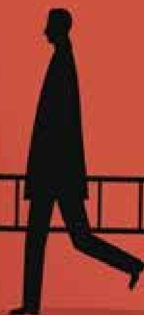
MAR 2023

# irfa talk

THE RETIREMENT INDUSTRY MAGAZINE

# Tighter reporting to protect members' interests



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- FOREWORD -

# FROM THE IRFA PRESIDENT

In this, our first issue of 2023, I would like to welcome all and wish you a successful 2023. May your days be pleasant and your nights be long.

In reflecting on the various regulatory and socio-economic fluctuations over the past few years I am reminded of the phrase "a whirlwind of change". Rest assured that for 2023 it remains our continued commitment to all stakeholders that IRFA will continue working determinedly to lobby, source information and provide you with the tools for seamless execution of these changes for the betterment our industry and all.

With the considerable change in retirement reform that has taken place in the last years it is imperative that the operational tools required for this evolution are aligned to optimally execute these important changes. This sentiment is reflected in the theme of the 2023 IRFA conference which is 'Making it Happen'. Discussions and speakers for this event will provide the sector with valuable information and insight to empower trustees and the industry to navigate the altered landscape.

The conference will be held at the Cape Town International Convention Centre on 18 and 19 September and I invite you all to participate. The future of retirement is in the hands of innovators. Join us and help us equip ourselves and our industry to align practices to regulatory reform and a changed world.

February 2023 sees the IRFA board having its annual planning session. 'Making it Happen' will form part of the board's preparation for 2023. In doing so, we are cognisant of the micro- and macro-environmental indicators. Our planned outcomes will continue to be underpinned by our key strategies of, stakeholder management, giving back, impact through inclusion, membership growth and being the number one representative body in the industry.

In reflecting on the past 12 months, milestones in 2022 saw a well attended industry conference in Durban in September; an extremely successful and well-received revamp of our awards programme, now rebranded as the Lwela Ukwenza Kahle awards.

The awards programme is robust, rigorous and a true reflection of excellence. The webinar series we introduced during the Covid-19 period to ensure ongoing engagement and information sharing with our stakeholders has been so well received that it now forms an essential part of our service offering. These webinars provide valuable insight and are open to the sector at large.

I look forward to partnering with you as we make it happen, together, for the members of our funds and broader society at large. IRFA

*– Our planned outcomes will continue to be underpinned by our key strategies. –*

Geraldine

**Geraldine Fowler**
President

# Turn and face the change

**14** The 2023 IRFA conference, to be held in Cape Town later this year, will be strongly focused on not only examining legislative and regulatory changes in the retirement sector, but also on furthering the conversation on what needs to be done to facilitate these changes.

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Philippa Owen, ESG Lead: GraySwan

**COP27 AND INVESTMENT IN AFRICA**
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*IRFA Talk* is published on behalf of the Institute of Retirement Funds Africa by Mikateko Media.
10 Freedom Way, Milnerton, Cape Town 7441
Postal address: PO Box 872, Green Point, 8051
Tel: +27(21) 550 2400
www.mikatekomedia.co.za

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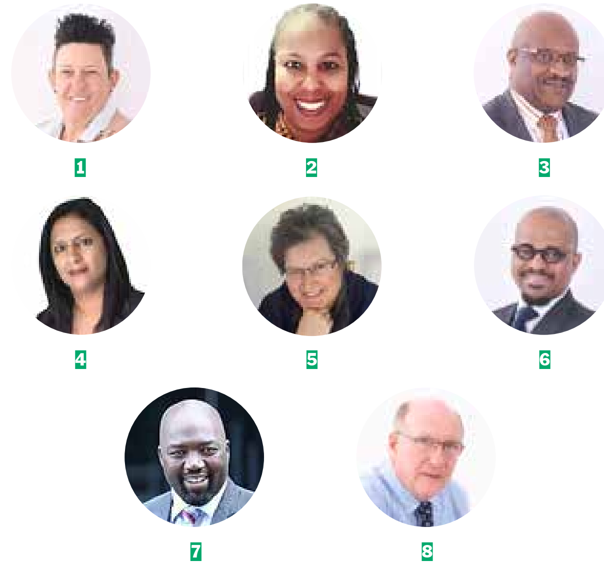


**1.** Geraldine Fowler (IRFA President) | **2.** Amanda Khoza (Vice President)
**3.** Prof. Enos Ngutshane | **4.** Nancy Andrews | **5.** Cheryl Ward | **6.** Mandla Nkosi
**7.** Mkuseli Mbomvu | **8.** Prof. Voet du Plessis



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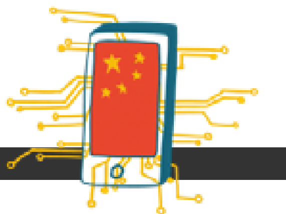
# GLOBAL HEADLINES

Business news developments from around the world.

## US economic growth stronger than expected

**NEW YORK** – The US economy did better than expected at the end of last year, despite higher borrowing costs and the rising cost of living dragging on growth. Official figures show that the economy grew at an annual rate of 2.9% in the last three months of 2022. Some analysts are worried that the US economy is headed for recession, although the jobs market has held up. In December [2022], traditionally a big month for consumer spending, retail sales dropped 1.1% from a month earlier. Manufacturing has also suffered, while the stock market dropped sharply last year. But consumer spending, the main driver of the US economy, continued at a solid, albeit slowing, pace. Last year, the Federal Reserve hiked interest rates from near zero to more than 4%, the highest rate in 15 years. By lifting borrowing costs, the bank is encouraging consumers to save more and spend less, hoping this will ease the pressures pushing up prices.

## China still wants to control Big Tech



**HONG KONG** – Investors have raced back into Chinese tech stocks this year, encouraged by an apparent truce in a two-year battle between some of the country's most powerful regulators and its biggest internet companies. But the enthusiasm may prove to be premature. Beijing is tightening its grip on household names such as Alibaba (BABA) by acquiring so-called 'golden shares', which allow government officials to be directly involved in their businesses, including having a say in the content they provide to hundreds of millions of people. In early January, a fund controlled by the Cyberspace Administration of China (CAC) took a 1% stake in Alibaba's digital media subsidiary in Guangzhou, according to business data platform Qichacha. The subsidiary – Guangzhou Lujiao Information Technology – has a portfolio of businesses under its wing, including mobile browser UCWeb and streaming video site Youku Tudou.

# Microsoft confirms it will invest billions in the creator of ChatGPT

**US** – In January, Microsoft confirmed it is making a multibillion dollar investment in OpenAI, the company behind the viral new artificial intelligence (AI) chatbot tool called ChatGPT. Microsoft, an early investor in OpenAI, said it plans to expand its existing partnership with the company as part of a greater effort to add more AI to its suite of products. OpenAI will be used to develop AI that is increasingly safe, useful, and powerful.

"We formed our partnership with OpenAI around a shared ambition to responsibly advance cutting-edge AI research and democratise AI as a new technology platform," stated Satya Nadella, Microsoft's CEO. The deepening partnership between the two companies has the potential to supercharge OpenAI's ambitious projects, including ChatGPT, which has captured the attention of academics, business leaders and tech enthusiasts with its ability to create lengthy and thorough responses to user prompts and questions. The investment could also catapult Microsoft as an AI leader and ultimately pave the way for the company to incorporate ChatGPT into some of its hallmark applications, such as Word, PowerPoint and Outlook.

## UK inflation likely to fall rapidly this year

**ENGLAND** – Inflation is likely to fall rapidly this year as energy price decrease, according to Bank of England governor, Andrew Bailey. The Bank was not trying to change market expectations that interest rates will peak at 4.5%, he added. The pandemic and the cost-of-living crisis meant a UK recession was still on the cards. A major component of inflation has been soaring energy costs as economies recover from the pandemic and Russia's war in Ukraine pushes up oil and gas prices. But wholesale energy costs have been falling in recent weeks, and energy bills are more than previously forecast. This has made the bank more optimistic that inflation could be on an "easier path", Bailey said. He went on to state that lots of vacancies for jobs mean employees are in a stronger bargaining position for wage rises, which could help push prices up.

# BUSINESS UPDATE

**5.30%**

Oil loadings from Russia's Baltic ports are set to rise by 50% from December 2022, as sellers try to meet strong demand in Asia and benefit from rising global energy prices.

**10 000**

US aircraft manufacturer Boeing is set to hire 10 000 workers as it recovers from the pandemic and increases jetliner production but will trim some support jobs.

**100 years**

US Treasury Secretary Janet Yellen lauded the Ford Motor Co's 100-year history of assembling vehicles in South Africa and underscored Washington's resolve to expand trade ties with countries that it "can count on", which includes South Africa.

**$346 million**

Crypto giant Binance processed almost $346 million in Bitcoin for the Bitzlato digital currency exchange; its founder was arrested by US authorities for allegedly running a money laundering engine.

# CAPITAL GAINS CANNOT FLOW THROUGH MULTIPLE DISCRETIONARY TRUSTS

*A recent Supreme Court of Appeal judgement has clarified that a capital gain distributed from one trust to a second and then to a natural person beneficiary must be taxed in the hands of the second trust, and not the natural person.*

The question whether a capital gain can flow through multiple discretionary trusts has finally been settled by the Supreme Court of Appeal (SCA). This is important because, in practice, the following situation could arise.

Discretionary Trust 1 sells an asset, realises a capital gain of R100 and vests it in discretionary Trust 2 in the same tax year. Trust 2 vests the R100 in John, one of its beneficiaries, in the same tax year. John is on the maximum marginal rate of 45%. If the gain could flow to John, he would pay tax of R18 (R100 × 40% inclusion rate × 45% marginal tax rate) (ignoring the annual exclusion of R40 000). But if the gain could travel only as far as Trust 2, it would be taxed at an effective rate of 36% (R100 x (80% inclusion rate × 45% flat rate)) and the tax would be R36.

In C: SARS v The Thistle Trust, 10 vesting trusts (collectively the Zenprop Group) operated business as property owners and developers. In the 2014 to 2016 years of assessment, these primary tier trusts disposed of capital assets, giving rise to capital gains which vested in The Thistle Trust in the same year of assessment. The Thistle Trust in turn vested the capital gains in its natural person beneficiaries in the same year of assessment, and they declared the capital gains.

