University of South Africa Retirement Fund

Investment Policy Statement

November 2024

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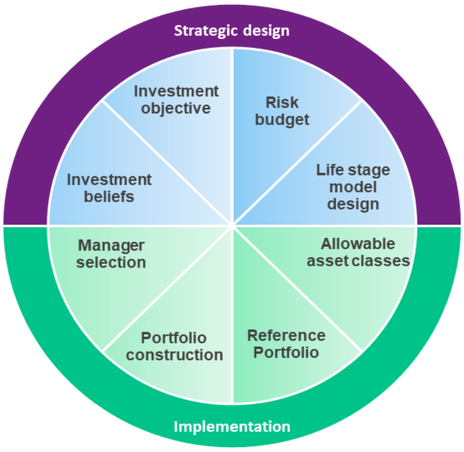
Section 1: Introduction

This document represents the Investment Policy Statement (IPS) of the University of South Africa Retirement Fund (the Fund) and has been adopted by the Board of Fund (the Board). The IPS is consistent with the governance principles set out in PF130 issued by the Financial Sector Conduct Authority (the FSCA). The chart below sets out the investment strategy control process of the Fund. The IPS sets out the *key principles* adopted in respect of each control process.



The life stage model design refers to the default investment strategy for members who are either uncomfortable or unwilling to choose their own investment strategy. A separate investment objective and risk budget is set for each investment channel that makes up the life stage model.

The Fund's investment strategy needs to comply with various statutory and guidance provisions. Compliance with these requirements is confirmed in Appendix A. The document is supplemented by a number of annexures which provide more detail on the derivation of the core principles and also covers the more operational aspects of the strategy.

Section 2: Fund overview

2.1 Governance

The Board has delegated the responsibility for the oversight of the Fund's investments to its Investment Committee subject to the mandate set out in Annexure 1. The Investment Committee's powers are limited to making recommendations to the Board. The Board retains control over the strategic issues related to the investment strategy and has the authority to implement the strategy and deal with operational matters. The Board also appoints the Fund's custodian, investment consultant, investment administrator and investment managers.

The Board takes the view that they are not experts in the field of investments. To deal with this position the Fund has appointed external investment managers. Furthermore, to bridge the knowledge gap between these investment managers and the Board, the Fund appointed an investment consultant that will advise the Board. The investment consultant holds the "trusted advisor" position and will be selected on the basis of their expertise and commitment to operate free from any conflict of interest in advising the Fund. The investment consultant is required to disclose any conflict of interest, the implications of which must be fully considered by the Board.

2.2 Nature of the Fund

The Fund is primarily a defined contribution arrangement meaning that the member's benefits depend solely on the contributions set aside as retirement savings plus investment growth thereon, but with a modest defined benefit underpin for most members who joined the Fund on or before 1 September 1996.

On retirement from the Fund, the member may elect to receive any combination of a life and/or living annuity from the Fund or to secure a pension from a registered insurer.

The Fund is open to new entrants and the membership consists of employees of the University of South Africa (Unisa), Universities South Africa (USA) and Purchasing Consortium Southern Africa (PURCO SA). These are all universities or organisations that operate in higher education in South Africa and any other employer permitted in terms of the Rules of the Fund. A summary of the key characteristics of the Fund's membership is set out in Annexure 2.

Section 3: Mission

3.1 Mission statement for in-service members

The Fund's purpose is threefold:

- Primarily the Fund exists to provide long serving members who have preserved their benefits throughout their working lifetime with reasonable retirement benefits. Specifically, the Fund targets (but does not guarantee) that a member with an average career progression[1] and 35 years of service, and who set around 16% of pensionable salary aside as retirement savings, should retire with a pension of around 75% of his/her pensionable salary at retirement at age 65.

- The secondary purpose of the Fund is to provide a vehicle whereby employees can make provision towards retirement on a cost and tax effective basis, using the bulk buying power of the membership and with oversight by the Board.

- Finally, the Fund aims to guide the investment strategy for members who are uncomfortable or unwilling to make investment decisions by offering a life stage model which is the Fund's default investment strategy. The aim of the life stage model is to provide an investment strategy that represents a reasonable balance between risk and return and that increases the chance of a member who meets specific conditions relative to length of service, retirement age and salary increase progression achieving a target net replacement ratio (NRR) of 75% at retirement age 65.

  The life stage model will be designed in such a manner that, under normal market conditions, members who invests their retirement savings according to this model should retire with a benefit close to that which they could reasonably expect allowing for any previous benefits for those members who joined the Fund later in their career.

  The Fund will engage with its members by providing helpful communication so that members can better understand their expected pension benefit and how their retirement savings can be applied to secure an income at retirement.

In addition, the Board aims to direct the Fund's investment strategy in a manner that is supportive of sound environmental, social and governance (ESG) principles with motivation of securing positive financial outcomes. The Board has outsourced the on-going ESG oversight to its appointed investment managers but requires the managers to report on how they are complying with ESG best practice and principles.

3.2 Mission statement for pensioners (life annuitants)

The Fund's guided annuity strategy as required in terms of Regulation 39 to the Pension Funds Act, is a life annuity. For these pensioners, the Fund has a pension increase policy which targets pension increases of 50% of inflation over the long term, subject to affordability. Thus, the Fund's mission in respect of pensioners in receipt of a life annuity is to deliver the targeted pension increases of at least 50% of inflation over the long term. The same principles of seeking superior risk adjusted returns and low costs will apply to the life annuitant investment strategy.

[1] Members who have an above average career progression are likely to retire with a lower benefit than the target and *vice versa*.

Retirees also have the option to secure a pension that provides for future pension increases of 100% of inflation. A retiree who elects this option will receive about a 25% lower initial pension than a retiree who elects the 50% of inflation option. The Fund will transition to a position whereby its guided annuity strategy becomes a life annuity targeting 100% of inflation by 2032.

3.3 Mission statement for living annuitants

The Fund also offers retirees a living annuity option or a combination of a life and living annuity from the Fund. A retiree who elects to receive any part of his/her pension as a living annuity is opting out of the Fund's guided annuity strategy.

The Income Tax Act limits remain applicable. The Fund limits the drawdown percentage of living annuitants on an age-related basis in order to reduce the risk of the retiree and his/her beneficiaries running out of the money. In addition, the Fund offers a default investment strategy for living annuitants.

Living annuitants may elect an own investment strategy and in this regard are allowed to invest in the same investment channels as in-service members.

Finally, the Board aims to oversee the Fund's overall investment strategy in respect of each of the membership categories above in a manner that is supportive of sound ESG principles with motivation of securing positive financial outcomes.

The mission for the living annuitants may thus be summarised as a design which is supportive of the sustainability of their income achieved through set drawdown limits and low costs, with investment options and guidance for retirees who are uncomfortable or unwilling to make investment choice.

Section 4: Core Investment beliefs

As described above, the mission of the Fund is to deliver superior risk adjusted real returns for each of the investment channels it offers. The strategy to deliver such returns is underpinned by a number of key beliefs that the Board has adopted in respect of how markets work.

Investment belief 1: Markets are broadly efficient, but pockets and periods of inefficiency exist

The price of an asset reflects the collective wisdom of many market participants all of whom aim to maximise their return.[1] This means that most of the time the price of an asset is a very good estimate of its intrinsic or fair value. However, markets are characterised by complexity and subject to human decision-making.

The complexity may cause many investors to avoid certain strategies as "too difficult" which may, in turn, result is less efficient fair price discovery. Human decision making is vulnerable to behavioural biases such as over-confidence, lack of courage / boldness as failing conventionally is more acceptable than succeeding unconventionally (and where the cost of being wrong is heavy criticism), recency bias etc. At times, these biases can intermingle into a crowded trade which results in an inefficient market (e.g., Dotcom bubble of the late 1990's).

