory framework and development of funds into this next era.

The territory set aside for African inhabitants during the apartheid era was known as Transkei, Bophutatswana, Venda, and Ciskei (TBVC) whereby separate autonomous states were created for indigenous South African people. It is not clear whether the Pension Funds Act was applied consistently across South Africa and the TBVC homelands. These homelands were seen as separate administrations and were governed separately with separate development plans. It is likely though that pension reform was not as stringent and the Act was not applied to its full level of requirements, as these were a people deemed inferior by the apartheid government. Non-contributory pensions were racially fragmented prior to convergence to a means tested level until
Prior to the equalization of state grants, whites earned more than ten times their African counterparts at R322 versus R31.

The Preservation of Pension Interest Bill that was withdrawn by Parliament after facing fierce opposition from trade unions (Van der Berg, 2002). It was promulgated in 1981 by the government and it sought to preserve pension rights of funds upon member withdrawals. This meant that workers upon leaving employment with a specific firm would be unable to access their savings from retirement income. The issue was polarized by legislation inhibiting Africans from accessing unemployment insurance, this payout proved to be an important safety net in times of labour mobility. This Bill also propelled trade unions to start their own provident funds, which were the first non-contributory schemes for Africans (Van den Heever, 2007). Trade unions strongly influenced restructuring of regulations to the benefit of employees. A major shift experienced in the 1980s was the movement from defined contribution funds to defined benefit funds. A shift attributed to the improved benefits faced by employees in defined benefit funds, supported by trade unions (Van der Berg, 2002; Standish & Boting, 2006).

By the end of this period there were 11,929 registered pension funds covering a membership of 5,124,439. Total assets under management had grown to R21.1 billion by 1984.

3.3 Continued Separation (1985-1994)

Entry into this phase is the passing of Public Investment Commissioners Act of 1984. It strengthened the regulatory role of the sector. Public Investment Commissioners were appointed to control and play an investment management role over public funds. Public funds were invested only in the bonds and fixed interest market but by mid 1990’s equity such as ordinary and preference shares received an allocation of public funds. The total market value of shares held by funds as at year-end of this period of 1984 was only R6.1 million (FSB, 1984). During the
period up to the first held democratic elections, the public investment commission maintained a close relationship with the apartheid government fulfilling its mandate as a debt provider to government. (Hendricks, 2008).

In this period Self-Administered, Underwritten and Foreign Funds were joined by Official Funds, which were administered by the Department of National Health and Population Development and by the South African Transport Services. In 1991 the establishment by the Department of Finance of the Transnet Pension Fund Act, no 62 of 1990 exempted these funds from certain provisions of the Pension Funds Act. Other such exempted funds include the Telkom and the Post Office Funds. Legislation was amended enabling this. Foreign funds dwindled towards the end of this era.

An amendment in the allocation of assets was passed; the abolishment of investing 53% of assets in prescribed assets was done away with (FSB, 1988). A new format had to be developed as new categories of assets came into operation in 1989, these changes had to be incorporated in the investment patterns of pension funds. Competitiveness was also introduced in 1994 with the PIC buying stocks on a competitive basis, which was a new development (PIC, 2011).

Government policy and legislation in the next phase would be influenced reports and investigations commissioned by the Mouton Committee of 1992 and the Katz Commission on Tax reform of 1995 (Van der Berg, 2002). The terms of reference for the Mouton Committee of inquiry was to investigate and make recommendations regarding principles that should apply for a retirement provisions system in the Republic. The report made 104 recommendations that would be the foundation for reform in the sector in the next phase (FSB, 1991). The large majority of the population was not covered for retirement in their old age. Only an estimated 5.5 million people’s retirement needs were covered versus 9 million people between the ages of 15-64 who weren’t members of any
retirement fund (Van der Berg, 2002). Various reports on the issue of social security and social protection as a means to combat poverty had also been commissioned by the state pre and post 1994. The crucial linkage between pension funds and poverty is that social policy is crucial for combating poverty upon retirement in the form of old age pensions where private savings have not been possible. The South African pension fund sector was well developed entering into the post 1994 era, and the coverage for the formally employed was noted as highly developed. The impoverished and those without employment were economically excluded and social security policy had to ensure the inclusion of pension benefits for the millions of South Africans whose retirement needs were not covered during this era.