SARS raised additional assessments for the years in question on The Thistle Trust as well as an understatement penalty of 50% plus Section 89quat interest. In the Tax Court (ITC 1941 (2021) 83 SATC 387 (G)), Wright J found in favour of the taxpayer, ruling that the capital gains were correctly taxed in the hands of the natural person beneficiaries of The Thistle Trust under s 25B, para 80(2) of the Eighth Schedule of the Income Tax Act and the conduit principle.

On appeal by SARS to the SCA, the SCA held that s 25B did not apply because the Eighth Schedule had a self-contained rule for dealing with capital gains in the form of para 80(2). Para 80(2) required the capital gains to be disregarded by the primary tier trusts and to be taken into account by The Thistle Trust. What was vested in the natural person beneficiaries of The Thistle Trust was simply a sum of money that did not give rise to a capital gain capable of attribution. The conduit-pipe principle formulated in the Armstrong and Rosen cases did not apply.

*— The lesson from this is that multiple discretionary trust structures are inefficient for capital gains tax purposes. —*

The lesson from this case is that multiple discretionary trust structures are inefficient for capital gains tax (CGT) purposes because they prevent gains from being taxed in the hands of natural person beneficiaries at the lower of 0% to 18% CGT effective rate. Instead, the capital gains are taxed in the secondary tier trust at 36%.

By implication, the case also puts paid to the argument that capital gains can be distributed to non-resident beneficiaries by resident trusts through the conduit principle.

It would be interesting to know whether the assessments of the natural person beneficiaries will be reduced or whether they have been prescribed.

The taxpayer at least enjoyed success in one area. The court found it was not liable for the understatement penalty of 50% because it had relied on a legal opinion. But the trust still had to pay the interest due on the underpayment of provisional tax. IRFA

**Duncan McAllister**
Consultant: Webber Wentzel

IMAGES: SUPPLIED





# ESG-FOCUSED PROCUREMENT WHERE IT'S NEEDED THE MOST

*Environmental, social and governance (ESG) compliance offers the hospitality and leisure sector in South Africa much-needed low-cost credentials as an additional competitive advantage, in a tight market, provided they leverage their supply chain.*

The hospitality and leisure sector in South Africa was arguably one of the worst-affected industries during the Covid-19 pandemic. The industry was cut-off from its customers, who could not travel and enjoy the experiences offered by operators in South Africa. As a result, it has become increasingly crucial for hospitality and leisure sector operators to find low-cost wins. The same undoubtedly applies to suppliers in the sector. ESG compliance can offer necessary low-cost credentials as an additional competitive advantage, especially in a tight market. ESG is far more than just a philanthropic buzzword, with industries ranging from the mining sector to financial services realising its value in unique ways and adopting ESG principles as core to their operations.

ESG factors encourage businesses to consider their impact on the environment and on their stakeholders, and to implement policies that benefit not only their organisation, but also broader society.

All South African businesses must comply with certain minimum ESG standards, such as health and safety, employment conditions, and corporate governance statutory and regulatory requirements. As compliance with the broader ideals of ESG is not mandatory in all cases, hospitality and leisure operators may ask, "How does ESG help my business and why should I consider it?"

Aside from the obvious benefits to society and the environment, ESG makes businesses more attractive to customers and investors who take these factors into account in their decision-making. ESG makes businesses more robust and resilient in the face of external shocks, and it reduces risks businesses face in the open market.

In the hospitality and leisure sector, consumers are more aware than ever of where their food comes from and whether the products they use are sustainably made. They also want to know if the suppliers to a hospitality business pay their workers a fair wage and recognise their labour rights.

However, not all businesses can comply with the broader ideals of ESG, whether for financial or operational reasons. Nonetheless, they can access the advantages of compliance by leveraging the ESG credentials of suppliers of goods and services.

An example of how this works within the hospitality and leisure industry is the purchase of serviettes and take-away cutlery by restaurants and hoteliers. If procured from an ESG-compliant supplier who manufactures wooden cutlery and serviettes made from recycled paper, the hotel or restaurant can enhance its ESG credentials. A bed-and-breakfast chain can purchase its linen from an ESG-compliant supplier who sources cotton from a sustainable agribusiness. These are just a few examples of how an ESG-focused supply chain can assist hospitality and leisure operators to bolster their own ESG credibility. The opportunities are wide-ranging yet easily accessed if some thought is applied to the supply chain process.

## SUPPLY CHAINS AS A KEY COMPONENT OF ESG

Codes and standards applicable to ESG in South Africa recognise that a company's supply chain directly influences a company's behaviour towards the environment and broader society.

An example is the JSE Sustainability Disclosure Guidance (SDCG), released in June 2022. The SDCG pays attention to who a business buys from when benchmarking that operation's ESG performance. If a business purchases goods or services from an ESG-compliant supplier, the buyer's own ESG standing is enhanced. Using its supply chain to support ESG-compliant businesses, a hospitality and leisure business can play a credible role in advancing ESG in ways that benefit stakeholders and the environment, all while strengthening its own market position through its enhanced ESG status.

Beyond the legal ramifications of ESG compliance, hospitality and leisure operators can use supply chain relationships to reach ESG-conscious customers credibly.

Even if a business cannot comply fully with the broader ideals of ESG, by recognising the value they can add to the ESG ecosystem at large and adapting their supply chain accordingly, they can meaningfully participate in, and contribute to, rising ESG awareness. IRFA

**Candice Meyer,** Partner, **Lize-Mari Doubell,** Candidate Attorney **Naledi Mbaba,** Candidate Attorney: Webber Wentzel

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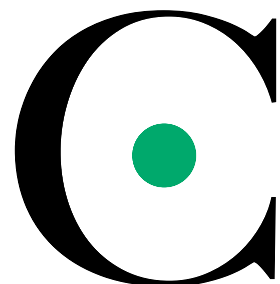


# Conduct Standard 1 of 2022: What does it mean for the local retirement sector?

*From 20 February 2023, Conduct Standard 1 of 2022 replaces Regulation 33 of the Pension Funds Act and sets out in more detail the requirements and responsibilities of both employers and funds when it comes to Section 13A. Nancy summarises these for the benefit of our readers and the broader sector. The IRFA conducted an in-depth review interview with Nancy Andrews, Chair of the Institutes of Retirement Fund Africa's Legal and Technical Committee. Andrews summarises the implications for our readers and the broader sector.*

Beginning with recordkeeping, says Andrews, it is important to remember that certain data will be mandatory from 20 February 2023. All initial contribution schedules will need to contain the following information:

- Name of the fund
- Fund registration number
- Period in respect of which the contribution is payable
- Name and address of the employer
- Where an employer has multiple pay-points, the pay-point which has made the deduction
- The contact person responsible at the employer or pay-point dealing with enquiries relating to contribution payments and statements
- The identity of the person envisaged in section 13A (8) of the Act as requested from the employer by the fund in terms of Section 13A (9) of the Pension Funds Act
- In respect of each member:
  - Full name
  - Date of membership
  - Fund membership number
  - Date of birth
  - South African identity number or passport number
  - Employers pay number
  - Income tax number
  - Contact number, including (where available) cell phone number
  - Email address (where available)
  - Postal address
  - Residential address
  - Annual pensionable emolument
  - Percentage and amount of contribution
  - Split between member and employer contributions
  - Details of any additional voluntary contributions paid.

According to Andrews, subsequent contribution schedules must include any changes as compared to the contribution schedule for the previous period. The schedule must reflect any differences in the data, including new members, terminations, adjustments for changes to pensionable emoluments or voluntary contributions, corrections, or any other relevant information.

In addition, all information must be accompanied by an employer declaration that confirms that all the information reflected on this schedule is correct, accurate, complete and aligned to the minimum requirements as set out in Section 13 of the Pension Funds Act and the FSCA Conduct Standard.

## NON-PAYMENT OF CONTRIBUTIONS

On the issue of non-payment of contributions, Andrews emphasises that the consequences of such non-payment are serious for members of the fund.

The employer's breach of the provisions of the Act in this instance causes substantial prejudice to the fund and its members, because it means that the fund is not able to invest the outstanding contributions in line with the fund's investment strategy which benefits the members of the fund. Consequently, it erodes the members' share (retirement benefits) to which they will be entitled upon retirement or termination of employment or membership.

Furthermore, Andrews explains that non-payment by the employer prevents the fund from paying risk premiums for members' insured benefits which are payable to the insurers in terms of the rules of the fund. This is because the money for risk premiums is deducted from contributions paid by the employer in respect of the members and paid to the insurers who underwrite risk benefits payable by the fund. Andrews is adamant that the fund cannot deduct this money from other sources. "Thus, if a member of the fund employed by the employer were to become disabled, sick or die while in service, there is a risk that the fund's insurers would repudiate the claim if, as a result of non-payment of contributions, that members' premiums are not up to date."

Andrews notes that there are options available in terms of fund rules, for example to reduce or suspend contributions, and she urges the sector to obtain further information on how to exercise either of these options should this be required.

She cautions that, should an employer's non-compliance persist for 60 days or more, the employer's participation in the fund could be terminated depending on the fund's rules .

## WHAT ARE THE CONSEQUENCES IF AN EMPLOYER DOES NOT COMPLY?

Andrews stresses that retirement fund trustees are obliged to report employers who do not comply with Section 13A to the Financial Sector Conduct Authority (FSCA), the South African Police Services (SAPS) and members. Compliance includes both the payment of contributions and the submission of the required minimum information by the due dates.

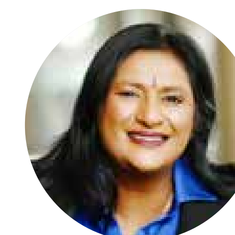
Non-compliance with the requirements of section 13A and the Conduct Standard is a criminal offence, warns Andrews, and there are serious consequences which include:

- The application of late payment interest on all outstanding premiums at prime rate plus 2%
- An obligation on the fund to notify members in writing when their employer fails to pay contributions
- Lodging of a criminal complaint by the Principal Officer with the SAPS against the person(s) personally responsible at the participating employer for compliance. Any person who fails to comply is guilty of an offense and may be liable, on conviction, to a fine not exceeding R10 million or imprisonment not exceeding 10 years, or both.
- The Principal Officer notifying the FSCA of non-compliant employers.

## WHAT HAPPENS IN THE CASE OF LATE PAYMENT?

Should contributions be late, Andrews strongly advises that the fund charge the employer late payment interest as prescribed by the Act. According to the Conduct Standard, compound interest must be applied on late or unpaid payments. She concludes that this compound interest must be calculated from the first day following the expiration of the period in respect of which such amounts were payable until the date of receipt by the Fund and are prescribed to be the prime rate plus 2%.