This inefficiency in markets provides the opportunity for skilled managers to out-perform, but it not easy to do so because the manager is taking on the collective wisdom of all market participant, which is an effective pricing machine most of the time. Nevertheless, this broad belief in the efficiency of markets is the reason why the Fund has allocated 35% of its South African (SA) equities 45% of its global equities and 100% of its emerging market equities and global listed infrastructure to passive (or index tracking) strategies.

Investment belief 2: The Board believes that the investment market is a complex adaptive system

The complexity arises from the multiple drivers of investment returns, e.g., interest rates, government and central bank policy, demographics, political dynamics, etc., whereas the adaptive component arises from market participants aiming to earn high returns and incorporating new information into their decision-making.

Complex adaptive systems are characterised by uncertainty and ignorance rather than risk.[2] Given complexity, the most productive approach is likely to be one that focuses on the simplest component of the system, namely the individual company. In addition, there is information available to do in-depth analysis and research on individual companies to form proprietary insights rather than for the macro economy where the same information is available to all the market participants. This characteristic improves the odds of outperforming the market for skilled stock pickers.

Investment belief 3: Uncertainty and ignorance describe the nature of markets rather than risk

Investment returns do not follow a known and reasonable stable statistical distribution; rather they evolve and adapt based on new information, which is uncertainty and at times unknown. This means that the widely used classic "mean variance optimisation" approach does not work well, and the investment puzzle is better characterised by better decision making under the conditions of uncertainty and ignorance.

[1] There are exception such as Central Banks that have different objectives such as managing inflation or stimulating economic growth and such different objectives may create an inefficient market where more than one party can be achieve their desired outcome

[2] Risk exists when the form of the underlying statistical distribution is known and remains stable over time.

In addition, the Board believes that there is a material difference between volatility and risk. Volatility is the variation of market prices because of changes in the collective wisdom of the market participants. In some cases, this variation arises for irrational reasons, but volatility may also arise because legislative requirements which may result in some investors being forced sellers; in other cases, the variation correctly reflects new information. The Board believes that volatility that arises for irrational reasons or because there are forced sellers in the market represents an opportunity for the Fund to buy assets at cheap prices and so are capable of being exploited.

Risk on the other hand is overpaying for an asset – the risk may manifest itself in a partial or total loss of capital in real terms. The Board believes that one of the better ways to assess the risk of a particular asset is to consider the expectation that is implicit in the current market price. In general, the higher these expectations the greater the risk and so the Fund will have a bias to invest in a contra-cyclical manner.

Investment belief 4: Diversification and resilience are useful tools in dealing with uncertainty and risk

Diversification arises to the extent that the returns of assets classes or instruments have different return drivers. In a world of uncertainty and risk, it makes sense to blend asset classes and instruments that offer such diversification benefits. However, diversification must be limited to a process that contributes positively to the return and risk payoff, noting that adding to diversification inevitably adds poorer investment ideas to the portfolio. In addition, the return drivers of a particular asset class / instrument may change over time and what was once a good diversifier may no longer be so. It is thus vital to review return drivers on an on-going basis. Resilience is the deliberate redundancy built into the system to deal with unexpected events. Most often resilience comes at too a high cost to be included in the investment strategy. However, there are times when the portfolio's resilience can be improved at a low cost at which time the Board will actively look to exploit this opportunity.

Investment belief 5: The Board believes in long term investing

- The Board believes that adopting a long-term investment horizon represents a significant advantage compared to most other investors in that such a long-term horizon allows the Fund to: Ride out short-term fluctuations in returns and so benefit from the value of time diversification – as per belief 4, asset returns are noisy or volatile in the short term. Long-term investors have the luxury of knowing there are no short-term funding or liability issues and can earn risk premiums that manifest more reliably but only over longer measurement periods.

- Being able to profit from periods of elevated risk aversion or short-term mispricing – over long measurement periods risk is usually reasonably stable. When prices are low, risk aversion is high and so investors bid down prices in order to receive higher future investment returns. For a long-term investor, the risk aversion remains reasonably constant and so it can take advantage of periods of low prices within acceptable risk levels.

- Take advantage of illiquid investment opportunities. However, it is noted that acquiring illiquid assets comes at the cost of not being able to reduce exposure if the asset has performed well (although liquidity improves when an asset has done well because pro-cyclical investors want a part of the action) and not having "dry power" to buy distressed assets during bad times. It also limits the ability of the Fund to exit a mistake.

Having said the above, the Board believes that it is essential to have the flexibility to exploit short term opportunities as and when they arise and so the Board will also invest in strategies which are more opportunistic in nature.

Investment belief 6: The investment strategy must target a return which is in excess of inflation

The member needs to plan for a benefit related to his or her pensionable salary at retirement. Pensionable salary is closely correlated to inflation and therefore the liabilities of the Fund are inflation related. Accordingly, the primary objective of the various investment channels offered by the Fund must be set relative to inflation. Out-performance relative to a strategic asset allocation or peer group is an important secondary objective.

In the same vein, the primary requirement of a retiree is to receive a lifetime income that retains at least part its purchasing power.

Investment belief 7: The Board believes that investment manager skill is rare and that a qualitative approach is best for assessing manager skill

The Board considers investment management to be a highly competitive industry and as in all competitive environments there are relatively few consistent winners. In order to identify such skill a strong qualitative approach is required which focuses on identifying managers that have a meaningful and relatively easy to understand competitive edge to the market. Such a competitive edge may be founded in an intellectual edge, better quality of research than other market participants and exploiting the mistakes most other investors make. The investment firm's organisational culture is also a key driver of allowing skilled managers to ply their trade successfully.

The Board further believes that it is not sufficient for the manager to have a discernible competitive edge and sound organisational culture; the firm must also strongly align their interest with that of the Fund.

Environmental Social Governance ("ESG") beliefs

This section sets out the Board's ESG beliefs which are a subset of its core investment beliefs.

ESG matters

The Board firmly believes that society needs to ascribe to a system in which "what we take from the land must be given back" and that the structure of society must promote fairness and transparency.

Investee companies whose business models don't incorporate these principles are more likely to fail over the long term. However, company management is not tone deaf and to survive almost all will adapt their models to incorporate ESG considerations. The key issue for companies that face significant ESG headwinds is whether they can transition their business models successfully to compete in a world that will examine ESG practices closely. On the other hand, there is a significant upside for companies that are able to solve climate change problems and/or whose business model leads the market on ESG factors.

Naïve ESG themed investing is unlikely to result in superior long-term returns

The market is efficient and any information related to ESG consideration is likely imputed into the price. It also seems somewhat unlikely that an investment thesis that is easy to adopt (i.e. "invest in good") is likely to be a source of long-term out-performance.

The belief that naïve ESG themed investment is unlikely to deliver superior long-term returns is supported by the research of the highly rated team of Dimson, Marsh and Staunton.

No exclusions applied

It follows that, considering the above, the Board believes that ESG considerations are vital in assessing the intrinsic value of a company. The Fund outsources this analysis to its investment managers who are expected to handicap or advantage companies on the basis of how they evaluate ESG factors to impact on intrinsic value. Given the limited opportunity set for South African equities and the economy's current dependence on fossil fuels, no exclusions will be applied. Nevertheless, as per the below, the manager is expected to engage with its investee companies on ESG issues, particularly where the manager is likely to hold the counter for a lengthy period.

Importance of engagement

The Board believes that active engagement with company management adds value. This responsibility, together with voting on the companies that the Fund owns directly or indirectly via collective investment schemes, is delegated to the Fund's investment managers. Active engagement includes pushing management on ESG issues as positive changes in ESG practices beyond the market consensus view is likely to translate into positive price performance. The failure to achieve positive results through engagement may also be a factor that leads to the manager selling their holding.

Most managers provide a Stewardship Report on an annual basis and this report, together with periodic manager meetings will be used to evaluate the quality of the manager's engagement process.