3.4 Corporatization and Amalgamation (1995 – 2015)
Several changes were seen in this next phase of the pension fund sector. Exempt Funds section 2(3)(a) were changed to Underwritten funds. Bargaining Council Funds were established, previously known as Industrial Agreements. The Government Employees Pension Fund (GEPF, n.d) was established. An important change is that state controlled funds were now formally managed by the PIC.

Several other reports commissioned include Smith Report of 1995, Lund Committee report of 1996 and the Taylor report of 2002. The latter two were produced in the period leading up to the corporatization of the biggest fund in South Africa.

It was in 2004 whereby the Public Investment Corporation Bill was amended, and the previously known Public Investment Commissioners were given a legal mandate to act as asset managers. The Public Investment Corporation Act transferred all the state assets to the Public Investment Corporation (PIC). The state assets would be derived from the GEPF and other state entities, such as the Unemployment Insurance Fund. The state remained in control of the fund as it attained its status as the sole shareholder, through the Minister of Finance to whom the
The Board of Trustees would be accountable. The PIC manages government funds, but is not accountable to government but to the Minister, an anomaly given the extent of assets under management. Hendrik (2008) argues that the PIC behaves no differently to a private asset management firm and it seeks returns and profits, rather than development or poverty alleviation. The PIC confirms this view with its centenary publication stating that it operates similarly to a typical asset management firm (PIC, 2011).

The Investment Policy of South Africa’s GEPF managed by the PIC outlines that the strategic asset allocation must be spread across domestic and foreign equities and bonds. It is this 5% allocation of equities and bonds, whose investment contributes towards economic and social infrastructure, and job creation. Furthermore the 5% allocation to the Isibaya and Pan African Infrastructure Development Fund targets social and economic infrastructure, job creation, BBBEE and environmental sustainability is inadequate given South Africa’s economic profile.

Pension funds act as social safety nets in a structurally unbalanced economy. South Africa, similar to Latin American countries is characterized by high levels of income inequality, low growth and investment levels, per capita GDP levels better than most of Africa but inadequate to reducing unemployment and poverty levels. It is important therefore to strengthen both regulatory framework in the management of the second and third pillar, but also the coverage of the non-contributory schemes.

4. Pension Fund Industry Growth Trends

The Towers Watson Global Pension Asset Study (2014) is an international pension fund growth study that is published annually analyzing trends in the pension fund sector. It shows South Africa’s
compounded annual growth rate of 14% is the highest annual growth over the past decade in the world. Followed by Australia (12%), Hong Kong (12%) and the United Kingdom (11%). The world average is 6.5% over the same period, showing that the South African growth far exceeds market average. This could be attributed partly to the growth in the total number of funds and total membership (Figure Two).

Figure 2: Number of registered funds and Total Membership (1959 – 2012)

![Number and Membership of SA Pension Funds](image)

Source: (Authors own compilation using data from the Registrar of Pensions, 1959-2014)

The total number of members has risen from 675 404 to 15 million individuals between 1959-2012 (FSB, 2012). Standish and Boting (2006) argue that the number of active members hasn’t moved substantially. South Africa’s number of members remained under 10 million members until 2005. It’s been in the last decade where a steady rise to the current 15 million members occurred. Van der Berg (2002) outlines that up to 69% of the South African labour force would be reliant on state old age social pensions in their old age. More than 75% of South African pensioners rely on the means tested social grants for
income post retirement (Stewart & Yermo, 2009). The coverage of private and state controlled pensions remains severely limited despite a well regulated and highly development pension system.

The National Development Plan records the labour force at 17.5 million in 2010, with a labour force participation rate of 54% (National Planning Commission, 2013). The majority of South Africans are excluded from formal participation in the labour market and this would explain the numbers of total pension fund members not capturing the majority of South Africans. There is no existing data on the informal labour market and its contribution to the pension fund sector.

