national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

## "Prudential Regulation of Foreign Exposure for South African Institutional Investors" Discussion document

In the 2008 Budget, the Minister of Finance announced the replacement of exchange controls on institutional investors with prudential regulation. The 2008 Budget also saw an increase in foreign-exposure limits as an interim step towards finalising the prudential regulatory regime for foreign exposure by institutional investors. This shifted policy from a transaction-based process, requiring application and approval, to a system of regulating foreign exposure of institutional investors.

In December 2010 the foreign asset limits for institutional investors were increased by 5 percentage points across the board (see Press Release on 13 December 2010). This announcement was in line with the above approach and the announcement by the Minister of Finance in the 2010 *MTBPS* that the prudential foreign exposure framework for institutional investors will be reviewed to support portfolio realignment and offshore diversification into Africa and other emerging markets.

In order to finalise the prudential regulatory framework for the regulation of foreign exposure for institutional investors, National Treasury commissioned independent research that resulted in the development of a discussion paper for public consultation. The paper by the Center for Research into Economics and Finance in Southern Africa (CREFSA) entitled "Prudential regulation of foreign exposure for South African institutional investors" is being released for public comment.

The paper argues that foreign asset limits in South Africa have both micro and macroprudential objectives. In the case of microprudential regulation, foreign asset limits for retirement funds and long-term insurance companies should promote the benefits of foreign diversification of institutional portfolios, while providing a limit on overall foreign risk exposure in line with the existing rules-based framework for the regulation of risk. In the case of macroprudential regulation, the objective of foreign asset limits is to limit the volatility of capital flows and contagion of international crises and more generally to avoid an excess reliance on volatile foreign capital to fund domestic investment.

Finally, the paper also discusses the definition of foreign assets for the purposes of prudential regulation of foreign exposure. It argues that the classification of foreign companies with listings on the JSE as domestic assets weakens the framework for the prudential regulation of foreign exposure. Options for classification are outlined that take into account the historical presence of non-resident companies on the JSE with substantial economic interests in South Africa.

While public consultations on the paper will be conducted, National Treasury reiterates that any change to the classification system would be forward looking and would not affect the current status of non-resident listed shares with a domestic classification on the JSE.

### Invitation for comments

Comments on the discussion document are invited from all interested stakeholders. Written comments should be sent to: financial.policy@treasury.gov.za or faxed to 012 315 5206 on or before the 30 April 2011.

**Issued by: National Treasury**
**23 February 2011**