Openness to invest in opportunities that offer fair risk adjusted returns and definite social benefits

The Board is receptive to investing in more complex investment strategies that have clear social benefits, but that also offer fair risk adjusted returns.

The Board believes that it is possible to earn at least fair risk adjusted returns and deliver positive social benefits. This outcome arises because most local investors are uncomfortable or unfamiliar with investing in private market opportunities in areas such as renewable energy, commercial farming, transport, water, and digital assets. There is thus a dearth of capital for such assets, which improves the return and risk payoff.

Actively seek out climate change solutions and other innovation

The Board believes that global accords on climate change will prove to be insufficient to deal with the climate change challenge. Rather history shows that to solve the problem, a combination of legislation and innovation is needed. The Board believes that there is a significant upside to being early investors in innovations that contribute to tackling the issue. The Board will actively seek to make an allocation to such strategies, be they in the public or private markets.

It bears emphasis that capital allocated in this way focuses on the innovation characteristics of the opportunity rather than being ESG themed.

Section 5: Life stage model and guided annuity strategy

The Board has designed a default investment strategy for members who are uncomfortable or unwilling to choose their own investment strategy, the so-called life stage model. This is consistent with the requirements of Regulation 37 of the Pension Funds Act. In addition, each investment channel will comply with the requirements of Regulation 28 on a look through basis.

Consistent with requirements of Regulation 39, the Board has also developed a guided annuity strategy.

5.1 Beliefs underlying the design of the life stage model

- Most members feel that they are not equipped or alternatively not willing to make their own investment decisions; hence the need for a default investment strategy (the life stage model). This belief is backed by empirical evidence which suggests that in excess of 90% of retirement fund members in South Africa simply follow the Board default strategy.

- The Board aims to provide a reasonably balanced risk and return strategy, which under normal investment conditions, should result in satisfactory outcomes for most long serving members who retire at or around their normal retirement age. However, the Board accepts that the life stage model may not meet the financial needs of all members and hence members may exercise investment choice.

- This philosophy of a default investment strategy designed to be efficient for the majority of members, but with an “own choice” provision is called *libertarian paternalism*. In this instance the term “paternalism” is used in the positive sense – the Board takes actions on behalf of the member that, for the majority of members, is expected to be in his or her best interest. The libertarian principle gives the member the choice to opt out of the paternal solution and self-select an investment strategy from the range of portfolios that the Fund offers.

- The life stage model is designed on the basis that the longer the member’s investment horizon, the more risk the member can take on. The six key reasons that underpin this logic are:

  (a) Whilst the member is young, he or she has relatively little money in the Fund and so the effect of a large negative return has a relatively small Rand impact on his or her retirement provision. The effect of future contributions and investment returns will swamp the effect of a large negative return whilst the member is still young.

  (b) On the other hand, when the member is close to retirement, he or she has the most money in the Fund and any negative return has a large Rand amount impact which reduces the member’s retirement income. In technical terms the member’s retirement benefit is determined by the money weighted return (i.e. the return taking into account the incidence of the contributions) rather than the time weighted return. Generally, this risk becomes more acute as the member approaches retirement, but the extent of this risk depends almost entirely on the form of the pension the member elects at retirement.

(c) The life stage model is designed to be consistent with the Fund's guided annuity strategy and the pricing basis of the Fund's life annuity. The return and risk profile of the Fund's Stable Portfolio is most consistent although not a perfect match, with this pricing basis. Accordingly, the model allocates the member's money to a combination of the Stable and Income Protection Portfolios pre-retirement, with the latter portfolio considering that retirees typically take part of their benefit in cash.

(d) The level of investment risk a member should take is related in part to the flexibility the member has. A member who is a long way from retirement can increase his or her retirement savings if he / she considers that his / her retirement provision is inadequate. Alternatively, the member can plan to work longer. On the other hand, a member closer to retirement has much less flexibility to change his / her retirement plans and therefore a more certain investment return is desirable.

(e) The benefits of time diversification – the argument here is that over the long term "things average out" and provided that a member does not buy assets at a price far in excess of fair value, then over time the premium for a riskier asset will come through thus reducing the cost of providing for retirement.

(f) It facilitates easier retirement planning if the member's expected investment return in the period just before retirement is more certain.

The implication of the above is that the life stage model will follow a glide path from a higher expected return and riskier strategy at younger ages to a conservative strategy closer to retirement.

- Consistent with the above, whilst the member is some way from retirement, the main risk he / she faces is that his / her retirement savings do not earn a sufficiently high return compared to inflation ("inflation risk") to secure his / her targeted benefit at retirement whereas the closer he / she gets to retirement protecting the terms on which he / she has to secure a pension becomes more important ("pension conversion risk").

5.2 Life stage model design

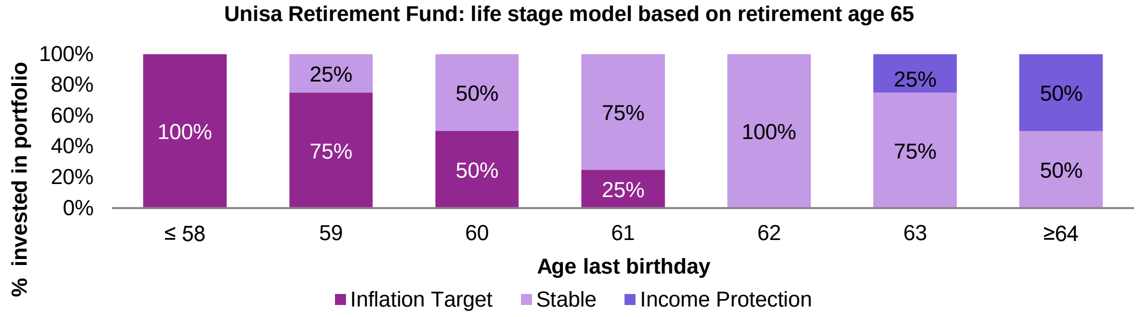
The Fund has adopted a three-portfolio life stage model with the three channels being:

- Inflation Target Portfolio – investment horizon at least 7 years and a targeted real return of 6.0% p.a. over rolling 7-year periods, net of investment management fees and charges.

- Stable Portfolio – investment horizon of 2 to 5 years and a targeted real return of 3.5% p.a. over rolling 3-year periods, net of investment management fees and charges.

- Income Protection Portfolio – investment horizon 1 year or less and a targeted real return of 1.5% p.a. over rolling 1-year periods, net of investment management fees and charges.

- The diagram overleaf sets out the structure of the life stage model of the Fund which is based on the principal employer's normal retirement age of 65. Please note that in respect of USA members (a participating employer in the Fund) and disability income claimants arising up to 30 June 2015, normal retirement age is 60 and so the life stage model is rolled back five years to be consistent with this earlier normal retirement age. Each investment channel will comply with the requirements of Regulation 28 on a look through basis.



Notes:

- The life stage model as per the diagram was implemented effective 1 August 2022. However, for members that were within two years of normal retirement age at this date, the pre 1 August 2022 ("old") life stage model will still apply. This period has expired on 1 August 2024.

- The model is designed around the normal retirement age of the member as notified by the employer.

- The member's accumulated savings will be transitioned according to this model at the end of the month in which he or she has a birthday.

- On-going retirement saving contributions will be invested in the same proportion as the Member's accumulated retirement savings (i.e. according to the model above) starting one month prior to the month in which the member has his or her birthday.

- During the transition period, the member's accumulated retirement savings (or Fund Credit) will be invested more or less in the percentages set out above (depending on the relative performance of the portfolios).

Members can also elect the life stage model with a retirement age of 55, 60 or 65. The default retirement age for members who don't nominate their retirement age is age 65 except in respect of USA members and disability claimants who became disabled before July 2015, where it is age 60. Deferred pensioners (also referred to as paid-up members in the regulations) that resign but who retain their money in the Fund will also default to life stage 65, unless they elect otherwise.