A decline in the number of pension funds has also been experienced as shown in Figure 2. This however is explained in more detail by the fluctuations in the type of funds registered in the sector. The rankings according to the asset size are shown in detail in Figure 3. The governance of funds is the responsibility of trustees who oversee regulatory compliance of the fund. According to Stewart and Yermo (2009) more than 80% of South African pension funds have less than 100 members, which has raised concerns about the availability of well-trained trustees to govern these funds.

Figures 3 shows the total assets under the management of the pension fund sector. The year on year growth flourished post-independence and can be attributed to both performance and growth in the contributions from the number of members as seen in Figure 2. The South African pension fund sector is the largest in Africa.
The Total assets under management grew in 1991 from R157.8 billion substantially to R2.7 trillion in two decades (Financial Services Board, 2012). The concentration of assets is mainly in privately self-administered, underwritten and GEPF funds. In 2012 privately administered pension funds contributed R1.29 trillion and the GEPF R1.05 trillion, together making up more than 85% of the total assets under management in the financial markets. Although underwritten funds are larger in number, by 2012 they only contributed 11.76% to total

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6 Telkom, Post Office and Industrial Agreements Funds are calculated but no reflected in the graph due the scale which disables visibility because their contribution to the total is very small. Industrial Agreements from 1995 became Bargaining Council Funds and a variety of funds inception was 1995 such as Transnet, Telkom and the Post Office. The GEPF was also established in mid 2000s.
pension assets. The trends in the types of funds exhibit the same pattern. Table 2 shows that the total number of funds recorded in 2012 has risen over the 50-year period from 3075 funds to a more than double 6581 in 2012. The number of privately administered funds has seen a sharp increase of 372% rising from 662 to 3128 funds. The post democratic era of 1994-2005 period sees a 66% rise in the number of privately administered funds, translating to 1393 funds being registered during this period. Underwritten Funds made up more than 75% of the number of registered funds, rising to levels of over 90% in the late 1980s and 1990s, this substantially decreased in the last decade post 2000. The sharp decline in the number of underwritten funds results in a low rise over the period of only 46%. Standish and Boting (2006) attribute the decline of the number of funds to the move towards umbrella funds.

There are several funds not supervised under the Pension Funds Act of 1958, namely Official Funds, the Government Employees Pension Fund (GEPF) and parastatals such as the Post Office Pension, Transnet and Telkom Funds. National Treasury supervises these funds.
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<tbody>
<tr>
<td>Privately/Self Administered Funds</td>
<td>662</td>
<td>674</td>
<td>810</td>
<td>798</td>
<td>788</td>
<td>1032</td>
<td>1375</td>
<td>2094</td>
<td>3056</td>
<td>3487</td>
<td>3340</td>
<td>3292</td>
<td>3128</td>
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<td>Underwritten Fund/Exempt Funds</td>
<td>2358</td>
<td>2768</td>
<td>5548</td>
<td>6046</td>
<td>10265</td>
<td>10953</td>
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<td>9888</td>
<td>6776</td>
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<td>Industrial Agreements</td>
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<td>16</td>
<td>13</td>
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<td>State Controlled Funds/GEPF</td>
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<td>14</td>
<td>14</td>
<td>11</td>
<td>10</td>
<td>9</td>
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<td>Foreign Funds</td>
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<td>35</td>
<td>27</td>
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<tr>
<td>Total</td>
<td>3075</td>
<td>3510</td>
<td>6435</td>
<td>6910</td>
<td>11102</td>
<td>12026</td>
<td>14610</td>
<td>15089</td>
<td>15587</td>
<td>13390</td>
<td>10123</td>
<td>9505</td>
<td>6581</td>
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</tbody>
</table>