For further information, contact Wayne Hiller van Rensburg on wayne@irfa.org.za. IRFA



**Nancy Andrews**
Chair of the Institutes of Retirement Fund Africa's Legal and Technical Committee

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P.

# PM Mudau vs Municipal Employees Pension Fund

*The IRFA has been admitted as an amicus curiae in a Constitutional Court case to be heard from 7 March 2023. Before we get into the reasons why we chose to join the case, we want to explain our role as an amicus curiae and why we were recognised as such and allowed to be part of the case and provide support.*

An *amicus curiae* (literally, 'friend of the court') is a person or organisation that is not a party to a legal case but offers information or expertise to assist the court in making a decision. In the context of a South African Constitutional Court case, being an *amicus curiae* can be important for several reasons:

• Expertise: *Amici curiae* can provide the court with expertise and information on issues that may not be fully understood by the parties to the case or the court itself. This can be particularly important in cases involving complex legal, technical, or scientific issues.
• Balance: *Amici curiae* can help ensure all perspectives on an issue are presented before the court. This is especially important in cases that may have a significant impact on the rights and interests of different groups of people.
• Public Interest: *Amici curiae* can represent the broader public interest in a case. They can provide the court with information on how the case may affect the public or society as a whole, and advocate for a decision that is in the best interests of the public.
• Legitimacy: *Amici curiae* can lend legitimacy to a court decision by showing that the decision was based on a thorough consideration of all relevant information and perspectives.

Overall, being an *amicus curiae* can be important for ensuring that the court has all the information it needs to make a fair and just decision respects the rights and interests of all parties involved and especially where the judgment of the court would impact a broader spectrum than just the parties before court.

## WHY IS THE MUDAU CASE SO IMPORTANT?

In accordance with the terms of his employment, Mr Mudau had worked for the Vhembe District Municipality and belonged to the Municipal Workers Pension Fund (MEPF). But Mr Mudau was given a promotion to a new position in May 2013 and, as a result, no longer qualified as a member of the MEPF and became entitled to a withdrawal benefit. The rules allowed for an "early withdrawal benefit", which was equal to three times the total amount of payments that had been made to the MEPF for or on his behalf.

However, the MEPF board decided that it would amend the 'early withdrawal benefit' rule retrospectively, with effect from 1 April 2013, to allow only for the payment of an amount equal to one and a half times the aggregate value of the member's accumulated contributions in order to ensure that the fund would remain financially sound over the long term. Section 12(1) of the Pension Funds Act (the PFA), states that rule amendments only become effective only once they are registered by the authority and for good reason, so that accrued rights are not affected.

The MEPF did not use the calculation in the registered rules that were in effect at the time Mr Mudau claimed his benefit. Instead, it treated the proposed rule amendment as having been accepted and registered in accordance with section 12(4) of the PFA for calculating his benefit. The Supreme Court of Appeal (SCA) agreed that the MEPF was right to do this. Before the matter was referred to the SCA, both the Adjudicator and High Court had dismissed the claim by the MEPF on the trite principle that retrospective amendments could not affect accrued rights.

However, many commentators have explained why the SCA may have made an error in law when it made this decision. The SCA may have made a mistake by approaching the problem from the perspective of whether the issue was a question that a fund could change its rules to lessen benefits for its members (it would in itself have been a strange approach and this issue has already been determined by the SCA in the matter of National Tertiary Retirement Fund v Registrar Pension Funds [2009] 2 BPLR 97 (SCA)). In this case, the benefit had already accrued to the member. The issue was whether the proposed rule amendment could be implemented retroactively before it had been registered by the FSCA. The amendment was created to make sure that the benefits of every member who leaves the fund are decreased in order to help the fund pay its future obligations.

The SCA held that "the amended rule retrospectively applied to all pension withdrawal benefits which had accrued to the Fund's members after 1 April 2013". This was done without providing reasons in law why this new approach has been followed. The effect was that the reduced benefit provided for in the amended rule would now apply to Mr Mudau's withdrawal benefit. Notwithstanding the fact that Mr Mudau left his position on 31 May 2013, the MEPF had submitted the rule amendment on 22 July 2013 and his withdrawal benefit was calculated and paid on 16 October 2013, and the amendment was only registered on 1 April 2014. In other words, his benefits were reduced before the FSCA had registered the new rule and furthermore, disregarded the fact that the amendment had not yet taken effect. The SCA did not address whether benefits that become due before the fund applies for a rule amendment should be retroactively reduced.

The IRFA wants to ensure there is clarity for all pension sector stakeholders in South Africa. In this case there was a move away from the accepted understanding of when a rule amendment becomes effective and what benefits members can expect to receive should there be such a rule amendment. We believe our role as an *amicus curiae* can assist the court in deciding on this important issue that affects all retirement fund members. IRFA

**Wayne Hiller van Rensburg**
Executive Officer: IRFA

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I.

# Investors must carry the energy transition torch, regardless of Eskom's fate

*Andre de Ruyter's resignation from Eskom and the news that he would vacate his position as CEO in March 2023 created extensive national anxiety over South Africa's energy supply as well as the future of the recently announced energy reform programme and the Just Energy Transition (JET) funding deal set out at COP27. This has been further compounded by his early exit from Eskom last week, before completing his notice period, which followed his candid comments on the extent of corruption within the state-owned entity in a recent interview with etv.*

Well-respected in the local and international market as someone willing to take on a difficult job and do what needed to be done despite political opposition, it was widely accepted that the JET deal and confidence in the Transition Plan was very closely tied to De Ruyter's role as the lead implementer.

It is therefore to be expected that our collective confidence is shaken by his departure from Eskom and overall leadership changes at the SOE. However, what has not changed is the overall objective set out by De Ruyter and his team over the past three years to get to net zero by 2050. SA reiterated this at COP27 through its JET-IP and again just after COP27 as a member of the G20, when the group restated their commitment to a Paris-aligned future. Therefore, the long-term target is unchanged, and the strategy proposed to achieve this has been submitted to our international funding partners. These are not easily amended, even if the person leading the charge to get to the finish line is no longer part of the race.

Finding a replacement to match De Ruyter's experience, expertise and gravitas will be a challenge. But regardless of who his permanent replacement might be, we should not expect significant changes to the strategy, as this has largely been solidified. There may, however, be some changes in implementation of the strategy – specifically with respect to efficacy, which is truly something that we cannot afford at this stage of our energy crisis.

So, let's look at the scenarios that might play out in 2023

1) We blow off this whole net zero by 2050 thing, abandon the transition entirely and reject renewables. In this event, we make ourselves a pariah in the global marketplace and the country falls apart, until we are forced to see reason and get on board again, late to the party. We would therefore have missed out on the majority of the potential socioeconomic benefits and been blamed by the international community for the inevitable negative environmental consequences of our actions. In the end, the transition still happens.

2) We remain committed to net zero by 2050, but fumble along on our transition plan implementation and don't make strides to achieve this goal, leaving us open to intervention by external parties who impose measures to get us to renewable energy dependence by 'force' – think draconian financing conditions, as an example. In the end, the transition still happens.

3) We remain committed to net zero by 2050, but fumble along until its almost D-day and then have no choice but to implement incredibly disruptive interventions (in renewable energy industry development) ourselves, which have disastrous social consequences. In the end, the transition still happens.

4) We remain committed to net zero by 2050 and build a massive renewables industry but deviate from the JET Partnership principles and therefore achieve environmental targets at the expense of social objectives thereby generating local unrest. In the end, the transition still happens.

5) We stay on course with our JET-IP and manage to achieve a just transition to low carbon, inclusive, sustainable economies. Year-on-year, our progress acts as an example for other emerging markets and fossil-fuel dependent markets on how to finance and implement a sustainable transition and we are held up internationally as a beacon of light in the darkness of the climate emergency and its associated geopolitical and socioeconomic tensions. This would be my personal preference.

Ultimately, any way you slice it, the transition still happens. It is inevitable. The nature of the transition though – how disruptive it is, how we handle the circumstances of those disproportionately impacted – is up to the decisions we make now and along the way. And very little of that has anything to do with whoever the Eskom CEO is.

What will be more consequential for how the transition plays out, is how investors across the market respond to the pressure to transition their current investments, regardless of renewable energy industry investment opportunities.

Institutional investors are critical to the success of the transition. It remains up to us, as allocators of capital, to keep things on track in the chaos of the current environment. We need to be the voice that rises above the noise and unites various stakeholder groups toward a common aim: a transition that is just. As investors we have a responsibility to our clients to deliver maximum risk-adjusted returns in a sustainable way. This necessitates keeping our eyes firmly on the end goal, and that we don't let ourselves get distracted by political drama along the way.

An Eskom without De Ruyter may see a delay in some of the projects coming online that we would have hoped to invest in. But that shouldn't stop us from making progress outside of those projects. Instead, we should use this as an opportunity to look at our existing portfolios. As investors, we should be asking ourselves what we can do, what leverage we can activate, to transition those investments already on our books. The new, shiny, renewables projects will come online soon enough, and when they do, we will run with those; but in the interim, there is a tremendous amount of work that needs doing within our existing investments. We need to be reviewing what we've got to work with and assessing which investments are at greatest risk and which present the greatest opportunity, given the inevitability of the transition.

This is where the role of stewardship becomes critical. Stewardship, or active ownership, is core to the transition. This process is especially relevant now that there may be a delay in accessing some of the expected greenfield projects. There will never be a better time for institutional investors to roll their sleeves up and start acting on their responsibility to be an active owner of their assets.

The shift that is currently in play impacts every company in every sector. No one is immune. It has become an imperative for investors to step up as stewards of these assets and to shepherd companies through the transition into the new order. And if the companies we invest in won't or can't adapt, then it is our role to guide them toward sustainable closure and responsible exit (and, where appropriate, remediation).