In addition, retirees who elect to defer the receipt of their pension to a later date will remain invested according to their investment strategy applicable at their retirement date unless they elect otherwise.

The life stage model is not intended to be the optimal investment strategy for each member. Rather it aims to provide a fair balance between return and risk and should under normal market conditions result in a reasonable benefit at retirement for a long serving member. The investment risk and return payoff of the model has been designed around what the Board has assumed to be the risk appetite of the average member.

5.3 Investment choice

The Board accepts that some members may be comfortable to elect their own investment strategy – they are the so-called “own choice” members. Such members may select any combination of the three life stage portfolios and the Shari’ah compliant portfolio. Members may elect a different investment strategy in respect of their accumulated retirement savings and their on-going (and future) retirement saving contributions in which case they become “own choice” members. Members are allowed to apply a different strategy to their Main and Supplementary Account. Members are permitted to change their investment strategy monthly, thus meeting the requirements of Regulation 37 of the Act.

A member entitled to the minimum benefit underpin at retirement will forfeit this benefit if he / she becomes an “own choice” member but retains the underpin guarantee if he / she elects a life stage model with a retirement age different from his / her normal retirement age. This restriction is required to mitigate anti-selection by the member.

The member’s investment will continue to be invested according to his or her choice unless the member makes an election to invest his or her money differently. Similar to the own choice members, the living annuitants can select any combination of the Inflation Target, Stable, Income Protection and Shari’ah Portfolios should such a retiree elect to opt-out of the Fund’s default investment strategy for this membership category.

5.4 Guided annuity strategy in terms of Regulation 39 of the Act

The Fund’s guided annuity strategy is a life annuity provided by the Fund. This life annuity provides a retiree and his or her spouse(s) with a life-long pension at a lower cost than the equivalent product from an Insurer. The life annuity provides an initial higher pension because future pension increases are expected to be 50% of inflation.

Retirees also have the option to secure a pension that provides for future pension increases of 100% of inflation. A retiree who elects this option will receive about a 25% lower initial pension than a retiree that elects the 50% of inflation option. The Fund plans to move to a position whereby its guided annuity strategy becomes a life annuity targeting 100% of inflation by 2032.

5.5 Two-pot Retirement System

The Two-pot Retirement System is implemented effective from 1 September 2024, which creates the vested, savings and retirement pots for members on their member credit accounts in the Fund. The investment strategies that are available to members pre-1 September 2024, remains available after 1 September 2024. In time, the available investment strategies will be considered to decide whether different investment portfolios should be made available for members’ savings pot investment than for their other pots. This will also be dependent on the Fund administrator’s administration system capabilities.

Section 6: Investment return objectives

As set out in section 5, the Fund operates a three-portfolio life stage model consisting of the Inflation Target, Stable and Income Protection portfolios. In addition, the Fund offers a Shari'ah compliant portfolio for in-service members and has a Pensioner Portfolio in which the assets backing the Fund's pensioner liabilities are invested.

6.1 Principles and objectives for the three life stage model portfolios

As described in section 2, the Fund has four broad categories of membership, namely defined benefit and defined contribution in-service members, paid-up members which may arise as a consequence of in-service members terminating service with the employer prior to retirement or, deferred retirees which may arise as a consequence of retirees who elect to defer receipt of their retirement benefits and pensioners (which includes life and living annuitants). The paragraphs below set out the principles adopted in setting the investment objective for each of these categories. Note that the investment objective in each case is set relative to normal market conditions and a long-term inflation rate of 5.5% p.a., which is broadly consistent with inflation expectations embedded in South African government bond yields.

6.2 Asset class returns

The return objective and risk constraint for each investment channel is set with reference to observed long term investment returns, the associated risk and correlation matrix for the three principal asset classes being cash, bonds, and equities, together with a subjective overlay to take due account of current market conditions. The derivation of the assumptions is detailed in Annexure 2 and are currently as follows: [WTW drafting note – small changes to be consistent with Annexure real returns)

Asset class	Expected real investment return p.a.	Volatility[1]
South African equities	8.00%	26%
South African listed property	9.00%	29%
South African nominal bonds	4.50%	16%
South African inflation linked bonds	3.75%	11%
South African Cash (Money Market)	1.50%	3%
Global equities (in ZAR)	5.00%	17%
Global listed Infrastructure (in ZAR)	5.00%	15%
Global listed property (in ZAR)	5.00%	16%

If achieved, the above investment return objectives would, for the *characteristic member*, result in a replacement ratio at normal retirement age of some 75% of the member's pensionable salary at that time. The assumptions made regarding the characteristic member are also detailed in Annexure 4.

[1] As measured by standard deviation.

6.3 Objectives for in-service member portfolios

A separate investment objective is set for each of the life stage investment channels offered by the Fund. The objective for a specific channel is driven primarily by its investment horizon. Portfolios with a long-term investment horizon will have a higher expected return target as a higher proportion of riskier but expected higher returning growth assets can be allocated to such portfolios.

The investment objective for the channels will also be sufficiently differentiated so as to be appropriate for members with different time horizons and risk appetite. The table below sets out the typical asset allocation and associated investment horizon for the three investment channels offered:

Investment channel	Typical asset allocation	Investment horizon
Inflation Target Portfolio	70% to 80% growth assets (e.g. equities and property) and 20% to 30% fixed interest assets (mainly bonds)	At least 7 years
Stable Portfolio	45% to 55% growth assets and 45% to 55% fixed interest assets being mainly cash and enhanced cash strategies	2 to 5 years
Income Protection Portfolio	Invested only in cash and enhanced cash strategies	1 year or less

Inflation Target Portfolio – objective and risk constraint

Investment return objective: a real investment return of 6% p.a. net of all charges over a rolling measurement period of 7 years with a risk budget as measured by standard deviation of 14% p.a.

The table below shows the modelled 10% to 1% (probability column) poorest *real returns* which may be expected over a 1-year and 7-year period for this channel assuming that the portfolio's return signature follows a normal distribution.

	1 year		7 years	
Probability	**VaR**[1]	**CVaR**[1]	**VaR**	**CVaR**
10.0%	-11.7%	-17.8%	-1.3%	-3.6%
5.0%	-16.4%	-21.8%	-3.1%	-5.1%
2.5%	-20.5%	-25.3%	-4.6%	-6.5%
1.0%	-25.2%	-29.5%	-6.4%	-8.1%

Thus, there is a 10% chance (i.e. once in every 10 years) that the real return over any 1 year will be worse than -11.7% ($VaR_{10\%}$) and should such an event occur the expected real return is -17.8% ($CVaR_{10\%}$). However, when measured over 7 years, there is a 10% chance that the real return over any 7 year period will be worse than -1.3% p.a. and once in this tail the expected real return is -3.6% p.a.

Stable Portfolio – objectives and risk constraint

Investment return objective: a real investment return of 3.5% p.a. net of all charges over a rolling measurement period of 3 years with a risk budget as measured by standard deviation of 7% p.a. Furthermore, the portfolio aims, but does not guarantee, to avoid a negative nominal return over any 12-month period.

The table below shows the modelled poorest *real returns* which may be expected over a 1-year and 3-year period for this channel assuming that the portfolio's return signature follows a normal distribution:

[1] The returns of all the portfolios follow a statistical distribution. In framing their risk budget, the Board is concerned about how poor outcomes can be over different measurement periods. For example, the Board may wish to estimate what the cut-off point is for the worst 10% of the returns (i.e. there is a 10% chance of the return being worse than this cut-off point). This point is called the Value at Risk for the 10% worst returns, abbreviated to $VaR_{10\%}$ which is -11.7% over one year. Arguably it is not sufficient to just know what the cut-off point is, it is more complete to estimate if one ends up with amongst the worst 10%, on average, how bad could it be. This statistic is called Conditional Value at Risk. The $CVaR_{10\%}$ is -17.8% over 12 months.