Source: (Author’s own compilation data sourced from Financial Services Board, 1959-2012)
The information provided in Table Three indicates that the largest % of total assets has been invested in Insurance policies in the last 2 decades. During 1992-2005 an average rate of 23% was invested in the asset class, rising to an average 47% in the last five years. This is because all fund types were reported on by the Registrar post 2005, prior investment allocation up to the year 2005 reflects the allocation of only self administered funds in their Annual Reports. The inclusion of underwritten, foreign and state controlled funds has strongly influenced the rise in allocation. Investment in shares in companies during the period 1992-2005 averaged 32%, however when additional fund allocation (inclusion of underwritten, foreign and state controlled funds) the average drops to 22%. Bills, bonds or securities issued over the 20-year period account for a 9% average and Krugerrands a meagre 5.2% average. There is no significant shift between privately administered funds and all other funds. This is consistent for all remaining asset types. It is post 2005 where foreign investments are shown reaching a high of 13% allocation of the total investment portfolio of pension funds. Debentures, Loans and immovable property cumulatively receive less than 5% of the investment allocation over the period under review. Section 28 Regulation sets out parameters and limitation for investment in each asset type, the Pension fund registrar also assesses compliance by funds to this regulation.
Table 3: Investment Portfolio of Funds (% of Total Pension Fund Assets)

<table>
<thead>
<tr>
<th>Year</th>
<th>Immovable property</th>
<th>Bills, bonds or securities</th>
<th>Debentures</th>
<th>Loans</th>
<th>Shares in companies</th>
<th>Equities</th>
<th>Collective Investment Schemes</th>
<th>Unit Trusts</th>
<th>Insurance and Policies</th>
<th>Deposits</th>
<th>Krugerrands</th>
<th>Foreign Investments</th>
<th>Other Assets</th>
</tr>
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<td>1992</td>
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<td>0.1</td>
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<td>-</td>
<td>29.6</td>
<td>8.2</td>
<td>-</td>
<td>9.5</td>
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<td>0.4</td>
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<td>-</td>
<td>26.8</td>
<td>9.3</td>
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<td>2.2</td>
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<td>0.3</td>
<td>47.7</td>
<td>-</td>
<td>24.6</td>
<td>7.5</td>
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<td>1996</td>
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<td>0.5</td>
<td>43.0</td>
<td>-</td>
<td>26.2</td>
<td>5.4</td>
<td>-</td>
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<tr>
<td>1998</td>
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<td>14.3</td>
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<td>37.4</td>
<td>-</td>
<td>26.1</td>
<td>6.4</td>
<td>-</td>
<td>6.0</td>
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<tr>
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<tr>
<td>2005*</td>
<td>0.6</td>
<td>8.6</td>
<td>0.1</td>
<td>0.1</td>
<td>23.3</td>
<td>5.5</td>
<td>47.6</td>
<td>4.3</td>
<td>7.8</td>
<td>2.1</td>
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<tr>
<td>2006</td>
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<td>8.0</td>
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<td>0.1</td>
<td>22.0</td>
<td>5.2</td>
<td>47.3</td>
<td>4.8</td>
<td>9.9</td>
<td>1.7</td>
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<tr>
<td>2009</td>
<td>0.7</td>
<td>7.4</td>
<td>1.1</td>
<td>0.1</td>
<td>18.0</td>
<td>7.3</td>
<td>48.0</td>
<td>6.2</td>
<td>9.5</td>
<td>1.7</td>
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<tr>
<td>2010</td>
<td>0.7</td>
<td>7.1</td>
<td>1.2</td>
<td>0.1</td>
<td>19.0</td>
<td>7.6</td>
<td>46.4</td>
<td>6.3</td>
<td>10</td>
<td>1.6</td>
<td></td>
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<tr>
<td>2011</td>
<td>0.7</td>
<td>7.5</td>
<td>1.1</td>
<td>0.0</td>
<td>18.8</td>
<td>7.9</td>
<td>45.9</td>
<td>5.1</td>
<td>11.8</td>
<td>1.2</td>
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<tr>
<td>2012</td>
<td>0.7</td>
<td>8.1</td>
<td>0.5</td>
<td>18.0</td>
<td>8.4</td>
<td>44.8</td>
<td>5.0</td>
<td>13.0</td>
<td>1.5</td>
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<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: (Author’s own compilation data sourced from Financial Services Board, 1992-2012)

