MINISTRY OF FINANCE
REPUBLIC OF SOUTH AFRICA

KEYNOTE ADDRESS OF THE MINISTER OF FINANCE AT THE

NATIONAL UNION OF MINEWORKERS RETIREMENT FUNDS SUMMIT

HERITAGE CONFERENCE CENTRE, ROSHERVILLE

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Good morning distinguished guests, ladies and gentlemen. I bid a special good morning to those of you who are sitting before me in your capacity as trustees.

I'd like to start by applauding the leadership of the National Union of Mineworkers for demonstrating the quality of leadership to convene a summit such as this. It shows great foresight and commitment to the common cause of protecting the interests of retirement fund members.

I also applaud the approach outlined in Gwede Mantashe’s letter inviting me to address you. The letter states that: “The objective of the summit is to empower our trustees and members about the control and administration of their retirement funds.”

This practical approach is to be encouraged. You will be debating a host of issues related to retirement funding, but my plea would be that you tackle these issues in such a way that each and every trustee here today will return to the workplace armed with the information and practical suggestions they need in order to make a palpable difference to the quality of fund governance. For that is what we are here to talk about today – the “quality of trusteeship”.

When I refer to each and every trustee here today, I am counting myself in that number. I am speaking to you today not as the holder of the Budget purse, but as a fellow trustee. My time is running out as the sole trustee of the largest pension fund in the country – the Government Employees Pension Fund with R350 billion under management, made up of the contributions of civil servants and Government as the employer – but I certainly understand the challenges of trusteeship (and I am more than happy to share them!).

It is in this spirit, as a fellow trustee, that I also want to be practical in my address to you today. Unlike fund managers and investment consultants, I will try not bewilder you with abstract concepts, nor speak to you in that strange language that actuaries use to converse.

I would like to come back to first principles and remind everyone here today that trusteeship is integral to the work of trade unions. Trade unions are established to protect the interests of their members. This includes not only the working conditions but also the living conditions of their members… and integral to this is making sure that members can continue to live with dignity in their old age. The funds in pension and provident funds are effectively deferred earnings. Trustees should ensure the long-term protection of those funds, in much the same way that unions fight for the protection of their members' working conditions on a day-to-day basis.

The right to pension and provident funds is something that unions such as the NUM fought hard for over many decades. For more than 100 years black mineworkers were given something called Long Service Awards while their white counterparts had fully fledged pension funds. The NUM has been instrumental in establishing and improving the retirement fund environment for all mineworkers. The rights that have been obtained today are the fruits of those struggles. They cannot be simply thrown away or treated casually.

This right of access to the means of providing for retirement is critical. It is one of the guiding principles laid out in Government's recently published Discussion

Paper on Retirement Fund Reform that each and every individual should have the opportunity to adequately provide for their own retirement and the needs of their dependents. Far too many individuals reach retirement age without a funded benefit and hence rely on a government social assistance grant programme.

With proper retirement provisioning, members need not rely solely on the R780/month social old age pension and can enjoy a more stable standard of living in old age. Two aspects that can seriously impact on these retirement benefits are the number of years of contribution and the costs of administration. These are both areas over which trustees can make a difference. Members need to be made aware of the need to preserve their savings for as long as possible and trustees need to scrutinise the costs associated with managing the fund.

Let us commit to using the hard-fought rights to retirement provision to their full potential. How can we as trustees be fully empowered to administer our funds effectively to the benefit of our members?

These questions become particularly relevant in the defined contribution environment. Whereas the GEPF is a defined benefit fund, the NUM's members belong to a range of different types of retirement funds – defined benefit, defined contribution and provident funds.

Under DB funds, such as the GEPF, financial obligations are determined by the earnings of its members. Members have certainty over the future value of their retirement benefit, while if there is a shortfall between these obligations and the market value of the fund’s assets, it is the employer, Government, through the Minister of Finance, who must top it up.

Members of DC schemes, however, bear the full brunt of fluctuations in the market. Under a DC arrangement, each member has, in a sense, his or her own mini-fund for retirement. The amount invested in the mini-fund is dependent on the value and length of the member’s contribution. These mini-funds are pooled together for the purposes of administration and investment. At retirement, the value of the mini-fund depends on how the assets of the pooled fund have been invested and how these investments have performed.

The ‘pooled fund’ is invested by a set of fund managers. If fund managers do an excellent job, the fund performs well and all its members are richer. If the fund manager makes lousy decisions, it is the fund members – and not the employer – who end up poorer.