	1 year		3 years	
Probability	**VaR**	**CVaR**	**VaR**	**CvaR**
10.0%	-6.0%	-9.3%	-2.2%	-4.1%
5.0%	-8.5%	-11.4%	-3.6%	-5.3%
2.5%	-10.7%	-13.4%	-4.9%	-6.4%
1.0%	-13.3%	-15.7%	-6.4%	-7.8%

In addition, there is about a 10% chance that the nominal return over any 12 month period will be negative and if such an event occurs the expected nominal return is -3.5%.

Income Protection Portfolio – objectives and risk constraint

Investment return objective: a real investment return of 1.5% p.a. net of all charges over a rolling measurement period of 12 months with a risk budget as measured by standard deviation of 2.0% p.a.

The portfolio aims to provide a high degree of certainty about the return over the next 12 months and has an extremely low risk of a nominal capital loss over any 12-month period.

Shari'ah Portfolio – objectives and risk constraint

Investment return objective: a real investment return of 3.5% p.a. net of all charges over a rolling measurement period of 7 years with a risk budget as measured by standard deviation of 14% p.a.

The Shari'ah portfolio must comply with Islamic law. This investment channel does not form part of the default investment strategy and is an own choice portfolio.

6.4 Investment objective for the Pensioner Portfolio

The Pensioner Portfolio is only applicable to retirees in receipt of a life annuity from the Fund.

Investment objective: The Pensioner Portfolio aims to out-perform the present value of the expected pension payments making provision for pension increases of 60% of inflation (i.e. higher than the 50% of inflation as per the Fund's pension increase policy) priced off the South African government bond yield curve by 1% p.a. over a 10-year period with a tracking error of less than 4% p.a. Should this objective be achieved, the Fund should be able to afford pensioner increases of closer to 75% of inflation, noting that the Fund will retain its current pension increase policy of 50% of inflation.

The Pensioner Portfolio is managed employing a liability driven investment (LDI) approach. This means that rather than consider the absolute level of investment return, the focus is on the funding level of the Pensioner Portfolio. This means for example, if the assets of the Portfolio are 100 units and the liabilities are also 100 units, it is of no consequence to the Fund if the assets earn a negative return of 10%, provided that the value of the liabilities also fall by 10%.

80% of the Pensioner Portfolio assets are allocated to the Matched Portfolio ("MP"). This portfolio is invested to deliver 60% of inflation increases on 1 April each year. However, the same 80% of the assets should aim to hedge 100% of the interest rate risk on the full pensioner liability. To illustrate what is meant by interest rate hedging, assume that at a time the value of the pensioner liabilities (providing for pension increases of 60% of inflation) is 100 units and the MP has assets of 80 units. Assume now that interest rates increase and the value of the liabilities reduces to 97 units; the expectation is that the value of the MP units will fall to 77 units, by more or less the same 3 units. Conservative yield enhancement strategies are applied to a maximum of 35% of the MP. These strategies are expected to enhance the total yield of the MP by 0.4% p.a.

The remaining 20% of assets are allocated to global growth assets (i.e. equities and property). It is assumed that these growth assets will deliver an equity risk premium (excess returns to government fixed assets) of 3% p.a., which if achieved would add 0.60% p.a. (i.e. 20% x 3%) to the portfolio's return over the risk free government bond yields. The aggregate of the yield enhanced strategies plus the 20% allocation to growth assets represent the targeted 1% p.a. out performance of the liabilities over 10 years.

The tail risk associated with the MP is the moral hazard of the South African government under-stating inflation to limit their interest cost if inflation is very high. The 20% investment offshore provides some hedge against such an outcome because the ZAR is likely to weaken significantly in such a scenario.

The LDI manager (Old Mutual) must structure the MP assets in such a way that it delivers the monthly schedule of pension payments as provided by the Fund. In this way sequencing risk is managed as the Pensioner Portfolio will not be a forced seller of assets to meet pension payments.

Note: For retirees who elect to target 100% of inflation increases, the LDI strategy will be adjusted to target such a level of pension increase.

Section 7: Asset classes and benchmarks

7.1 Preamble

As per Section 6, the investment return objectives for the three investment channels have been set with reference to the three principal asset classes, namely equities, bonds and money market instruments. These asset categories have much more granularity – for example equity type assets include *inter alia* listed and private equity, property, infrastructure assets and agriculture. Similarly, bonds consist of listed and unlisted debt of sovereigns or companies. Furthermore, categorisation by region is possible e.g. domestic, global developed world, emerging markets, and frontier markets.

7.2 Principles for inclusion of a particular asset class

The Board has applied the following principles in deciding whether to include a particular asset class in the Strategic Asset Allocation Portfolio or not:

- The Board must have a good understanding of the asset class and in particular of the factors driving returns and the risk premiums the specific asset class offers.
- The market price of a particular asset class is driven by a number of factors. The Fund looks to invest in asset classes which prices are driven by different factors or more likely a different weighting to a specific factor so as to target good diversification benefits. Thus, asset classes which offer good diversification benefits will generally be an allowable asset class for investment. The factors driving the investment returns of the main asset classes are set out in Annexure 5.
- In addition to selecting asset classes on the basis of their returns being driven by different factors, the Board will seek to build a diversified portfolio by allocating assets to a wide range of risk premiums. The possible nature of the premium per asset class is also set out in Annexure 5.
- The allocation to a particular asset class needs to comply with the restrictions of the Pension Funds Act and in particular Regulation 28 to the Act.
- A maximum of 15.0% of the Fund will be invested in unlisted equity, hedge funds, property, and private equity arrangements (The maximum investment in any private equity and hedge fund is limited to 5% of the portfolio market value).
- For investments in long term themes, a thorough due diligence and risk assessment needs to be undertaken.

7.3 Benchmarks per asset class

In the case of listed assets, a published market capitalisation index will be available. The Board will select a market capitalisation benchmark that is a reasonable representation of the universe from which investments can be made.

In the case of unlisted assets, a suitable published benchmark may not be available. In this case the Board will set the benchmark with reference to the underlying nature of the assets (i.e. equity, bond, or money market) plus an appropriate premium to reflect the specific risks taken on. The current asset class benchmarks adopted by the Fund are set out in Annexure 5.

Section 8: Asset allocation

8.1 Strategic Asset Allocation

The Board has set a Strategic Asset Allocation (SAA) for each investment channel. The strategic asset allocation represents the mix of asset classes that is expected to generate a return over the long term which is consistent with the investment objective of that investment channel. The expected risk for the Strategic Asset Allocation also sets the risk budget for the relevant investment channel.

The Strategic Asset Allocation reflects a "do nothing" or passive approach and the calculated investment return and risk for a particular investment channel (using the benchmark return for each asset class) represents the return that would have been earned had the Fund simply invested in accordance with its Strategic Asset Allocation.

For the Pensioner Portfolio, the Liability Benchmark Portfolio is calculated based on life expectancy of the pensioners (and their beneficiaries) allowing for 60% pension increases on 1 April each year and the South African government nominal and inflation linked bond curve.

8.2 Methodology for deriving the Strategic Asset Allocation

In deriving the Strategic Asset Allocation for an investment channel, the Fund has used a combination of quantitative techniques (re-sampled mean variance optimisation) and subjective judgement.

The Board believes that a quantitative technique is based on too many assumptions and therefore the results of such a model should need to be interpreted with a common-sense overlay. The Strategic Asset Allocation set for each investment channel is therefore not positioned as the optimal solution; rather it represents a sensible approach which is expected to deliver reasonable outcomes under normal market conditions over the measurement period of the channel.

However, if the Board assesses a particular asset class to be very expensive or very cheap, it could revise the Strategic Asset Allocation materially on the basis that there is an assessed high probability that the specific asset class will move towards its fair value over a period of around three to five years. This medium-term approach to asset allocation is called dynamic asset allocation and are taken with at least a three year view because it may take a long time to revert to their normal state.