*Investment in collective investment schemes started in 2005 and unit trusts were discontinued post 2005. Shares in companies also started in 2005. Investment in collective investment schemes started in 2005 and unit trusts were discontinued post 2005. Shares in companies also started in 2005. Investment in collective investment schemes started in 2005 and unit trusts were discontinued post 2005. Shares in companies also started in 2005. Investment in collective investment schemes started in 2005 and unit trusts were discontinued post 2005. Shares in companies also started in 2005. Investment in collective investment schemes started in 2005 and unit trusts were discontinued post 2005. Shares in companies also started in 2005. Investment in collective investment schemes started in 2005 and unit trusts were discontinued post 2005. Shares in companies also started in 2005. Investment in collective investment schemes started in 2005 and unit trusts were discontinued post 2005. Shares in companies also started in 2005. Investment in collective investment schemes started in 2005 and unit trusts were discontinued post 2005. Shares in companies also started in 2005. Investment in collective investment schemes started in 2005 and unit trusts were discontinued post 2005. Shares in companies also started in 2005. Investment in collective investment schemes started in 2005 and unit trusts were discontinued post 2005. Shares in companies also started in 2005. Investment in collective investment schemes started in 2005 and unit trusts were discontinued post 2005. Shares in companies also started in 2005.
5. The role of the Public Investment Corporation

The PIC is a wholly state owned Investment Management Company. It was formed in 1911 and it became a corporate entity when the PIC Act of 2004 was passed in April 2004. The PIC is a financial services provider in terms of the Financial Advisory and Intermediary Services Act thereby allowing it to invest funds on behalf of its members. Its main objective is to manage client investments and ensure returns that exceed benchmarks. The PIC manages the Government Employees Pension Fund, Unemployment Insurance Fund, Compensation Commissioners, Political Office Bearers Fund and the Associated Institutions Pension Fund. It also seeks to ensure client and customer satisfaction. It has secondary objectives of managing risk return attribution levels and practicing effective enterprise risk management. It also seeks to contribute positively to South African development by investing 45% of its mandated funds to the Isibaya fund. This fund comprises equity investments in social and economic infrastructure, environmental sustainable projects, and investment in priority sectors that will foster growth, BBBEE and job creation. The Board of Directors of the investment company are appointed by the Minister of Finance in consultation with Cabinet, seven of the Directors are Non Executive Directors.

According to the PIC Annual Reports (2011) the GEPF historically and to date contributed a minimum of 90% to the funds on behalf of which the PIC invests. According to the GEPF Investment Policy Statement (2011) there exists a special relationship between the PIC and the GEPF. A mandate has been given to the PIC to act as the funds asset manager over a substantial portion of the funds assets. Without the contribution of the GEPF, the PIC would likely cease to function in its existing capacity. Where the PIC does not manage the assets of state employees, agreements must be entered into with the mandates drawn from the GEPF for other asset managers. The active members of the GEPF are employees who work in national and provincial governments, including armed forces and correctional services department.
It is recognized by the GEPF Investment Policy that the sole mandate of the establishment of the PIC is to manage GEPF assets. It is also a public entity and it must comply with the Public Finance Management Act. According to the PIC Act of 2004, the state is the sole shareholder of the PIC and the Minister of Finance is the shareholder representative. This policy change has led to little political interference in the management of the PIC. In fact the strengthened independence and autonomy of the PIC has led to the harsh critique by Hendricks (2008) of operating a privately run, state owned entity that does little to drive the urgent developmental agenda of the country.

The growth of assets in the PIC has been significant in the last three decades (Figure 4).