We need collaborative, deliberate, solutions-focused engagement with companies that drives the attainment of real-world impact. We need this, regardless of how the future unfolds for Eskom's leadership and regardless of what delays we may see in the growth of the renewables industry. Without proactive stewardship now, we will have forced, disruptive change later. Because, just as the sun continues to rise, no matter how the Eskom story unfolds, in the end, the transition is happening despite all the odds. IRFA

**Nicole Martens**
Head of Stewardship: Old Mutual Investment Group

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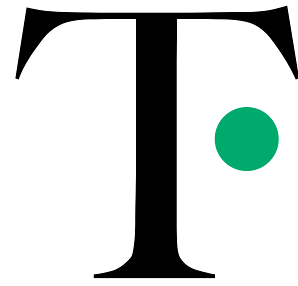

# Turn and face the change

IRFA Talk *interviews Executive Officer Wayne Hiller van Rensburg.*

The 2023 IRFA conference, to be held in Cape Town later this year, will focus strongly on not only examining legislative and regulatory changes in the retirement sector, but also on furthering the conversation on what needs to be done to facilitate these changes. *IRFA Talk* spoke to Executive Director Wayne Hiller van Rensburg about making it happen.

According to Hiller van Rensburg, the conference will be aimed at providing the necessary information and tools for retirement funds to navigate the changes and innovations in the sector. It will also focus on defining the precise nature of the 'it' as it refers to the required sectoral transformation, in other words, unpacking what all is encompassed in these changes.

He says, "The past few years have seen significant regulatory and policy changes and innovations in the pension sector. Furthermore, the retirement sector is being called upon to contribute substantially to socio-economic upliftment and development in the country and on the continent. During this time, many trustees have been faced with the task of communicating important changes to member benefits, and developing and implementing the necessary processes, procedures and agreements to accommodate these innovations and changes."

## IRFA'S EXECUTIVE OFFICER ENUMERATES SOME OF THESE MAJOR SHIFTS IN THE LOCAL RETIREMENT SPACE:

"The first and major change trustees have to work with are amendments to Regulation 28 of the Pension Funds Act," advised Hiller van Rensburg. The revised Regulation 28 was issued on 5 July 2022 and came into effect from 3 January 2023. Major changes can be summarised as follows:

- Introduction of the definition of infrastructure investments with an overall 45% investment limit and a limit of 25% per investment (for all types of investments and not only infrastructure investments, with a few exceptions).
- Ban on investment in crypto assets.
- Removal of the reporting exemptions for pooled investments (collective investment schemes and insurance policies) which require funds, administrators, and investment managers to provide more information on the underlying investments.
- Reduction in housing loan limit to 65%.
- Hedge funds and private equity fund investment limits delinked. Private equity fund limit set at 15% and the hedge funds limit set at 10%. Investments in hedge funds registered in terms of the Collective Investment Schemes Act will be permitted.
- Offshore investments allowed up to 45% of asset value.

Hiller van Rensburg also draws attention to the Conduct Standard 1 of 2022 (RF): Requirements related to the payment of pension fund contributions.

The standard covers reporting and notification requirements, information that is to be provided by an employer to the fund. The interest rate applicable to arrear contributions and requirements for a fund to follows if it appoints attorneys to collect outstanding contributions. This regulation will come into effect on 20 February 2023.

## WHAT IS IN THE PIPELINE FOR LOCAL RETIREMENT FUNDS?

**FSCA Discussion Paper: A framework for unclaimed financial assets in South Africa**

A wide range of financial products and assets, including retirement fund benefits, bank deposits (including foreign currency deposits), participatory interests in collective investment schemes, life and non-life insurance policies, securities, and any investment, return, income, dividend, or other proceeds derived from the financial products, are anticipated to be included in the scope of the proposed unclaimed assets framework.

The Financial Sector Conduct Authority (FSCA) published a discussion paper entitled: Framework for unclaimed financial assets in South Africa. The purpose of the paper is to promote discussion about how unclaimed assets and lost accounts should be handled in a way that adheres to the Treating Customers Fairly (TCF) principles.

**IRFA Executive Officer Wayne Hiller van Rensburg** urges the sector to turn and face the change at the industry body's September 2023 conference in Cape Town.

IMAGES: SUPPLIED

Hiller van Rensburg says, "The proposals have far-reaching effects for retirements funds as it means that the existing unclaimed benefit funds would be replaced with the new Central Fund. The legal structure of existing unclaimed benefit funds as preservation funds, governed in terms of the Pension Funds Act and Income Tax Act, is beneficial. Therefore, it would seem that the application of the Central Fund to retirement funds does amount to some 'reinventing of the wheel'. It is necessary that an exercise is done to determine the pros and cons of the proposals as well as a cost-benefit analysis. The results of this analysis should ultimately indicate whether or not the existing unclaimed benefit funds should remain in place in respect of unclaimed benefits from retirement funds."

**Governance of umbrella funds**
In terms of fund governance, Hiller van Rensburg says that National Treasury released a discussion document titled titled *Governance of umbrella funds* in December. "The aim of the discussion document is to initiate a consultation process with industry, labour unions and interested stakeholders on measures to improve the governance of umbrella funds, particularly commercial umbrella funds. We are still waiting to hear what the outcome of this will be. For now, the National Treasury has advised that this will be picked up after the finalisation of the two-pot system."

In terms of pending legislation he makes reference to:

- The Conduct of Financial Institutions (COFI) Bill:
  The COFI Bill 2018 was made available by National Treasury for comments, and there were various interactions about the Bill in 2021 and 2022. National Treasury is still considering the suggestions but plans to finalise the Bill and present it to Parliament for review as soon as possible. The forthcoming legislative action will have a significant influence and must be closely watched.
- Draft Revenue Laws Amendment Bill (RLAB) of 2022 (two-pot retirement system):

The draft RLAB sets out the legal provisions around the two- pot retirement system. The two main concerns giving rise to this proposed change are lack of preservation before retirement, and some households in financial distress have assets within their retirement fund(s) that are not accessible, even in case of emergencies. There will be new definitions in the legislation, namely : 'savings pot', 'retirement pot' and 'vested pot'. The proposed implementation date has been moved to 1 March 2024.

## REGULATORY SHIFTS

**Omni-CBR for Retirement Funds**
The Omni-CBR is intended to facilitate streamlined cross-sectoral statutory reporting and sets out the types of conduct indicators to be reported on in future by various financial institutions, including:

- Banks
- Insurers and micro-insurers
- Investment providers
- Co-operative financial institutions (CFIs)
- Financial services providers (FSPs)
- Retirement funds and retirement fund benefit administrators.

The proposed date for this to come into effect is 2026.

**Draft Conduct Standard: Conditions prescribed in respect of pension fund benefit administrators**
Currently, conditions in respect of benefit administrators are prescribed by Board Notice 24 of 2002, published by Government Notice No. 10505 in Government Gazette 23153 of 1 March 2002 (BN 24 of 2002).

Explaining this, Hiller van Rensburg notes, "In terms of section 13B(1) of the PFA, the FSCA may prescribe conditions for benefit administrators who, on behalf of a pension funds, administer the receipt of contributions or the disposition of benefits provided for in the rules of a fund (Administrators)."

On 29 July 2021, the FSCA issued the Draft Conduct Standard: Conditions Prescribed in respect of pension fund benefit administrators for comment by 13 September 2021. This draft Conduct Standard will replace BN 24 of 2002.

The draft Conduct Standard will come effective into effect upon publication of the final version. However, benefit administrators approved prior to the effective date of the Conduct Standard must comply with its provisions within six months after the effective date.

The FSCA has advised that this is pending the development of the Conduct Standard until such time as the COFI Bill is finalised.

**Joint Communication 4 of 2022 | Revised Draft Joint Standard – Cybersecurity and cyber resilience for financial institutions, 2023**
The requirements for governance, cybersecurity strategy and framework, cybersecurity and cyber resilience basics, cybersecurity hygiene practices, as well as notification and regulatory reporting relevant are covered by the Revised Draft Joint Standard. Specific financial institutions covered by the Draft Joint Standard include:

- Pension funds registered under the Pension Funds Act, 1956
- An administrator approved in terms of Section 13B of the Pension Funds Act, 1956.

The IRFA annual conference aims to provide support for trustees and other role players in the retirement sector who are faced with these significant requirements around change. "Speakers and topics at the 2023 IRFA conference will be carefully selected to empower participants with these shifts," says Hiller van Rensburg.

"In this year's conference, we're going to start looking at the following:

- What is it that needs to be done to achieve the desired state?
- Are all the innovations and changes implementable?
- Who is doing it?
- Who are the role players?
- What do those role players need to do to support the boards of management that need to do all the implementation (including regulators and policymakers)?
- Are the innovations developed in such a way that they ensure acceptance?
- Consideration of the impact of the cost on of any proposed changes?
- And what still needs to be done?"

Hiller van Rensburg concludes: "How do we make sure the role players are talking to one another, supporting one another, and ultimately, doing all of this to the benefit of retirement fund members in general, and for society at large?"

He concedes this is a tall order but the conversations will commence at the ICC in Cape Town and IRFA urges the sector to participate and contribute. This is the largest gathering of its kind on the continent and an appropriate forum to define the future. IRFA





# COP27 LAYS FOUNDATIONS FOR LONG-TERM INVESTMENT OPPORTUNITIES IN AFRICA

*After several days of focused negotiations in Sharm el-Sheikh, last year's COP27 closed with a sense of comfort that the needs of emerging and developing markets have not been overlooked.*

The agreement to create and implement a loss and damage fund to rescue and rebuild physical and social infrastructure comes years after questions were first raised about the non-delivery of promised finance to facilitate the developing world's transition to a greener economy and the move away from fossil fuels.

It is seen as a crucial first step that places the onus on the countries most responsible for the effects of climate change to contribute to those countries worst affected (and the least responsible). From a local perspective, South Africa's request for additional funding, at more lenient repayment terms, was welcomed. The aim of this funding is to fast track the replacement of the country's fossil fuel infrastructure with renewable solutions and to address the crippling energy crisis.

As with other developing countries, the debt burden in South Africa has become a critical sticking point in terms of finance. It therefore follows that accelerated finance, at more attractive terms, will unlock new long-term investment opportunities in Africa.

These opportunities will not only be limited to clean energy solutions and a just transition, but also include projects that support the Global Goal on Adaptation (GGA), including sustainable agriculture and food security, ecosystems, biodiversity and clean water, while addressing poverty, inequality, and cultural heritage.

## ONE STEP FORWARD, TWO STEPS BACK?

While the creation of a loss and damage fund was agreed to at COP27, the means of delivery are yet to be established. Mechanisms for finance were not provided, and there were no significant changes to fossil fuel reduction targets. And although COP27 was due to set a collective quantified goal and action plan for climate finance to replace the failed US$100 billion annual target, which has not been met, this too failed to materialise.

Furthermore, there was much criticism of the ongoing greenwashing around net zero goals, where companies are preferring to offset carbon emissions as opposed to actually cutting them. Analysts expressed major concerns at what is deemed a misguided focus on rhetoric and measuring mechanisms rather than physical action to reduce emissions.