Section 9: Portfolio construction

9.1 Active versus passive management

The Board believes that the market is broadly efficient and for this reason it has allocated 35% of South African, 45% of global equities and 100% of emerging market equities to index strategies. In addition, the Fund's exposure to global listed infrastructure is managed on a passive basis.

In respect of the active manager component of the strategy, the Board takes the view that it, together with the investment consultant appointed, have a reasonable chance of identifying skilled investment managers that can exploit market inefficiency.

9.2 The asset allocation decision

The Board recognises that if it was possible to get the asset allocation decision right, significant value can be added in the form of higher return and/or reducing risk.

The Board will seek to add value via asset allocation in the following ways:

- The Board via its Investment Committee will review the Strategic Asset Allocation for each investment channel on a quarterly basis with a view to identifying asset classes that are significantly mispriced (i.e. very cheap or very expensive) by long term measures. The identification of such situations may lead to a change to the Strategic Asset Allocation for a specific investment channel. This approach is called dynamic asset allocation.

- Within a particular asset class, the mandate given to the specialist manager could allow investment of a specified percentage of the assets in cash if the manager regards the asset class as expensive.

Having dealt with the asset allocation decision in the manner described above, the Board will appoint specialist asset managers for each asset class, but it may use multi-asset class products if this represents the best implementation route.

Given the difficulty in getting the asset allocation decision right on a consistent basis, the Board will maintain an asset allocation quite close to the strategic asset allocation (except at assessed market extremes) and as such most of the value add and risk reduction is expected to be generated from instrument selection rather than asset allocation.

9.3 Specialist asset managers

The Board believes that specialisation in a particular asset class is likely to be a competitive advantage in a field as diverse and complex as investments. Hence, as described above, the Board has appointed specialist asset class managers for almost all mandates.

It is noted that if the amount to be invested in a particular investment channel is small, the Board will prefer multi-asset class mandates on the basis that the associated implementation difficulties argue against the use of specialist mandates.

9.4 Investment approach blending

There are three principles which inform the Board's approach to blending different investment approaches, namely:

- A portion of the South African and global equity allocation will be managed on a passive basis, thus reducing the "tracking error" to the benchmark and keeping costs low.

- The most robust approach to blending managers that constitute the active management component of the strategy is to combine skilled managers that approach the market differently and where there is little overlap in their shareholdings. In this way, each manager can hold a portfolio that is very different from the benchmark (called a high “active share” portfolio), with the aggregate blend having a high active share but the combination of the managers being largely neutral on factors such as country exposure, sector exposure and style. In this way, stock picking rather than macro factors drive the portfolio returns.

  It is possible to follow this approach in relation to global equities where there is a deep opportunity set; this is the approach that the Fund has adopted. However, in narrow markets like South Africa the efficacy of such blending is reduced.

- Selecting skilled investment managers is difficult and to diversify against selection error the Fund will appoint more managers rather than fewer. The constraint on diversification is that one reaches a point where the blend represents an enhanced index strategy but at a very high cost. Accordingly, blending of active managers should be done to the extent that it keeps the active share high. Naturally, in the deep global markets the Fund can appoint more managers than in the narrow South African market.

It is highlighted that the above principles apply to the equity asset class, noting that the same principles can be used, but to a lesser extent, in appointing fixed interest managers.

The current specialist mandates and the blending of investment approaches per investment channel are set out in Annexure 7.

Section 10: Manager selection

10.1 Qualitative assessment of managers

The Board will place a higher weighting on qualitative considerations in appointing its investment managers and so assign a lower weighting to past performance. The reason for this approach is that in a highly competitive industry only a small proportion of managers have exceptional skill and given the uncertainty in anticipating future returns, the very good observed performance by a particular investment manager could just as well be attributed to luck as opposed to skill, particularly over shorter measurement periods.[1]

The qualitative analysis must however be supplemented with a good quantitative analysis to better understand how the manager generates its performance and to check that the manager's holdings are consistent with the investment approach the manager claims to follow. The quantitative analysis will include an understanding of whether the manager's performance is due to getting a few big decisions right (less attractive) or more ideas contributing to the performance (a better outcome), the manager's performance under different market conditions (upside capture and downside protection), risk taken on (tracking error) for return generated, consistency between the counters held in the manager portfolio to their stated investment approach, etc.

10.2 Criteria for selecting managers

The Board has adopted the following criteria for the selection of an investment manager:

- The manager's Black Economic Empowerment credentials which must be consistent with the Fund's Transformation Policy.
- The manager must be assessed to have a discernible competitive edge to the market. This edge could take form of inter alia an intellectual edge, superior research giving rise to an information advantage and/or avoiding the mistakes other investors routinely make (i.e. a behavioural advantage). The competitive edge should be expressed via superior idea generation and portfolio construction.
- The assessed skill of the key investment professionals together with the diversity of opinion and constructive challenge within the team. The empirical evidence suggest that different perspectives and diverse opinion improve the quality of decision-making for complex adaptive problems.
- The manager should be part of a firm that has superior investment driven culture which has at its core the objective of delivering outstanding investment results for its clients. Characteristics of a superior investment culture may include a meritocracy that is regarded as fair, the ability to work together as a team, openness and transparency, and importantly giving power to the individuals that drive strong performance to clients as opposed to gathering assets.
- The manager must have strong portfolio construction skills which includes position sizing, buying and selling disciplines and careful management of risk to limited unintended aggregation of risks within the total portfolio.
- The firm should have an impeccable standard of ethics and should align their interest with that of the Fund. This includes a consideration of the investment management fees.

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[1] Over longer measurement period the luck starts to even out and a greater weighting can be attached for past performance in assessing manager skill. There are however very few managers with a long enough track record investing with the same approach and the same key decision-makers with materially similar assets under management.

- Where the manager adopts a long-term investment horizon, they must allocate sufficient time and thought to the consideration of ESG factors in selecting the instruments included in its portfolio.
- The investment approach of the manager must be consistent with the beliefs of the Board and add to the intended diversification characteristics of the portfolio taking into account risk and returns.
- Fees should form a key criteria in the selection of managers and not be only negotiated once the selected managers have been identified.

The Board accepts that it will be rare to find managers that comply with all the above criteria, but the appointed managers should meet a significant percentage of the listed criteria. Furthermore, the Board understands that assessing managers against the above criteria necessarily is somewhat subjective and therefore there is a risk that the Board could over-rate a manager's skill. In order to diversify against this risk, the Fund will appoint a number of asset managers for each asset class that constitute a significant percentage of the asset allocation of the particular investment channel.

10.3 Terminating or reducing exposure to an investment manager

The following events would lead to a review and the possible termination of the manager's appointment or the down-weighting of exposure to the manager:

- Rapid growth or decline in assets under management;
- Change in the investment philosophy and approach or a material change in the investment process;
- The manager increasing the risk profile of the portfolio significantly without being able to provide good reasons for doing so;
- Poor performance over an extended period if such poor performance cannot be reasonably explained by market mispricing, poor luck or a once-off "extreme event" error. Monitoring thereof will be done by using the Fund's quarterly investment dashboard;
- Loss of key personnel, including a situation where a key decision-maker is "promoted" to a different role;
- Perceived loss of passion and focus by the key decision- maker;
- Material change in the shareholding structure of the manager;
- Perceived adverse changes in the ethics of the manager;
- Poor policies in respect of ESG issues, especially if the manager adopts a long-term investment horizon;
- Change in market conditions or regulatory environment which has the effect that the manager's investment approach may no longer be effective;
- A significant exposure to a specific investment sector that cannot be reasonably justified;
- A negative change in the manager's Black Economic Empowerment rating;
- Perceived changes in the alignment of interest including the competitiveness of management fees.
- Any other matter that is perceived to affect the ability of the investment manager to carry out its mandate effectively or is considered by the Board to necessitate a review.