**Figure 4: PIC Total assets growth**

![PIC Total Assets](image)

Source: (South African Reserve Bank, 2015)

Over the last decade we have seen the PIC contribute almost half of the total South African pension asset funds. In the year ending 2012, the PIC assets under management exceeded a trillion contributing to 49% of the total pension assets in the financial system. The contribution of state employees pension funds to the financial development of the South African economy is significant.
Table 4: Proportions of GEPF and PIC in Total Financial Market Assets

<table>
<thead>
<tr>
<th></th>
<th>GEPF Total Assets</th>
<th>PIC Total Assets</th>
<th>All Funds Total Assets</th>
<th>% GEPF</th>
<th>% PIC</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>293 256</td>
<td>299 923</td>
<td>867 396</td>
<td>34%</td>
<td>35%</td>
</tr>
<tr>
<td>2003</td>
<td>307 637</td>
<td>358 711</td>
<td>909 099</td>
<td>34%</td>
<td>39%</td>
</tr>
<tr>
<td>2004</td>
<td>377 340</td>
<td>438 525</td>
<td>1 091 807</td>
<td>35%</td>
<td>40%</td>
</tr>
<tr>
<td>2005</td>
<td>462 596</td>
<td>545 701</td>
<td>1 283 921</td>
<td>36%</td>
<td>43%</td>
</tr>
<tr>
<td>2006</td>
<td>545 600</td>
<td>677 638</td>
<td>1 620 923</td>
<td>34%</td>
<td>42%</td>
</tr>
<tr>
<td>2007</td>
<td>673 408</td>
<td>773 540</td>
<td>1 938 569</td>
<td>35%</td>
<td>40%</td>
</tr>
<tr>
<td>2008</td>
<td>725 046</td>
<td>754 776</td>
<td>1 973 318</td>
<td>37%</td>
<td>38%</td>
</tr>
<tr>
<td>2009</td>
<td>738 281</td>
<td>875 388</td>
<td>1 874 062</td>
<td>39%</td>
<td>47%</td>
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<tr>
<td>2010</td>
<td>817 593</td>
<td>1 025 703</td>
<td>2 198 384</td>
<td>37%</td>
<td>47%</td>
</tr>
<tr>
<td>2011</td>
<td>942 832</td>
<td>1 115 052</td>
<td>2 429 843</td>
<td>39%</td>
<td>46%</td>
</tr>
<tr>
<td>2012</td>
<td>1 057 325</td>
<td>1 358 916</td>
<td>2 749 145</td>
<td>38%</td>
<td>49%</td>
</tr>
</tbody>
</table>

Source: (Authors Own Compilation, Data from South African Reserve Bank, Financial Services Board, 2002-2012)

6. Conclusion

A significant portion of pension assets are used for social protection and distribution to alleviate poverty in the first pillar, these are state funded. High levels of unemployment rates, job insecurity and income levels translate to small number of workers participating in the formal pension systems. Historical inequalities led to a large dependence on state support for social protection in old age. A mandatory second pillar doesn’t exist, and herein lies opportunity for further development of the South African pension system. The closest is state employee contributions whose pension assets are managed by the state owned PIC, significant on financial markets contributing almost half of all assets. The concentration of total assets is mainly in privately self-administered, underwritten and state employee funds in the third pillar.

It appears that the size of the banking sector has shrunk relative to total financial assets, in contrast non-banking assets have flourished with rising levels of institutional investors. They have the potential to impact savings rates, capital market development but empirical analysis must
be undertaken to assess these linkages. Further empirical work must be undertaken to measure the extent and intensity of pension systems in improving capital market development, growth and savings rate.

The study also shows significant changes occurred during the different phases of growth in the sector. From an early stage the development of regulatory framework to manage the non banking financial sector played a significant role in the financial development of the sector. There remains huge potential for growth of the South African pension fund sector but there is limited research on the performance of the sector and its impact on growth. Government regulation and interventions have ensured that pension funds are well managed and bad practices discouraged in the pension sector through institutions such as the Pension Fund Registrar who plays an oversight role in the sector.

Pension funds are a crucial source of capital that can be used to drive national priorities, however policy recommendations on the regulatory framework and management of institutions will need to be reviewed.
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