SIMEKA

member of Sanlam group

Investment Commentary

7 of 2020

Investing in South Africa's infrastructure

It is well known that Government and the private sector have both reduced their investment spending over the last few years. The private sector is looking for more favourable (business-friendly) economic policies from Government, whilst Government has over-extended itself on consumption expenditure along with an increase in interest expenditure, which is crowding out spending on investment.

The impact of the COVID-19 lockdown on the economy, and emergency spending by Government on the health crisis and immediate poverty alleviation, along with fiscal stimulus steps taken to kick-start the economy, is likely to result in a debt trap for Government. This means that our government now has very little room to allocate spending on much-needed investment into our economy.

At the same time, if we are able to mobilise efficient investment into infrastructure - attracting new investments into energy, water and sanitation; roads and bridges; human settlements; health and education; digital infrastructure and public transport - this activity will be an important catalyst to achieve much-needed economic growth.

For some time, Government has been putting in a considerable amount of work, led by the President's office, to mobilise private sector investment into infrastructure. On 23 June 2020, the presidency held a Sustainable Infrastructure Development Symposium, where it announced around 55 projects with some estimates indicating a value of over R700 billion that could be invested in over the next 10 years.

On 17 August 2020, National Treasury and the Department of Public Works and Infrastructure announced that they had signed a memorandum of understanding with the Development Bank of Southern Africa (DBSA) to establish and manage the country's Infrastructure Fund. Government has committed R100 billion to the Fund, in instalments of R10 billion a year for the next 10 years, highlighting that the shortfall in funding may be as high as R600 million or more, simply considering the projects that have been identified so far!

In July 2020, the ANC's Economic Transformation Committee issued a discussion policy paper on the role of infrastructure development in transforming our economy. This paper suggests that Regulation 28 be amended so that retirement funds could be mobilised to provide "cheap" funding for infrastructure spending. Although the paper does not mention prescribed assets, it does state that retirement funds should "enable cheaper access to finance for development and that retirement funds be "mobilised to take over certain restructured Eskom assets". It also states that development finance institutions need help in accessing cheaper finance from retirement funds, so that they can provide development finance at cheaper rates than commercial banks.

Simeka supports Government's initiatives to promote investment into infrastructure in South Africa. Efficient infrastructure investment has the potential to kick-start our economy in the short term and create a strong foundation for many years of sustainable growth leading to poverty alleviation in our country.

In our view, there is no need for any changes to be made to Regulation 28, as it already allows retirement funds to:

- invest up to 50% of their assets in debt of a listed entity or debt guaranteed by a public entity registered in terms of the Public Finance Management Act of 1999 (Reg 28, Table 2, s2.1(d)),
- 10% in private equity and
- another 15% in private unlisted debt that is not backed by Government.

This means a total of up to 75% of a retirement fund's assets could be invested into infrastructure projects. Furthermore, over time, companies that operate in this space could raise capital via listing on the JSE, to facilitate further investment into infrastructure in our country.

However, these projects must be supported by regulation specifying property rights; appropriate and preferably independent governance structures; and transparent tender, financial and project management processes, amongst others.

A number of opinions are aired on this topic at the moment. The voice of reason is coming out of National Treasury. The ruling party's voice is, however, much more ambiguous. Our hope is that sanity will prevail. Retirement funds should invest in infrastructure because these projects can offer solid long-term investment returns that are de-correlated from other investment opportunities available to them, if the projects are commercially viable and the opportunity provides a solid investment case. However, the projects must be commercially viable from the start. It is not the role of retirement funds to provide "cheap" finance to invest in infrastructure projects that are not commercially viable and don't offer adequate risk-adjusted returns. It is important to recognise that a retirement fund must act in the interests of its membership and take the fund's liability structure into account.

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