Section 11: Social responsibility

The Fund's investments will be managed in a manner that is consistent with the FSCA Guidance Note 1 of June 2019 and the King IV principles.

11.1 ESG policy

The Board believes that part of its social responsibility is to manage and oversee the Fund in such a manner that it delivers superior risk adjusted returns as such an outcome would increase the chances of the member being able to retire with reasonable benefits.

Negative screening

The Board draws a distinction between investments that have far-reaching social implications (e.g. climate change, child labour) and investments that may have negative ethical characteristics depending on the view of the investor (e.g. tobacco, alcohol and gambling).

The Board has decided not to apply any negative screening. The most likely candidate for negative screening is a ban on investing in fossil fuel companies on the basis that their outputs are primarily responsible for climate change. However, currently the local economy's energy supply is generated almost entirely by coal. Consequently, the economy would face enormous difficulty if all investors banned capital allocation to this sector, an outcome that the Board believes is not in the best interest of South African society.

Nevertheless, the Board is supportive of a transition plan to reduce the country's carbon footprint. To this end, the Fund will look to invest in clean energy forms (e.g. renewable energy) and will require the local investment managers that invest in fossil fuel companies to engage with the management of investee companies to improve their carbon footprint. The managers will be required to report at least annually to the Board on the outcome of such engagement. The Fund has exposure to the debt of local renewable energy projects.

Positive screening

Whilst the Board believes that positive ESG characteristics generally results in better company performance, it also takes the view that these characteristics are largely priced in by the market. Accordingly, the Board believes that investing in companies with positive ESG characteristics is unlikely to result in sustained market out-performance, although it accepts that there may be a short-term momentum effect.

ESG integration

The Board believes that investment managers need to take proper account of ESG factors in assessing the fair value of any instrument. The thoughtful inclusion of such factors is particularly important if the manager intends to hold the position for a reasonably lengthy period or owns a significant stake in the company.

Consequently, when selecting investment managers that adopt a long-term investment horizon, the extent to which the manager integrates ESG into their research process and assessment of fair value, will be an important criterion.

Active ownership

The Board recognises that as opposed to becoming an active shareholder, the investment manager has the option to sell if their firm becomes concerned about the ESG characteristics of any investee company. However, where the manager is a large shareholder with the consequence that it will only be able to trade out of the position over an extended period, it should be a more active owner. Naturally, an investment manager whose investment thesis is part based on improving the ESG profile of the firm also needs to take an active owner role.

The Board is of the view that a key element of active ownership is effective engagement with the company's management. Accordingly, the Board places less emphasis on the voting record of the investment manager (although this is still important) and greater store on engagement that delivers positive results.

At this time the Board delegates the voting rights to its appointed investment managers, without issuing any voting guidelines. Nevertheless, the Fund's investment managers will be required to report at least annually on their engagement with investee companies and how they have voted on the company resolutions where at least 10% of the shareholders have voted against the matter. They will also be required to report on the extent to which their voting complies with King IV Principles , CRISA 1 and 2.

In addition, the Fund has exposure to a shareholder activist South African equity manager (Value Capital Partners).

Impacting investing

The Board believes that impact investing is an important social responsibility. As per the above, given the fiduciary responsibility of the Board it will only allocate capital to investment opportunities that offer the prospect of a fair risk adjusted return. Accordingly, the Fund will not compromise investment returns in pursuit of social returns. The Board is of the view that fair investment returns, and positive social returns, are not irreconcilable if the current inefficiency and multiple agents sometimes observed in such investments can be eliminated.

To date the Fund has invested in the debt of renewal energy programmes in South Africa. The manager will be required to report on the social impact of these investments annually.

ESG reporting

The Board will rely on its appointed investment managers to provide at least annual reporting on company engagement and voting. Specific reporting is required in respect of companies whose activities impact negatively on climate. In addition, where the investment has a clear social return, the manager is required to report on these social returns.

Furthermore, the Board requires the investment consultant to report on the efficacy of the Fund's investment managers in integrating ESG into their research process.

11.2 Voting policy

The Board is of the view that the Fund's voting rights are a very important contractual right to protect its interest.

At this time the Board has delegated its voting rights to the appointed investment managers who are expected to exercise these rights in the best long-term interest of the Fund. The Board will require its investment managers to report the following items in a periodic basis:

- How it has voted on the resolutions of all the companies in which it has invested on behalf of the Fund.

- Which annual general meetings or special shareholder meetings it has attended.

- The extent to which they subscribe and comply with the principles of the Code of Responsible Investing in South Africa (CRISA 1 and 2) and King IV governance principles.

Section 12: Governance principles

12.1 Conflicts of interest

The Board accepts that conflicts of interest, whether actual or potential, is part and parcel of any investment strategy and that such conflicts, if left unmanaged, represent a material risk to the success of the Fund's investment strategy.

The Board requires full and transparent disclosure of actual and potential conflicts of interest from all its service providers and from Board members. Any breach of this requirement of full disclosure will be regarded in a serious light and may lead to the termination of the service provider's appointment or the Board member being required to resign.

All service providers are required to receive their entire remuneration from the Fund and so may not receive any direct or indirect benefit or remuneration from any other service providers associated with the Fund. Although difficult to assess accurately the Board will evaluate what the key motivator of a service provider is – the Board is looking to appoint service providers where the staff are driven by intrinsic motivators like "doing the right thing for the client", "continuous improvement" rather than financial reward.

The Board will look to appoint Investment Committee members who have the ability to challenge the advice and investment strategies of their service providers. As a further risk mitigation factor the Fund will only invest in strategies which, after due consideration, the Board considers that it has a reasonable understanding of.

In addition, the Board and sub-committee members will comply with the conditions of Directive PF No. 8 of 2018 which deals with the prohibition of the acceptance of gratuitous benefits.

12.2 Manager fees

The Board has adopted the following principles in relation to investment manager fees:

- Costs are certain whereas manager out-performance is only an expectation. As such the Board aims to keep costs low but recognises that in certain circumstances it is worth paying a premium fee in order to access high skill and alignment of interest.

- The fee arrangement must reflect and promote a clear alignment between the interests of the Fund and that of the investment manager.

- The manager's fee can be structured either on a fixed fee or performance fee basis. Where a performance fee structure is used, it must be designed in such a way that option value of the performance fee to the manager is nil (or very close thereto). This would generally require the fee system to operate on a high water mark basis with the reward for out-performance measuring manager skill and not capital market returns.

- As a general guideline the manager's fee (including any performance fee) should allocate about 75% to 80% of the expected value added by the manager to the Fund (with the manager's share being 20% to 25%). There are circumstances in which a lower sharing ratio to the Fund may be appropriate but even in these circumstances the Fund would seek to benefit from at least 65% of the expected value added by the manager.

- All fees and costs charged by managers and or incurred in the management of portfolios (indirect fees and costs) must be fully and consistently disclosed by all managers.

12.3 Manager mandates

The Board will agree a mandate with each of the investment managers it appoints. The mandate will set out the performance target, measurement period and risk constraints for the manager and will also contain specific provisions to deal with potential conflict of interest situations. The various mandate conditions per asset class are set out in Annexure 8.

12.4 Use of derivatives

Derivative instruments may at no time be used for the purpose of speculation or to leverage or gear the assets within the portfolios.

The Board will require each of its investment managers to identify, measure and take steps to manage and mitigate, as appropriate, the exposure to and risks of derivative instruments, and the contribution of these to the overall risk profile of their mandate and at all times to comply with the provisions of Regulation 28 and the FSCA Conduct Standard 1 of 2023 in relation to use of derivative instruments.

12.5 Monitoring

The performance of the Fund's investment channels, and the underlying investment managers will be monitored on a quarterly basis. The manner in which the Fund's investments will be monitored is set out in Annexure 9.