## A MEGATREND

There is no doubt that sustainability is a core requirement for long-term growth, at both a micro as well as macro level.

Climate change is an emerging megatrend that will increasingly impact daily life and touch on multiple sectors. From rising global demand for electricity and the accompanying demand for renewable energy to a more eco-conscious way of living, consumers seek to reduce their overall impact by the choices they make when buying products and services. Access to clean water is another growing sector, as is the development of more sustainable transport.

Despite the inherent challenges, being able to understand and navigate the changing markets will present many long-term investment opportunities. It is our view, therefore, that investor research should identify those sectors and industries that will be most affected by climate change, as where there is innovation, mitigation and adaption, there will be sustainability and significant investment opportunity in the long term.

Where sectors, industries and companies are not sustainable, or are not adopting sustainability enhancements, there remains significant risk and therefore these are investments to be avoided. IRFA

**Philippa Owen**
ESG Lead: at GraySwan

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- INVESTMENT -

# T.

# Tighter regulations and reporting requirements to protect members' interests

*Members of retirement funds have different needs, time horizons and options available to them to target their specific outcomes throughout their journey to and during retirement. Achieving a reasonable outcome in retirement for members is therefore the main objective for the establishment of a retirement fund. In a defined contribution fund, the timeous payment and investment of the contributions are critical to ensure growth of the members' assets within the fund.*

IMAGES: SUPPLIED

*— TCF is a critical component within the Conduct of Financial Institutions Act —*

As part of the fundamental duties of the board, they are required to always act in the best interests of members and, by extension, the members' beneficiaries. TCF (treating customers fairly) ensures that the customer (in this case the member) is central to all decision-making.

### TIMEOUS PAYMENT AND INVESTMENT OF CONTRIBUTIONS

TCF is already embedded in the Policyholder Protection Rules (PPR) when it comes to group risk benefits and is a critical component within the Conduct of Financial Institutions Act (COFI). A key factor to improving and ensuring that members are fairly treated is making certain the contributions committed to in terms of the rules of the fund are adhered to by the employer and paid over timeously.

### THE CONDUCT STANDARD HAS REPLACED REGULATION 33

Previously Section 13A and Regulation 33 to the Pension Funds Act (PFA) set out the requirements relating to the payment of contributions by employers to funds. Regulation 33 has now been repealed with effect from 27 January 2023, and replaced by the Conduct Standard, which came into effect from 20 February 2023.

### FSCA CONCERNS WITH THE EXISTING LAW

The Financial Sector Regulatory Authority's mandate is to protect the interests of fund members, while holding boards of funds, authorised persons and contractors accountable. With this in mind, the FSCA identified the following concerns with the existing law:

- Standardised reporting by principal officers and funds must be required.
- Undesirable practices and outcomes were noted where funds outsourced their responsibility to recover outstanding contributions from an employer to an attorney or third party.

Examples include:

- Failure to provide proper instructions to the attorneys
- Exorbitant fees being charged.
- Attorneys retaining interest on contributions recovered

Potential drafting improvements for clarity of the requirements were identified relating to:

- Payment of pension fund contributions to retirement funds
- Reporting of contraventions.

Taking the above into account, the Conduct Standard reinforces and is consistent with the objectives of the Financial Sector Regulatory Authority. The key points contained in the Conduct Standard are as follows:

- Minimum information to be contained in a contribution statement.
- A fund must notify every employer before they join the fund and annually thereafter of the employer's duties, obligations and liability under section 13A of the PFA and this Conduct Standard.
- The FSCA will determine the format for that notification.

The minimum information to be provided by an employer to a fund in an initial contribution statement (or the monthly schedule if this information has changed for a member) must include:

- Name of the fund
- Fund registration number
- Period for which the contribution is payable
- Name and address of the employer establishing or participating in a fund
- Paypoint that made the deduction, if an employer has multiple paypoints
- Contact person at the employer or paypoint dealing with enquiries relating to contribution statements and payment of contributions
- Identity of the person at the employer who is personally liable for compliance with the legislation (section 13A of the PFA and the Conduct Standard)
- For each member, their:
  - Full name
  - Date of membership
  - Date of birth
  - South African identity number or passport number.

Subsequent contribution statements provided by the employer to the fund must contain:

- Any changes to the member's personal information.
- The membership number allocated to each member by the fund.
- Any changes compared to the previous contribution statement showing any differences in the data, including new members, membership terminations, adjustments as a result of changes in pensionable salary, additional voluntary contributions and corrections due to error or any other information.

The data requirements for members in particular are similar to those required in terms of the Policyholder Protection Rules (PPR) for the group risk benefits. Hence, we see the regulators' line of sight is always directed towards the members to ensure information is shared on benefits, reporting of information and notification of any breaches.

## REPORTING

There are set reporting requirements, which are summarised on the following page:

| Withdrawal benefits | Who is responsible? | Report to | Timeline |
|---|---|---|---|
| Matters previously reported on were not resolved or any new compliance matters have arisen | The person responsible for checking that the contributions are received into the fund's bank account | Principal officer or monitoring person | 15 days after the end of the month applicable |
| Submit a written report about every relevant employer if non-compliance occurred or if previous non-compliance is still unresolved | Principal officer or monitoring person | Board | 7 days after the receipt of the above report |
| Any material contravention or failure to submit the employer schedule or contributions timeously | Board to communicate | • Each affected member, or all members where affected members cannot be identified, and<br>• The FSCA | 30 days after the board has been informed |
| Any material contravention or failure to submit the employer schedule or contributions timeously that continues for a period of 90 days | Principal officer or monitoring person | • South African Police Service, and<br>• Communicated to the affected members, or where affected members cannot be identified, all members (or all members relating to the participating employer) | 14 days after the expiry of the 90-day period of continued contravention |

## INTEREST ON LATE PAYMENTS

Compound interest on late payments or unpaid amounts must be calculated from the first day following the expiry of the period during which such amounts were payable until the date of receipt by the fund. The applicable interest rate is the prime rate plus 2%.

## OUTSOURCING OF THE RECOVERY OF ARREAR CONTRIBUTIONS

If a fund outsources the collection of outstanding contributions to attorneys, the trustees are responsible for:

- Considering any actual or potential conflict of interest in the selection and appointment of an attorney.
- Considering any approved policies of the fund relating to conflict of interest and outsourcing to avoid any conflict of interest.
- Ensuring fees payable to the attorney are reasonable and commensurate to the service provided and do not impede the delivery of fair outcomes to members and the fund.

Entering into an agreement with the attorney which provides for at least the following:

- Any amount recovered by an attorney for arrear contributions must be transferred to the fund's bank.
- Issuing an account within seven business days of receipt of such amount.

The fee structure:

- Specific instructions relating to the steps the attorney must take should the employer fail to pay the arrear contributions on demand
- Anticipated timelines in recovering all arrear contributions
- Frequency of reporting by the attorney to the fund on the status of payments made by the employer.

Employers will need to ensure the contributions continue to be paid on the seventh of the month following the due date and comply with the relevant regulatory requirements to avoid falling foul of the law. There is equal responsibility imposed on the relevant parties required to report on these transgressions, which will need to be monitored every month.

These regulations ultimately protect the members' interests and ensure contributions deducted from their salaries are paid over and invested for their future.

It is therefore imperative that both employers and trustees ensure that they are fully aware of the requirements placed on them with these changes and that these are properly implemented in practice. IRFA

**Belinda Sullivan**
Head of Corporate Consulting Strategy: Alex Forbes



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# Few competitive concerns for new Rapid Payments Programme

*The first quarter of 2023 should see the introduction of a new Rapid Payments Programme (RPP) in South Africa under the guidance and regulation of the South African Reserve Bank (SARB). The digital system, developed collaboratively between the larger local banks, will offer a cashless, simple, near-frictionlessnear frictionless and, most importantly, cheaper way to conduct real-time transactions for anyone with just a cellphone number or even an email address.*

IMAGES: SUPPLIED, ISTOCK

While these are all excellent attributes that should greatly benefit consumers and business owners – especially in the informal economy – should investors be concerned that it will create too much competition and undermine profitability of the banks?

## HOW WILL IT WORK?

By way of background, the system has been tailored for smaller-value and higher-volume payments, based on advanced technology used in a simple architecture to keep costs as low as possible. To make a payment, the user will send a message to a recipient's email address, mobile phone number or bank account with the payment amount. Upon receipt, that amount will immediately reflect in the recipient's account, to be used later for their own digital payments. It can also be converted into cash if needed.

What is different about the RPP is that the payer will bear the transaction cost, which is expected to be as low as 0.1%–0.3% of the total payment value, which is substantially cheaper than cash withdrawal charges and the 1.5%–2.0% or more charged by credit card providers. However, these credit card charges are generally borne by merchants, and banking clients are actively incentivised via loyalty programmes to use their credit cards as the preferred method of payment.

One largely unknown factor at this stage is the security risks to of these transactions and the risk to individuals' accounts on their cellphones or emails. There is certainly some capacity for fraud. One potential mitigant is for the SARB to limit payment values, at least to start with, to reduce incentives for fraudsters, at least to begin with. We understand the initial transactions will be capped at R3,000.

## BOON OR BUST FOR BANKS?

At first glance, SA banks and their investors might be worried about the new competition, given that they earn high fees and margins from the existing payments set-up, and the RPP is a lower-margin service. Additionally, it uses open architecture that will ultimately allow non-banks access to the payment infrastructure, creating even more competition. Some may assume that its lower cost will encourage droves of bank clients to switch immediately to the new system and give up their existing higher-margin bank products.

However, in our view, this would be an incorrect assumption: based on evidence from several other countries, there are strong incentives for the existing structures to remain in place. In the first instance, the existing bank reward structures typically ensure that transactions like credit card payments not only remain relevant, but grow. In the second instance, the low value/high volume nature of the RPP system has been very effective in capturing a large part of the existing cash-based activities. This increases the overall pool of electronic money in the system and more importantly, the velocity of the transactions. Key to this is the pricing of the service. The cheaper the service, the better its take-up, especially among those operating in the informal economy.

In South Africa, estimates show just over half of all point-of-sale purchases are still made using cash, while in the informal economy nearly 90% of transactions are cash-based. To persuade more people to move away from cash, the RPP must be affordable enough to outweigh the benefits of avoiding taxes, simple enough to be almost as convenient as cash, while overcoming questions around distrust of new technology. The feature of its greater security works in its favour. Based on what we know of the service so far, we believe the RPP does have a good chance of eventually attracting many users like the average taxi driver or shop owner.