Fund managers far too often reap the benefits of upside performance, while avoiding exposure to any of the downside risk. The only people that can hold fund managers to account are the trustees. In short, the difference between members being richer or poorer will depend on the quality of trustees.

Fund managers are highly skilled professionals who have an interest in growing the assets they have under management. They have no interest in losing money, but at the same time, the desire to grow these assets as quickly and dramatically as possible can often lead asset managers down the path of temptation in making risky investment decisions with the money of workers… After all, the losses are not theirs to pay for.

Healthy fund management will consist of a prudent balance of government bonds to provide inflation protection, equities to provide growth, and alternative investments to hedge against dramatic downturns or to try and gain an extra few basis points of return. An extra layer of diversification of risk is added by spreading these investments, both across countries and across sectors – the idea being that when one area or sector is doing badly, hopefully another is doing well. However, despite all of these prudent precautions, there are more than a few examples of where fund managers have blatantly flaunted the rules and got it badly wrong!

Many of you sitting before me are aware of a South African pension fund which lost about R1,8 billion of member's money speculating in maize futures contracts. What was the fund doing putting that amount of money at risk on agricultural derivatives?!! Internationally, the well-known example of Enron is a painful lesson in both corporate governance and pension fund investment. Since the Enron pension fund invested its assets in Enron itself, when Enron collapsed, so did their pension fund. This is a situation that could have been easily avoided by appropriate and diversified investment of the pension fund's assets.

Who has responsibility for avoiding these types of tragedies? It can only be the trustees. I cannot stress more firmly that the conduct of fund managers is determined by the quality of trustees.

Let me give you another example. This time of the power of trustees. A celebrated case in England a few years ago was that of Unilever Pension Fund Trustees versus Merrill Lynch Asset Managers. Unilever took Merrill to court arguing that the fund manager's high-risk investment strategy, which lost it hundred of millions of Pounds, ignored the mandate of the trustee's investment strategy. The case was settled out of court and is believed to have cost Merrill Lynch Asset Managers in excess of R600 million (£50 million).

This illustrates the power that trustees can wield, if properly armed. This potential places a responsibility on the NUM and its members to ensure that the trustees are empowered to act. There can surely be no greater risk than to place power in the hands of persons who do not know what to do with it.

Those of you who attended the NEDLAC trustees conference held in October last year will remember me speaking of the proverbial David as trustee versus the Goliath of fund managers. We don't want trustees to be dazzled by the fancy speak of investment managers and actuaries. Truly powerful trustees are those that are confident to ask questions, no matter how stupid they may seem, and stand firm by their responsibilities.

Trustee power also means shareholder activism. Again, this is something I raised at the NEDLAC conference. I note that this matter has received some publicity in the past few days. COSATU has said that it intends playing a more active role through its members, whose pension monies represent shares in a host of listed companies. I welcome this initiative. I would like to stress that I see the primary goal of shareholder activism as member and shareholder protection via improved fund and company governance. Members can, in effect, use their collective financial muscle to, for instance, encourage investment in companies that create jobs, and to limit the exorbitant increases in executive remuneration we have seen over the past few years.

But it is also important to note that the role of trustees is not to be fund managers. Quality trusteeship demands an arms length relationship with the fund manager to ensure impartiality in the setting and monitoring of mandates. Let me insert a word of caution here to trustees: make your decisions objectively. Don't be swayed by service providers who may offer you a free box seat at the Orlando Pirates and Kaizer Chiefs derby match!

The Retirement Fund Reform Discussion Paper dedicates a section to trustee conduct. We invite comment not only on this section, which deals with issues such as conflicts of interest, trustee training and the conduct of service providers in relation to fund business, but also on any of the proposals listed in the document. The deadline for the submission of comments is 31 March 2005. Let me assure you that all stakeholder inputs will be carefully considered, prior to the issuing of a final principles document.

In conclusion, what do the responsibilities of trustees cover? First and foremost, ensuring that they are adequately empowered to protect the value of workers' earnings. This requires education and training. Education of trustees themselves – so that they are not dazzled by fancy PowerPoint presentations; so that they can develop investment mandates and interrogate investment performance – but also education and empowerment of members. Trustees must ensure that members themselves have all the information they need, in an easily understandable form and on a regular basis, to be able to track what is, ultimately, their money.

We as trustees have the power in our hands. Let's ensure that we are quality trustees who use it wisely.

Thank you.