The investment consultant is responsible for the compilation of the quarterly regulation 28 and SARB monitoring and submissions whilst the Administrator is responsible for the correct and timeous submission thereof.

The Board will obtain confirmation from its investment managers that at all times the manager will manage the Fund's assets in accordance with FSCA Conduct Standard 1 of 2023 applicable to the use of derivative instruments.

12.6 Registration of the Fund's assets and scrip lending

The Board is comfortable for the assets to be registered in the name of the Fund or to access investment via comingled funds (e.g. insurance policies or collective investment schemes). The use of comingled funds is however subject to the conditions set out in Annexure 10.

The Fund will not engage in scrip lending where the assets are registered in its name. The Board however recognises that where the investment is via a pooled vehicle, the investment manager may be allowed in terms of the founding documents to scrip lend – in this case scrip lending is permitted provided that the terms of such lending are disclosed to the Fund before the date of the investment manager's appointment and the manager warrants that its scrip lending programme complies with the relevant legislation.

12.7 Treating Customers Fairly

The Fund's investment strategy complies with the Treating Customers Fairly principles. Specifically, the Fund provides an appropriate range of options so that individual members can meet their investment needs in most instances. Furthermore, the Board focuses on keeping costs low and provides complete and transparent disclosure to the members regarding costs. There are no hidden fees. In addition, there are no lock-in clauses and any limits on member choice are only included to the extent that they are required for administrative purposes and to mitigate against anti-selection.

Section 13: Review of statement

In the normal course of events the Board will review the investment strategy annually or at shorter intervals where investment opportunities may also arise. The investment strategy must be reviewed within 3 months of any of the following events occurring:

- A change in exchange control regulations affecting retirement funds.
- A change in the tax basis affecting the investment strategy of the Fund.
- A change in the Pension Funds Act or the Long-Term Insurance Act that affects investments.
- A change in the economic policy regarding inflation targeting or the mandate of the South African Reserve Bank.
- An indication that the Fund will have significant cash flow requirements (particularly outflows).
- Any extreme market event in which case the Principal Officer may convene a special meeting of the Investment Committee.

Adopted on: 2 DECEMBER 2024

Prof Muthundine Sigwadi (Jan 14, 2025 15:36 GMT+2)

Chairperson: Board
Date: 2025-01-14

Principal Officer
Date: 2025-01-20

Mr Levi Orometswe Moleme (Jan 14, 2025 13:46 GMT+2)

Trustee
Date: 2025-01-14

I have reviewed the investment strategy of the Fund and am satisfied that it is appropriate in relation to the nature of the Fund's liabilities.

Valuator
Date:

Appendix A: Check list of compliance with legislative requirements

Compliance with Regulation 28 Principles

Clause	Requirement	Compliance	IPS /other reference
2(a)	Fund must comply with limits of Regulation 28	✓	Annexures 6 and 8
2(b)	Fund must have an IPS which is reviewed at least annually	✓	Section 13
2(c) (i)	Education of board members in relation to investments must be promoted	✓	Fund trustee training program
2(c) (ii)	Monitor compliance with Regulation 28	✓	Annexure 9.4
2(c) (iii)	In contracting Fund must consider the need to promote board based black economic empowerment	✓	Section 10.2, Fund's transformation policy
2(c) (iv)	Assets must be appropriate to liabilities	✓	Signing page and Annexure 12
2(c) (v)	Fund must do proper due diligence of processes, risk control and liquidity risk when appointing a third party manager	✓	Sections 10.1 and 10.2; Fund's DD process in selecting managers
2(c) (vi)	For foreign assets the due diligence should extend to an understanding of currency and country risk	✓	As per above
2(c) (vii)	Credit ratings may be considered in assessing risk, but the Fund's investment managers should do independent credit analysis	✓	As per above
2(c) (viii)	Board must understand how the risk profile of the Fund may change over time	✓	Annexure 9.2 plus quarterly performance report
2(c) (ix)	Sustainability and ESG factors must be considered before making an investment	✓	Sections 4 and 11 read with Annexure 8.2

Compliance with requirements of Regulation 37 – default investment strategy

Clause	Requirement	Compliance	IPS /other reference
37.1	The Fund must have a default investment strategy for DC members	✓	Section 5.2
37.2 (a)	The design of the default investment strategy must include (a) objective (b) underlying asset allocation (c) fee principles and (d) risk profile.	✓	Section 6 read with annexures
37.2 (b)	The composition of the assets and performance must be communicated to members	✓	Monthly fact sheet
37.2 (c)	Fees and charges must be reasonable and competitively priced	✓	Section 12.2 read with annexure 9.3
37.2 (d)	Fees and charges must be disclosed	✓	Monthly fact sheet
37.2 (e)	Passive and active strategies must be considered	✓	Section 9.1
37.2 (f)	No loyal bonus or other complex fee structure are permitted	✓	Section 12.3
37.2 (g)	Members must not be locked into the default portfolios	✓	Sections 5.3 and 12.6
37.2 (h)	Default strategy must be reviewed	✓	Done annually with IPS review

Compliance with requirements of Regulation 39 – guided annuity strategy

Clause	Requirement	Compliance	IPS / other reference
39.1 (b)	Provident Funds that allow a member to elect an annuity must have a guided annuity strategy	✓	Section 5.4
39.2 (a)	Guided annuity strategy must be appropriate and suitable for membership	✓	Guided strategy is a life annuity / members can opt out and elect a living annuity
39.2 (b)	Objectives, asset class composition and performance must be communicated to members	✓	Options at retirement guide and annual pension increase
39.2 (c)	Annuities have reasonable and competitive fees	✓	Section 12.3, fees much lower than insurer costs
39.2 (d)	Fees and charges and impact on benefits must be disclosed	✓	Retirement guide
39.2 (e)	Members must be given access to retirement benefit counselling	✓	Retirement guide, retirement seminar
39.2 (f)	Guided annuity strategy must be reviewed	✓	Done annually with IPS review
39.3 (a)	Permits the Fund to provide a living annuity as part of the guided annuity strategy	n/a	Fund provides the option of a living annuity, but it is not the guided annuity strategy
39.3 (b)	Sustainability of drawdowns must be monitored and communicated	✓	Fund limits drawdown on an age related basis; annual review of drawdown with living annuitant

Compliance with Guidance Note 1 of 2019 (PFA) – Sustainability of investments

Please note that the provisions of clauses 5 and 6 are advisory and not a statutory requirement

Clause	Requirement	Compliance	IPS / other reference
4.1 (a)	When IPS was approved and by whom	✓	Signature page
4.1 (b)	Frequency of the IPS reviewed	✓	Section 13
4.1 (c)	IPS must set-out policy in respect of ESG including how monitoring will be done	✓	Section 11.1
4.1 (d)	Active ownership policy	✓	Section 11.2
4.3	Investment manager mandates and reporting requirements should include provisions around ESG	✓	Section 11, read with annexure 8.2
5.1 (a)	Make a copy of IPS or an abridged version thereof <u>on request</u> and at no cost to any member and the participating employer	✓	
5.1 (b)	IPS should be available on the Fund's website	✓	
5.1 (c)	Annual inform members that the IPS is available on the website, noting material changes	✓	
6.3	Annual financial statements should include confirmation members that have requested a copy of the IPS have received such, material changes to the IPS should be noted, which of the Fund's asset comply with this guidance note and market value of such assets	✓	

King IV Principles – Supplement for Retirement Funds as it relates to investments

The principles below are embedded in the IPS.

Principle	Requirement	Compliance
1.3	The board should ensure that the retirement fund is a responsible corporate citizen	✓
2.1	The board should lead the value creation process by appreciating that strategy, risk and opportunity, performance and sustainable development are inseparable elements	✓
2.2	The board should ensure that reports and other disclosures enable stakeholders to make an informed assessment of the retirement fund and its ability to create value in a sustainable manner	✓