## GRADUAL ADOPTION WON'T MATERIALLY IMPACT SA BANKS

However, in our view, the adoption of RPP will take time, and it is not likely to fully replace cash as a transaction medium. We don't believe it represents a material risk to the banks' profitability. This is because the RPP is designed largely for the lower-income segment of the market, where the big commercial banks have few higher-margin clients to lose. Also, banks are likely to be able to retain their middle- to higher-income debit and credit card clients who appreciate the benefits of loyalty programmes, fraud protection, and not having to carry cash. Electronic fund transfers (EFT) will remain a competitor for the RPP.

Lastly, another important point is the positive knock-on effect of bringing so many informal market participants into the formal economy over time. First is the expected boost to growth from the improved efficiency and productivity it will create for users like shop owners all while lowering security risks. Second, experience in other countries has shown that as people become comfortable with using technology to transfer funds, they adopt more sophisticated banking products. This can help banks gain greater acceptance among lower-income South Africans and small businesses, and in turn broaden their client base. Expanding the formal economy can only be positive for our banks over time. IRFA

**Stefan Swanepoel**
Equity Analyst: M&G Investments

I.

# Investing for impact on behalf of retirement funds

*In the environment, social and governance (ESG) framework, all three elements are equally important and, in many ways, interdependent. Arguably it is the social that deserves particular attention right now in southern Africa as the environment and governance could have the most negative impact on citizens, unless these issues are urgently and holistically addressed. Climate change (environmental) and the associated energy and water shortages, further exacerbated by rampant corruption (governance, or the lack thereof), have serious consequences for communities (social).*

Government and the private sector need to combine efforts to improve and transform social conditions in the country. More public-private partnerships (PPP) are needed. In his Budget Speech in February, the finance minister clearly stated that government is looking at initiatives to leverage private sector resources in public infrastructure delivery. This is to strengthen state capacity to expand infrastructure and to catalyse private finance. It is government's intention to fast track the implementation of the PPP regulatory review framework recommendations.

Within this context, institutional asset managers have the power to direct investments to where they make an impact on social conditions, especially given the changes to the limits to alternatives within Regulation 28 of the Pension Funds Act.

Funds can now allocate up to 15% of their fund exposure to unlisted infrastructure investments through infrastructure-focused private equity funds and up to 15% exposure to unlisted infrastructure debt through direct exposure or private infrastructure debt funds. Funds can allocate an additional 15% exposure to listed infrastructure assets (debt and/or equity).

Here are some brief case studies of investments leading to positive social impact as well as providing sound investment returns for investors. These investments are typically made through infrastructure and development funds, via debt or equity.

## PPPs WITHIN THE WATER SECTOR

Mergence is invested in the only two long-term water concessions governed by PPPs in South Africa, between the two local municipalities and the concessionaires responsible for the operation, repairs and management of the water and sewage infrastructure as well as the supply of water. This water is either bought from the water board or obtained through recycling of waste water to potable water.

The two concessions, in KwaZulu-Natal and Mpumalanga, have existed since 1999 and are valid for a 30-year period. We are actively involved in their management via a special purpose vehicle called South African Water Works (SAWW).

We believe it is a matter of urgency for more water concessions to be open to the private sector. The state can continue to regulate water but leverage off private sector expertise and capital to invest, operate and maintain the reticulation systems, thereby improving service delivery. The impact of the Mergence investment as stated below could be replicated country-wide by asset managers via PPPs to bring water – one of the most basic of services – to millions of South Africans.

The impact: through SAWW, potable water has been delivered to an estimated 450 000 people, including people in indigent communities. These households earn less than R4 000 per month and receive water for free. Technical water losses, outside the indigent communities, at the SAWW concessions, average 20% compared to the country average of 37%.

In one of the concessions, we produce three million litres of potable water per day from recycling. This results in the concessions drawing 30% less water from the bulk water supplier. These types of innovative, practical solutions should be at the forefront of our water strategies across the country.

## INVESTMENT INTO SOCIAL HOUSING

Live Easy is one of South Africa's largest affordable housing rental lifestyle brands with approximately 2 500 units in six building complexes in prime locations between Johannesburg and Pretoria in Gauteng, and with an additional 1 000 units under development. The focus is on the affordable housing market, aiming to close the gap between social housing and privately owned homes.

We identified Live Easy as a first-of-its-kind initiative in South Africa as it provides options and opportunities for people living in unsuitable or undesirable conditions to live in a safe, secure and well-managed housing environment.

The tenant age profile ranges predominantly between 21 and 30 years of age. Many are in their first jobs or professions, with around 30% earning less than R15 000 per month and a further 40% earning less than R20 000 per month. They need accommodation that matches their aspirations and provides easy access to their place of work.

The impact: Live Easy has already impacted the lives of thousands of tenants. There is a long waiting list for units, with upwards of 300 queries each month at some properties.

## MICRO-LENDING

Financial inclusion has become an important term in recent years, whereby the average citizen can be empowered to learn about money matters. In this regard, Mergence Lesotho is involved with Thusong Financial Services, a microfinance institution founded in 2011, offering loans and advances to salaried government employees at the lower-income level, with loans varying from M800 to M50 000. The Thusong products are housing loans, education/student loans and healthcare loans.

The impact: providing individuals with access to financing for education, housing, healthcare services and business ventures creates an opportunity to directly and indirectly affect and uplift individuals and communities.

## CONCLUSION

These are just a few examples of how institutional investors can make a social impact through carefully researched and managed investments into various sectors on behalf of their retirement fund clients. Other sectors could include bulk infrastructure, digital connectivity, education, healthcare and renewable energy.

It would be interesting to try to quantify the collective impact made by asset managers on the social factors in ESG. We are currently working on this very with external advisors to tangibly measure the collective impact of some of its portfolio companies and put forward a much-needed good news story for citizens suffering at multiple social levels. IRFA

**Kasief Isaacs**
Head: Private Markets: Mergence Investment Managers

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- FINANCE -

# Are we at the sweet spot for SA fixed income?

*The deceleration of inflation globally, combined with the growth impact of China reopening its economy, finds emerging markets in somewhat of a sweet spot. Data out of the US at the start of the year showed continued gains in the labour market, but there are indications of some wage normalisation through a slowdown in average hourly earnings.*

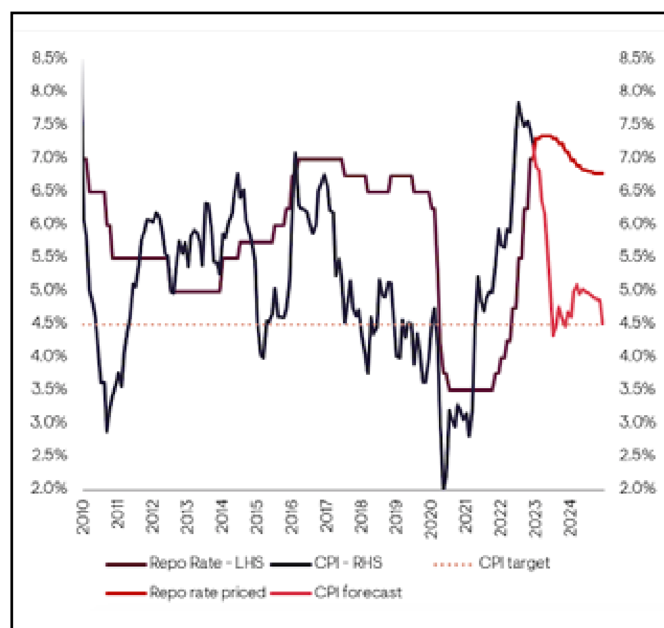
With headline consumer price index (CPI) slowing, the Fed Federal Reserve could slow the pace of its tightening cycle to 0.25% at its February Federal Open Market Committee (FOMC) meeting.

Across the pond, a relatively warm winter in Europe has softened demand for natural gas and still tempers energy prices. The relatively benign outlook for global energy prices still places downward pressure on global CPI, allowing central banks to take their foot off the throttle and slow the pace of monetary policy tightening.

Late in December, China relaxed their Covid-19 controls, which has already improved sentiment about Chinese growth. This move, combined with measures to support the property sector taken in late 2022, will likely bolster commodity prices and further buoy the commodity-exporting emerging markets.

Here at home, headline inflation peaked in July 2022 at 7.8% in July 2022, falling to 7.2% in December. Looking ahead, we see headline inflation averaging 5.4% in 2023, largely owing to declining petrol prices and a deceleration in food inflation. At the current 7.25%, the repo rate reflects a more neutral policy setting (relative to expected inflation). With the inflation picture improving and many of the upside risks abating, we expect we are close to the end of the SARB's South African Reserve Bank's hiking cycle.

*Inflation and repo rate outlook*




*— As we expect commodity proces to remain elevated, we also see fiscal revenues performing well. This should allow National Treasury to further consolidate the debt burden over the coming year. —*

The growth outlook remains difficult with consumer sentiment souring after a year of rate increases and high inflation. We remain optimistic about private investment in the energy sector on the back of structural reform underpinning our 1% GDP forecast for 2023. As we expect commodity prices to remain elevated, we also see fiscal revenues performing well. This should allow National Treasury to further consolidate the debt burden over the coming year. The economy has shown remarkable resilience to the high levels of power outages in 2022, but load shedding undoubtably places a cap on sentiment and potential growth.

So how do we construct fixed income portfolios in this environment? For most of last year we thought SA bonds were cheap but not riskless. Our job was to find a way to own SA bonds, earning the attractive interest on offer, but in a way where we protected the portfolio from the many developing risks. With global risks subsiding, local inflation likely to have peaked in the third quarter of 2022, and local political risks abating post the ANC elective conference, we are optimistic on bond market returns.

Hefty income on the table, combined with dynamic portfolio construction, will further help protect capital against global monetary policy and growth volatility, as well as constant load shedding locally. We remain overweight as the 10- to 15-year sector of the curve relative to longer-dated bonds as valuations look most attractive in this space. These shorter-dated bonds should benefit further from a slowing down or pause in the monetary policy cycle over the first half of the year. With yields on credit looking less attractive given where government bond yields are, we remain underweight investment-grade credit. However, we continue to look for yield-enhancing opportunities in high-quality counterparties.

The portfolio's currency exposure remains underweight, given dollar momentum waning and elevated terms of trade supporting the rand. Although, yields on offshore credit look attractive. We hold material exposure to high-quality SA counterparties issuing in dollars, and US investment-grade credit. This portion of the portfolio yields 6.3% in US dollars.

With listed property balance sheets in a healthier position post-pandemic and the sector once again paying dividends, we have marginally increased our exposure during the fourth quarter of 2022, further reducing our underweight. As we expect a slowdown in economic growth in response to global monetary policy tightening, we remain more constructive on the prospects for SA government bonds relative to listed property. **IRFA**

**Peter Kent,** Co-Head of SA & Africa Fixed Income: Ninety One
**Adam Furlan,** Portfolio Manager, Fixed Income: Ninety One

**IMAGES:** SUPPLIED. **SOURCE:** NINETY ONE, STATS SA AND BLOOMBERG, JANUARY 2023

- TRENDS -

# HOW SA IS WELL POSITIONED TO ACCELERATE ITS MOVE TOWARDS SMART CITIES

*Smart cities offer a multitude of advantages for both governments and residents. They use technology and data to improve their efficiency as a city and to improve the lives of their residents, including making the city more environmentally sustainable.*

Take Singapore, for example. From digital healthcare and contactless payments systems to near-universal broadband and energy-efficient buildings, Singapore has become the global poster child for smart cities.

Dubai is another global frontrunner offering over 120 fully digital government services on the DubaiNow app, allowing residents to do everything from paying fines and settling bills to applying for residency and accessing healthcare services. Other leaders in the move to digitise city-living are Zurich, Oslo, Helsinki, Auckland and Lausanne.

## WHAT CAN SOUTH AFRICA LEARN FROM THE GLOBAL LEADERS?

In 2019, President Ramaphosa announced the intended development of three smart cities, namely Nkosi City, bordering the Kruger National Park, Lanseria Smart City in Gauteng, and the African coastal smart city in the Eastern Cape, which is still in the planning stages.

Nkosi City is intended to be a job generator where employment will be driven by agricultural projects built alongside RDP housing in an integrated manner and will allow residents to sustain themselves from the farms. The city will derive power at least partially from a solar farm and a biomass renewable energy plant.

The African coastal smart city is still in the planning stages and will serve as an investment catalyst for one of the country's under-developed regions. The Lanseria Smart City will take advantage of the nearby airport to drive its growth and economic development, and feature rainwater harvesting and solar energy, along with urban planning that encourages a pedestrian lifestyle. The African coastal smart city is still in the planning stages and will serve as an investment catalyst for one of the country's under-developed regions.

What the global smart city leaders have in common, however, is that they have built on and developed existing infrastructure, transforming cities iteratively. South Africa is well positioned to adopt this approach in concert with our development of new cities.

South Africa's 'unsmart' cities are ripe for digitising. Our biggest cities have a lot of the essential infrastructure that forms a solid base for a smart city conversion including high levels of smartphone penetration, high-speed fibre networks, CCTV camera networks and, increasingly, internet of things sensors, solar power and rainwater harvesting systems.

Cape Town is already hailed as one of the leading smart cities in Africa, along with Nairobi. It boasts end-to-end solutions, including fibre, that can support everything from emergency systems to billing processes. CCTVs located throughout the city provide data, which can be used to analyse traffic volumes and other variables that affect congestion and need to be considered in city planning. Capetonians have already experienced how this can be used to their advantage: recent data revealed the city should scale back on the number of buses on the road.

Both Johannesburg and Pretoria have extensive CCTV networks, which could be used to collect and analyse data.

Maintenance of many of these systems is needed, but South Africa has the skills and the expertise to do this quickly and effectively, harnessing the potential these cities have to establish themselves as global competitors. Leveraging the infrastructure already in place would not only be less costly, but would also enable us to start delivering on our smart city vision more rapidly. South Africans are ready. IRFA

**Jan Bouwer**
Chief of Digital Platform Solutions: BCX

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# THREAT HUNTS FORM PART OF A PROACTIVE CYBERSECURITY STRATEGY

*Ransomware remains one of the top cyber threats facing businesses in South Africa and the world – causing financial, reputational, and collateral damage.*

In today's world, responding after the fact to a ransomware attack may be too late. While it remains essential to always have backup and the ability to recover from a clean copy of data, this is no longer sufficient to mitigate the threat of ransomware. Increasingly, the data itself is being used for extortion purposes, so the goal post has shifted from reactive recovery to proactive prevention.

There are many tools available to assist with this, including threat hunting, which offers a proactive solution to preventing threats from dwelling on networks, wreaking havoc, and stealing data that can then be used for nefarious purposes. Threat hunting helps organisations stay a step ahead and mitigate the growing risk of cybercrime.

There is a growing trend towards cyber extortion, where data encrypted for ransomware purposes is then leaked to the public or even used against individuals. Backup and recovery, while they remain essential, are no longer sufficient to adequately protect businesses against this threat. A more proactive approach is now crucial, including threat hunts, which proactively search networks for cyberthreats that may be lurking undetected.

## LUCRATIVE TARGETS

The threat of cyberattack is real and growing, and the likelihood of businesses being attacked is increasing daily. In fact, South Africa is the second most targeted country in Africa, with ransomware among the top five cyberthreats. The public sector, infrastructure and large organisations are the most attractive targets for several reasons, chiefly because they have information that is valuable as well as the means to pay the ransom.

The cost to benefit ratio for cybercriminals of an attack on large organisations is highest, whereas smaller businesses may be a lot of effort for cybercriminals with little reward. However, realistically any business could potentially fall victim to a cyberattack, and it pays to be prepared.

## CHANGING ANGLES

In addition to becoming more frequent and more sophisticated, ransomware attacks have also shifted away from merely encrypting the data to hold it to ransom. The entire modus operandi has changed from denying data availability to disclosing data that has been stolen. There are many repercussions to this, including extortion of individuals based on stolen data, reputational damage resulting from leaked information, as well as compliance breaches and fines.

It also means that having a backup and restoring data from a clean copy is no longer an effective approach to mitigating risk. Once data has been stolen, there is no way to get it back, even if the organisation has another copy of the data with which they can attempt to carry on business Rather, prevention and detection have become critical.

## SEEK AND FIND

Threat hunts are automated tools that proactively search for security risks on the internet, the dark web, and within an organisation's network. Where threat detection systems will identify known threats, threat hunting looks for threats that are unknown, undetected and unpremeditated. When potential threats are identified, an alert can be triggered so they can be investigated further, and appropriate action taken.

These technologies make use of intelligent software, which combines next-generation technologies, such as big data processing, artificial intelligence and machine learning, with human intelligence to complement existing security solutions, add another layer into the security mix and drive an enhanced security posture. IRFA

**Simeon Tassev**
MD & QSA: Galix Networking

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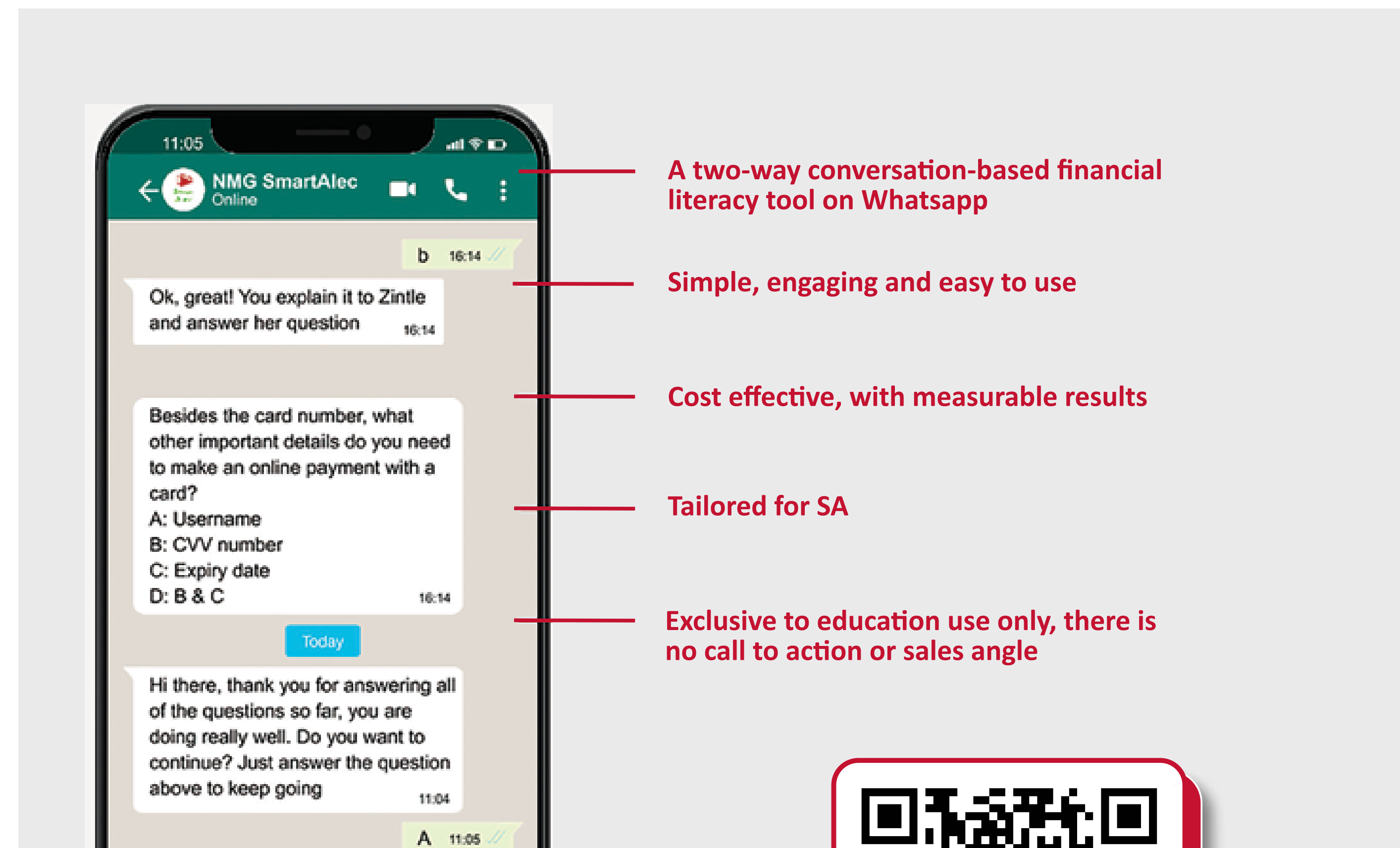


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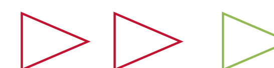

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- TRENDS -

# How retirement fund trends will affect you

*According to the South African Treasury, only six out of every 100 South Africans will be able to retire comfortably. A recent BusinessTech poll shows more than a third (35%) of middle-class South Africans aren't putting any money away at all for their retirement.*

The two biggest reasons that retirement fund members don't have enough money to retire on are that they don't save enough, and that they don't preserve their retirement assets when they move jobs. And if you think you can easily catch up on your retirement savings by making additional contributions later, you're in for a rude awakening. Depending on when you start contributing again, the required rate could be anything ranging from 17% to 50% of your salary.

One of the positive effects of Covid-19 is that it made South Africans more aware of the need to put themselves on the road to good financial health and a comfortable retirement. To do this, it's important to know the key trends in the retirement fund industry right now, and how they affect you.

## THE TWO-POT SYSTEM

Government's proposed new two-pot retirement system (which is currently set for 2024) tries to balance the need to survive financially, both now and after retirement. Basically, the system will see you put one-third of your retirement contributions after the effective date to a savings pot that allows early access, and two-thirds to a pot that is used to buy an annuity after retirement.

The benefit is that it will prevent people from having to take out expensive short-term loans, while being forced to preserve two-thirds of their funds over the long term and not cashing in when they change employers. The downside is that any withdrawals are fully taxed and erode your capital. The bottom line: get advice.

## GROWING DIGITISATION

Like most industries, the retirement fund sector is rapidly digitising. This means retirement fund members can easily monitor their funds' performance and will be able to have greater insight when they discuss their options with a retirement counsellor. In fact, using digital tools to understand the retirement income you are likely to receive is an important part of proper retirement planning.

## MORE ANNUITY OPTIONS

The days of being locked into a retirement income that was chosen for you are over. There are various forms of guaranteed retirement annuities that provide an income for life (and your spouse's life, if you elect this option), or pay a lump sum benefit upon death. Get advice on which works for you; there are options that can secure your fixed living expenses via a guaranteed annuity to ensure these costs are covered for life or a living annuity where any residual capital can offer some sort of financial legacy for your family. IRFA

*— Like most industries, the retirement fund sector is rapidly digitising, which means retirement fund members can easily monitor their funds' performance and will be able to have greater insight when they discuss their options with a retirement counsellor. –*

**Craigh Chidrawi**
Executive Head of Retirement: NMG Benefits

IMAGES: SUPPLIED

# A sustainable alternative for one of SA's biggest sectors

*Like its counterparts across the world, the South African mining industry is an electricity super user. Unsurprisingly, it was one of the first industries that had to comply with South Africa's Carbon Tax Act, which is driving mining companies to consider alternatives to reduce their operating expenses while meeting their regulatory obligations.*

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It is not only the Carbon Tax Act that is moving the industry towards change; mining companies are moving towards more sophisticated process and control equipment, which in turn requires stable, consistent and high-quality power to ensure these systems run optimally and won't fail prematurely or frequently, causing downtime. Additionally, mines require reliable electricity to remote locations where new operations are designed and constructed. Combined with electricity tariff hikes, one can understand why mining companies are scrambling to find feasible alternatives.

To counter grid instability, as well as availability, many mining operations are relying on internal power sources such as diesel generators to run operations. Mines are also bringing renewable energy sources, like solar and wind, into the mix to establish a hybrid energy model.

While the above does provide some form of renewable energy, it unfortunately still relies too heavily on fossil fuels, in the form of generators and grid supply, to meet daily operational demand.

## THE MICROGRID – SELF-CONTAINMENT OPTIMISED

To truly make the most of our country's abundance of natural energy resources in a sustainable manner, while reaping the benefits of reliable and quality energy, mining companies should incorporate the concept of microgrids into their operations.

Microgrids offer mines the following important benefits:

- They harness modern renewable power generation – wind and solar are widely available, and becoming increasingly cost-effective and generally safer to operate than traditional sources.
- Energy storage – comprising battery energy storage systems (BESS) and/or thermal and mechanical methods, storage abilities support a clean energy transition by firming up the availability of intermittent power sources and increasing grid flexibility to drive positive outcomes. Moreover, battery storage is becoming increasingly affordable and attainable.
- Advanced control technologies – such as cloud computing, data analysis and the Internet of Things (IoT) to optimise, autonomously schedule and control energy production and consumption.
- Facilitating compliance and ESG – self-contained, on-site energy generation from greener sources can improve a network's sustainability, reliability and resilience.

*— Software and analytics need to be used to make the most of microgrids and ultimately mines' sustainability goals. —*

## THE DIGITAL AND ENERGY PARTNERSHIP

Software and analytics need to be used to make the most of microgrids and ultimately mines' sustainability goals:

- Transparency of consumption, in other words, energy's visibility, is the starting point for decarbonisation, and obtaining insight from across the corporate value chain is vital to measuring and controlling what power resources are used.
- Analytics and AI can automate the conversion of data-driven insight into real-time decision-making.
- Digital twin technologies enable modelling the characteristics of the mine (demand/load) to facilitate predictive shifting of flexible operations to when renewable generation is at peak.
- Ecosystem collaboration leverages the skills and know-how of end-users, technology partners and integrators.

To forge a future that offers reliable, quality and sustainable energy, mines should include on-site generation such as microgrids into their energy mix, which is realised by a partnership of energy transition and digital transformation. Ultimately, using on-site energy more efficiently improves mining processes' productivity, reliability, safety and the expansion of operations. IRFA

**Vladimir Milovanovic,**
Vice President, Power Systems: Anglophone Africa Cluster at Schneider Electric

- LAST WORD -

# CAN CHATGPT AMPLIFY CYBERCRIME?

ChatGPT is a new artificial intelligence (AI) chatbot that understands natural human language, and provides comprehensive and concise responses to questions. It can write essays that feel like a human was the author (much to the concern of teachers, academics and authors) and it can create computer code, sparking worry ChatGPT could be used as a cybercrime tool. That may happen; however, the real risk lies in how this software and its peers could amplify impersonation and other existing cybercrime attacks that already work very well.

ChatGPT will make it easier to access cybercrime tools and learn how to use them, but this is a secondary concern, at least for now. The bigger problem is how it will be used for scams. ChatGPT and similar AIs won't create new cybercrime threats; they will make current threats worse.

ChatGPT is part of a new trend called generative AI. While ChatGPT conjures written paragraphs, image generators such as DALL-E and Stable Diffusion create spectacular art in minutes. Several companies, including Google, have AI systems, which generate realistic videos. Last year, a startup showcased a fake voice interview created by an AI between podcast star Joe Rogan and the late Apple CEO, Steve Jobs!

OpenAI, the company behind ChatGPT, also created an AI called Codex that writes computer code. It wasn't long before criminals and security experts tested the combination of Codex and ChatGPT to create hacker scripts. Darkweb forums, where online criminals meet, started posting examples of AI-generated attack code.

ChatGPT will not make a newcomer good at cybercrime coding. A potential cybercriminal would still need a lot of experience to combine different codes. But an AI could generate code at a pace and scale that would help experienced criminals do more, faster. It could also help inexperienced people get better access to the many cybercrime tools available online, with support on how to use them.

*— Cybercrime often uses social engineering, a set of proven techniques that scam people into sharing access details. —*

Cybercrime often uses social engineering, a set of proven techniques that scam people into sharing access details or valuable information. It's the oldest trick in the book. Social engineering is when someone pretends to be somebody or something else. The Trojans thought they got a big wooden horse as a gift, not an invading army. This has never changed. Cybercriminals do this all the time, using methods like phishing and man-in-the-middle attacks.

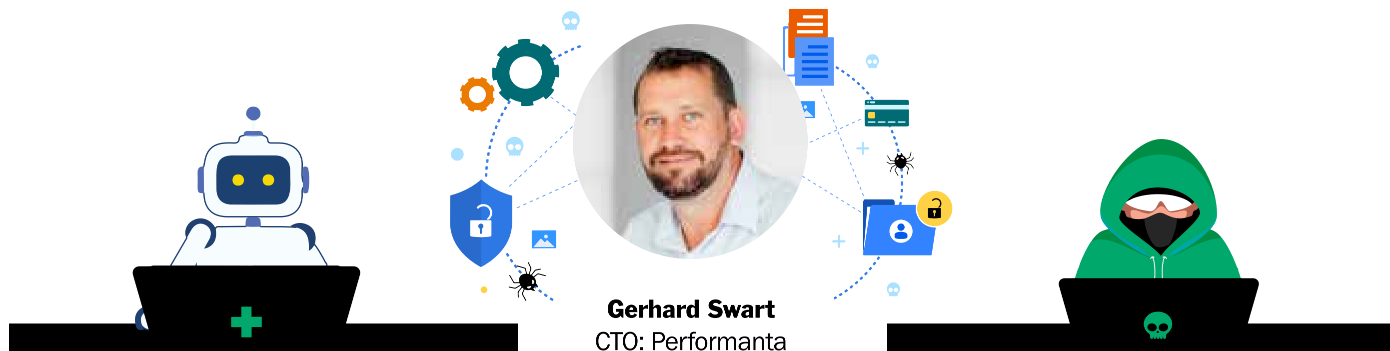
From this perspective, generative AI could become a significant cybercrime enabler. Criminals can generate emails that mimic the language and style of executives. They can create correspondence in different languages, and they might even start to clone people's voices and faces. There is no evidence these latter activities have happened, but it's no longer science fiction.

This development is a huge concern in the long run. Generative AI poses a very real cybersecurity risk and the concerns about cybercrime are certainly not overhyped. They're just not so simple, for now.

Fortunately, the cybersecurity world knows these tricks. Modern security can deal with phishing and impersonation attacks. It can detect and prevent the type of tricks, which generative AI generates. But to create the advantage, people and companies need to take cybersecurity more seriously.

Most attacks happen, not because we cannot secure systems properly, but because we do not bother to do so. Companies leave cybersecurity as an afterthought, or just throw money at the problem. They don't collaborate with staff to create cybersecurity awareness and they neglect to involve their cybersecurity people in business conversations. They forget to create what I call a cybersafe environment.

In the future, generative AI may radically change cybercrime, but it may already be amplifying what online criminals can do. IRFA



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